

Shades of the American Dream: Race, Class, Tax Policy and Homeownership Wealth

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Abstract

No one decides to purchase a home based upon whether they receive a tax deduction. Empirical data show that the tax subsidies for homeownership encourage prospective home buyers to purchase more expensive homes. Homeowners who purchase more expensive homes accumulate tax subsidized housing wealth. No prior study has examined whether all homeowners are encouraged to purchase more valuable homes regardless of their race or class. This Article provides such an analysis and shows that the tax subsidies for housing are increasing wealth disparities in this country.

Low income taxpayers, as well as black and latino middle and upper income taxpayers are least likely to purchase more valuable homes (and least likely to benefit from the other tax subsidies associated with housing). Middle and upper income white homeowners benefit the most from the wealth building aspects of the tax subsidies and from other housing tax benefits. This Article proposes four changes to current tax laws which if enacted would both minimize the race based housing wealth disparities and provide meaningful tax benefits to low income homeowners regardless of race, and middle and upper income black and latino homeowners.

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*A nation of homeowners is unconquerable,*¹

Franklin D. Roosevelt

I. Introduction

Homeownership is synonymous with the American dream.² The goal of homeownership is such a universally shared phenomenon that it is one of the few things upon which Republicans and Democrats can agree.³ Yet all the news is not positive.

Record home foreclosures associated with the subprime lending market, has brought into the public eye the obvious fact that not everyone benefits from homeownership.⁴ Low-income homeowners and homeowners of color face discrimination in the housing market. Federal tax policies which subsidize homeownership not only reinforce such marketplace discrimination but increase wealth disparities in this country.

1. See Eduardo Porter and Bikas Bajaj, *Rising Trouble With Mortgages Clouds Dream of Owning Home*, N.Y. TIMES, March 17, 2007, at A1.

2. See Douglas G. Baird, *Consumer Bankruptcy and Credit in the Wake of the 2005 Act: Technology, Information, and Bankruptcy*, 2007 U. Ill. L. Rev. 305, 307 (“Living in one’s own home is often touted as an integral part of the American Dream, and promoting homeownership is often an explicit government policy.”) (citations omitted); Allison D. Christians, *Breaking the Subsidy Cycle: A Proposal for Affordable Housing*, 32 COLUM. J.L. & SOC. PROBS. 131, 145 (1999) (“Homeownership has long been identified with the “American dream.” It is considered to be “a basic value in American society” and a “national good.”)(citations omitted); Michael S. Knoll, *Taxation, Negative Amortization and Affordable Mortgages*, 53 OHIO ST. L.J. 1341, 1378 (1992) (“Homeownership is a cherished part of the American dream.”).

3. See Michael Moss and Andrew Jacobs, *Blue Skies and Green Yards, All Lost to Red Ink*, N.Y. TIMES, April 11, 2004, at A1 (“Indeed, encouraging homeownership is one of the few issues the Clinton and Bush administrations pursued with equal ardor.”).

4. See e.g. Clifford Krauss, *Belatedly, Some States Move to Limit Damage From Subprime Lending*, N.Y. TIMES, Aug. 24, 2007, at C1 (“The Mortgage Bankers Association reports that 550,000 homeowners with subprime loans began a foreclosure process over the last year, and specialists say that the number could double in the next couple of years.”); Vikas Bajaj, *In the Current Foreclosure Crisis, Echoes of the Past*, N.Y. TIMES, Aug. 12, 2007, at 12 (“At the end of March, nearly 20 percent of loans to subprime borrowers -- those with weak credit history -- were past due or in foreclosure.”). Alexandra Marks and Ron Scherer, *As US Foreclosures Mount, States Step In*, CHRISTIAN SCIENCE MONITOR, Apr. 5, 2007 (“The stakes are high: As many as 130,000 homeowners - the most in 30 years - are going into foreclosure each month. Experts worry that entire neighborhoods will decline - similar to what happened in the 1960s and ’70s - as abandoned foreclosed homes cause property values to drop.”). Cf. Frank Alexander, *The Housing of America’s Families: Control, Exclusion and Privilege*, 54 EMORY L. J. 1231, 1232 (2005) (“Though homeownership rates may now be at sixty-eight percent, we also are witnessing the highest recorded rates of residential foreclosures, and the average family has less equity in their home than ever before.”).

Those policies must be changed.

Homeowners are allowed to deduct from their income their mortgage interest expenses⁵ as well as real property taxes⁶ in computing their tax liability,⁷ yet imputed rental income is excluded from income.⁸ When we sell our homes we have some (or all)⁹ of the gain excluded from our income and if any of the gain is taxed, it is taxed at the lower capital gains rate.¹⁰ If we sell our homes at a loss, however, that loss is not recognized.¹¹ Interestingly, however, the empirical data show that no one decides to purchase a home because of the mortgage interest deduction.¹²

5. I.R.C. § 163(h) (2007). (Generally personal interest cannot be deducted, however, there is an exception for “qualified residential real estate.” The interest can be on a mortgage (or mortgages) not to exceed \$1 million and a home equity loan not to exceed \$100,000.)

6. I.R.C. § 164(a)(1) (2007).

7. Recently Congress enacted to phase-out the limits on itemized deductions that previously faced middle-and upper-income taxpayers under I.R.C. § 68 (2007). *See* Reed Shuldiner and David Shakow, *Lessons From The Limitation on Itemized Deductions*, 93 TAX NOTES 673, 679 (2001) (“The most important change in the 2001 Act affection section 68 is obviously the phasedown and repeal of the provision. The 2001 Act reduces the section 68 limitation by one-third for 2006 and 2007 and two-thirds for 2008 and 2009. The act repeals sections 68 for 2010 and reinstates section 68 as currently enacted for 2011 and beyond.”)

8. *See e.g.* Joseph Bankman and Thomas Griffith, *Social Welfare and the Rate Structure: A New Look At Progressive Taxation*, 75 CALIF. L. REV. 1905,1909 n.10 (1987) (“The nontaxation of imputed rental income is without specific statutory or case authority but is nonetheless a fundamental feature of the present tax law. *See* 1 B. BITTKER, FEDERAL TAXATION OF INCOME, ESTATES AND GIFTS P5.3.3 (1981).”); Roberta F. Mann, *The (Not So) Little House on the Prairie: The Hidden Costs of the Home Mortgage Interest Deduction*, 32 ARIZ. ST. L. J. 1347, 1348-49 (2000) (“The Federal income tax system subsidizes the dream of home ownership through the home mortgage interest deduction, the property tax deduction, and the exclusion of imputed rental income from owner-occupied housing, as well as other forms of preferential treatment.”) (citations omitted)

9. I.R.C. § 121 (2007). (exclusion for gain up to \$500,000 for married couples filing a joint return and \$250,000 for everyone else) on sale of principal residence)

10. I.R.C. § 1(h) (2007). (reduced rate for capital gains)

11. *See* Treas. Reg. § 1.262-1(b)(4).

12. *See e.g.* Edward L. Galeser and Jesse M. Shapiro, *The Benefits of the Home Mortgage Interest Deduction*, 17 TAX POL’Y AND THE ECON., 37, 39 (2003) (“While the deduction appears to increase the amount spent on housing, it also appears to have almost no effect on the homeownership rate.”); William G. Gale, Jonathan Gruber, and Seth Stephens-Davidowitz, *Encouraging Homeownership Through the Tax Code*, 115 Tax Notes 1171, 1171 (June 18, 2007) (“Evidence suggests, however, that the mortgage interest deduction... does little if anything to encourage homeownership. Instead, it serves mainly to raise the price of housing and land and to encourage people who do buy homes to borrow more and to buy larger homes than they otherwise would.”); Mann, *supra* note 8, at 1384-85 (2000) (“Economists don’t agree on much, but they do agree on this: the interest deduction doesn’t do a thing for homeownership rates. If you eliminated the deduction tomorrow, America would have the same number of homeowners....”) (citation omitted).

The empirical data show that the mortgage interest deduction encourages homeowners to buy more expensive homes which will then lead to greater opportunities for accumulating tax subsidized housing wealth¹³ None of those studies however have been analyzed from a race and class perspective. This Article provides such an analysis.

Any homeowner who is unable to parlay the mortgage interest deduction into a more valuable home does not benefit from the wealth building aspects of the deduction. While prior articles have analyzed housing tax subsidies from a race¹⁴ and/or class¹⁵ perspective no prior article has analyzed whether federal tax policies are contributing to the racial wealth disparities in this country because they are encouraging only certain homeowners to purchase more valuable homes.

This Article shows that low income taxpayers regardless of race as well as middle and upper income black and latino taxpayers are unable to benefit from the wealth building aspects of housing tax subsidies while white middle and upper income taxpayers receive significant tax subsidized wealth benefits.¹⁶ Low income homeowners and middle and upper income black and latino taxpayers are similarly not benefiting from the tax subsidies for housing to the extent that their middle and upper income white counterparts are benefiting. Tax policies which are not benefiting all homeowners regardless of their race and/or class are exacerbating housing wealth disparities and must be changed.¹⁷

13. *Id.*

14. See e.g. Beverly I. Moran and William Whitford, *A Black Critique of the Internal Revenue Code*, 1996 Wisc. L. Rev. 751, 780 (describing racial impact of the mortgage interest deduction); Mann, *supra* note 8, at 1365-66 (describing racial impact of the mortgage interest deduction); Mylinh Uy, Note and Comment, *Tax and Race: The Impact on Asian Americans*, 11 ASIAN L.J. 117, 124-127 (2004) (describing racial impact of the mortgage interest deduction)

15. See e.g. Mann, *supra* note 8, at 1360-62 notes 67-90 and accompanying text (describing class effects of the mortgage interest deduction); Leo P. Martinez, "To Lay and Collect Taxes": *The Constitutional Case for Progressive Taxation*, 18 YALE L. & POL'Y REV. 111, 150 n. 280 (1999) ("regressive deductions, like the mortgage interest deduction, tend to make progressive rate structures less progressive.")

16. The Article tries wherever possible to provide data on all racial and ethnic groups. Alas, the studies cited herein generally provided information on black, latino, and white homeowners, (and sometimes only black and white homeowners) but rarely asian homeowners. As a result, the Article leaves largely unexplored the racial dynamics of asian homeowners. I hope in a future project to be able to examine in detail the issues facing asian homeowners and how they are impacted by housing tax subsidies.

17. Cf. Thomas M. Shapiro, *Race, Homeownership and Wealth*, 20 WASH. U. J.L. & POL'Y 53, 68 (2006) ("Just as home ownership creates wealth for both whites and blacks, it simultaneously widens the racial wealth gap under current conditions."); Kerwin Kofi Charles and Erik Hurst, *The Transition to Home Ownership and the Black-White Wealth Gap*, 84 REV.

Part II describes the tax benefits available for homeownership which are not available to renters. Part III provides demographic information about today's homeowners and renters. Whites and asians are more likely to be homeowners and blacks and latinos are more likely to be renters. Low-income homeowners are most likely to sell their homes at a loss and return to renting without receiving significant wealth from their homeownership. Middle and upper income blacks and latinos are most likely to receive subprime mortgages hindering their ability to accumulate wealth. Part III also demonstrates that the race of one's neighbors impacts the price of housing. When more than ten percent of blacks own homes in a neighborhood, the value of those homes depreciate by sixteen percent.¹⁸ As a result, appreciation in housing and therefore housing wealth accumulation is greater in predominantly white neighborhoods than in predominantly black neighborhoods.

Part IV provides a race and class critique of the tax subsidies for homeownership and makes two primary points. First, you can only benefit from the tax subsidies if you are a homeowner since rent is not deductible. The majority of whites and asians are homeowners and eligible to receive tax subsidies for housing. The majority of blacks and latinos are renters and ineligible to receive tax subsidies for housing. Second, you receive the maximum benefit from the tax subsidies if you are able to buy a more valuable home and accumulate housing equity. White middle and upper income homeowners are able to accumulate significant housing equity, while low income homeowners and middle and upper income blacks and latinos are not, albeit for very different reasons.

Low-income homeowners are unable to accumulate significant housing wealth for three primary reasons. First, their income is insufficient to enable them to purchase more valuable homes. Second, they are most likely after they sell their first home to return to renting, never receiving significant wealth from homeownership.¹⁹ Third, they are most likely to sell their homes at a loss – which is nondeductible under current tax law.²⁰

Middle and upper-income blacks and latinos are similarly unable to buy more valuable homes, but not because of income constraints. They are more likely to receive a subprime loan than whites with comparable

ECON. STAT. 281 (2002) (“Given the strong historical association between home ownership and wealth, it is likely that the racial wealth gap derives, at least partially from the large observed racial differences in housing wealth.”).

18. *See infra* Part II.

19. *See infra* Part III.

20. *Id.*

incomes which by definition will result in a lower approved mortgage amount than their white counterparts.²¹ In turn, the subprime loan results in middle and upper income black and latino homeowners paying more interest and less principal over a longer period of years resulting in less housing wealth accumulation. Second, blacks are more likely to purchase older homes which are less valuable again resulting in less housing wealth accumulation than their white counterparts.²² Third, blacks are more likely to live in majority minority neighborhoods and whenever a neighborhood is more than 10 percent black, property values decline.²³ Accordingly, low-

21. *Id.*

22. See R. Richard Banks, "Nondiscriminatory" Perpetuation of Racial Subordination, 76 B.U.L. REV. 669, 686 (1996) ("It is well established that the slower appreciation rate of property in black areas disadvantages black homeowners.") (citation omitted.); Francine D. Blau and John W. Graham, *Black-White Differences in Wealth and Asset Composition*, 105 Q.J. ECON. 321, 333 (1990); Charles and Hurst, *supra* note 17, at 288 ("Not only are blacks less likely to own homes than are whites, but, when they do own, the value of their homes is smaller at the means, at the medians, and with and without controls."); Lisa A. Keister, *Race and Wealth Inequality: The Impact of Racial Differences in Asset Ownership on the Distribution of Household Wealth*, 29 SOC. SCI. RES. 477, 479 (2000) ("Indeed there is considerable evidence that white families are more likely to own homes than black families, that the values of the homes owned by whites appreciate more rapidly than those of blacks...."); Mann, *supra* note 8, at 1365 n. 108 ("One study found that black couples own a disproportionately lower share of aggregate housing wealth, both because they are less likely to be homeowners and because they are more likely to own homes with low market values. The researchers found that race alone explained differences in the value of homes." citing James E. Long & Steven B. Caudill, *Racial Differences in Home Ownership and Housing Wealth, 1970-1986*, 30 ECON. INQUIRY 83, 95-97 (1992)); Myron Orfield, *Land Use and Housing Policies to Reduce Concentrated Poverty and Racial Segregation*, 33 FORDHAM URB. L.J. 877, 901 (2006) ("Moreover, studies have shown that Black homeowners, more than any others, are steered toward real estate that actually loses equity value.") (citation omitted); Shapiro, *supra* note 17, at 68 ("On average, homes owned by whites appreciate in value approximately \$ 28,000 more than those owned by blacks."); Lior Jacob Strahilevitz, *Exclusionary Amenities in Residential Communities*, 92 VA. L. REV. 437, 446 (2006) ("Real estate has historically appreciated much more quickly in all-white neighborhoods than in neighborhoods that have a ten percent African American population, and noticeably more quickly in ten percent African American neighborhoods than in twenty percent African American neighborhoods. Thus, relatively minor changes in the racial composition of a neighborhood can have enormous consequences for a home owning family's net worth, and may cause families to change residences more frequently than they would prefer.") (citations omitted).

23. Shapiro, *supra* note 17, at 68. ("Moreover, homes lose about 16% of their value when located in neighborhoods that are more than 10% black.") (citation omitted); Nancy A. Denton, *The Role of Residential Segregation in Promoting and Maintaining Inequality in Wealth and Property*, 34 IND. L. REV. 1199, 1207-1208 (2001). Professor Denton writes:

Though the work is not yet complete, our initial findings reveal that both blacks and whites are penalized for living in neighborhoods that are more heavily black.... units lose approximately sixteen percent of their value when neighborhood composition increases from less than ten percent black

income homeowners regardless of race, as well as middle and upper income blacks and latinos do not receive the wealth benefits from the tax subsidy that middle and upper-income whites receive. The tax subsidies which encourage middle and upper income whites to purchase more valuable homes are exacerbating the wealth disparities in this country.

Part V describes what housing tax policy would look like if it was designed to encourage housing wealth accumulation for all taxpayers regardless of their race and class by proposing four solutions. First, the mortgage interest and real property tax deductions would be converted into refundable credits. Second, losses on the sale of primary residences would become deductible for low income homeowners. Since currently this problem is faced mainly by low-income homeowners, only those households should receive the benefit of the loss deduction. Third, only allow the credits for “racially diverse” neighborhoods, namely those neighborhoods with more than 10 percent black homeowners, because those neighborhoods currently face market based race discrimination. The tax deduction would ameliorate the market premium currently paid to homeowners in homogeneous white neighborhoods. Fourth, to discourage race based discrimination in the mortgage lending industry, (and to help pay for the proposed credits and allowed losses) there should be a new tax on lenders who provide loans to middle and upper income black and latino homeowners at significantly higher interest rates than their loans to comparable white homeowners as well as lenders who in response to this tax seek only to provide loans to white homeowners. This Article concludes by noting that current federal tax policies which encourage homeownership both replicate the race and class bias that currently exists in the housing market and increase wealth disparities. Tax policy can and should do better.

to between ten percent and sixty percent black, and they lose forty-six percent of their value if the neighborhood's black population rises above sixty percent. These results vary significantly by region, following the same pattern as the declines in segregation discussed above. Western housing loses no more than 33% of its value when located in neighborhoods that are more than 10% black. By contrast, reductions in annual costs are as much as 40% in the South, 52% in the Midwest and 70% in the Northeast for dwellings located in neighborhoods that are more than 10% black. (citations omitted)

Abraham Bell and Gideon Parchomovsky, *The Integration Game*, 100 COLUM. L. REV. 1965, 1984 (2000) (One study “finds that prices of residential units drop by 16% when the percentage of blacks in a neighborhood changes from less than 10% to 10-60%.”) Perhaps we can call this an ironic twist on W.E.B. DuBois’ tenet of the “talented tenth.”

II. Tax Subsidies for Housing

A. Tax Deductions Do Not Impact The Decision to Purchase A Home.

Numerous articles have examined the tax benefits associated with housing.²⁴ From the beginning of the income tax in 1913, until the Tax Reform Act of 1986, all interest was deductible.²⁵ While the legislative history on the allowance of personal interest is sparse, in 1986 when Congress amended the Internal Revenue Code to continue to allow the mortgage interest deduction, while disallowing for example, a deduction for credit card interest payments, they cited encouraging homeownership as justification²⁶ notwithstanding the empirical data that shows the tax benefits do not encourage taxpayers to purchase homes, but encourage taxpayers to purchase bigger, more expensive homes.²⁷ None of the studies which have examined the issue have considered whether all homeowners regardless of their race or class are equally likely to purchase more expensive homes.

Generally whether homeowners will purchase more expensive homes is largely a function of supply and demand. The more inelastic the supply, the more the mortgage interest deduction will result in a price increase. If housing stock is fixed, the mortgage interest deduction increases the price

24. See e.g. Mann, *supra* note 8, at 1361 (“The home mortgage interest deduction thus constitutes an upside-down subsidy – the greater the need, the smaller the subsidy.”); William T. Mathias, *Curtailing the Economic Distortions of the Mortgage Interest Deduction*, 30 U. MICH. J. L. REF. 43 (1996) (describing tax benefits of the mortgage interest deduction); Mark Andrew Snider, *The Suburban Advantage: Are the Tax Benefits of Homeownership Defensible?*, 32 N. KY. L. REV. 157 (2005) (describing tax benefits of the mortgage interest deduction for suburban homeowners as opposed to urban homeowners).

25. Mathias, *supra* note 24, at 45 (“From the inception of the income tax in 1913 until the passage of the Tax Reform Act of 1986...the general rule was that a taxpayer could deduct all personal interest payments, including interest payments on home mortgages.”). See also Joseph A. Snoe, *My Home, My Debt: Remodeling the Home Mortgage Interest Deduction*, 80 KY. L. J. 431,436-438 (1992) (describing the Tax Reform Act changes to interest deductions).

26. Mathias, *supra* note 24, at 73 (“When Congress fashioned the current rules for the mortgage interest deduction, its stated goal was to foster home ownership.”) (citation omitted).

27. See *supra* note 12 and accompanying text.

of housing by 10 percent.²⁸ The price increase will be greatest in areas with high tax rates and high housing prices.²⁹

Time-series studies in the United States show that the mortgage interest deduction does not influence the decision to purchase.³⁰ The value of the deduction increases with the inflation rate and tax rate increases.³¹ Even though over the last 40 years there has been significant fluctuation in the inflation rate and tax rates, the homeownership rate has moved very little.³²

Further support for the fact that the mortgage interest deduction does not encourage the decision to purchase a home can be found by comparing American homeownership rates (67 percent) with countries that do not have a mortgage interest deduction.³³

Australia has a slightly higher homeownership rate (70 percent) but does not permit a mortgage interest deduction and Canada has the same (67 percent) homeownership rate but does not allow a mortgage interest deduction.³⁴ Nevertheless homeownership is a tax favored investment in America.

B. Tax Rules.

Interest paid on a mortgage secured by a personal residence is deductible,³⁵ however, rent is not deductible.³⁶ Imputed rental income is excluded from income,³⁷ yet homeowners are allowed to deduct from their

28. See Gale et al, *supra* note 12, at 1179 (One study using a “fixed stock of housing (completely inelastic supply) ...estimate[s] that the [mortgage interest deduction] increases the price of housing by 10 percent. The increases are greatest in areas with high tax rates and house prices.”)

29. *Id.* At 1180 (“The increases are greatest in areas with high tax rates and house prices.”)

30. *Id.*

31. *Id.*

32. *Id.* (“Despite substantial variation in the values of inflation and itemization – and thus the [mortgage interest deduction] – over the past 40 years, the homeownership rate has barely budged....”)

33. *Id.* at 1182.

34. *Id.*

35. I.R.C. §163(h) (2007).

36. See Treas. Reg. §1.262-3 (“Expenses of maintaining a household, including amounts paid for rent,...are not deductible.”)

37. See e.g. Joseph Bankman and Thomas Griffith, *Social Welfare and the Rate Structure: A New Look At Progressive Taxation*, 75 Calif. L. Rev. 1905,1909 n.10 (1987) (“The nontaxation of imputed rental income is without specific statutory or case authority but is

adjusted gross income their mortgage interest expenses³⁸ as well as real property taxes³⁹ in computing their tax liability.⁴⁰ In addition, when we sell our homes we have some (or all)⁴¹ of the gain excluded from our income and if any of the gain is taxed, it is taxed at the lower capital gains rate.⁴² If a taxpayer sells her home at a loss, it is however, not deductible.⁴³ It is estimated that for fiscal year 2007, the estimated loss in tax revenue from those tax advantages (not counting the exclusion for imputed rent) exceed \$125 billion.⁴⁴ One study of imputed rent placed the value of the exclusion in 2004 at \$900 billion.⁴⁵

nonetheless a fundamental feature of the present tax law. *See* 1 B. BITTKER, FEDERAL TAXATION OF INCOME, ESTATES AND GIFTS P5.3.3 (1981.); Mann, *supra* note 8, at 1348-9 (“The Federal income tax system subsidizes the dream of home ownership through the home mortgage interest deduction, the property tax deduction, and the exclusion of imputed rental income from owner-occupied housing, as well as other forms of preferential treatment.”) (citations omitted)

38. I.R.C. § 163(h) (2007). (Generally personal interest cannot be deducted, however, there is an exception for “qualified residential real estate.” The interest can be on a mortgage (or mortgages) not to exceed \$1 million and a home equity loan not to exceed \$100,000.) In addition for taxpayers with incomes no greater than \$100,000, they are allowed to deduct premiums paid or accrued for qualified mortgage insurance for mortgage insurance contracts entered into on or after January 1, 2007 and amounts paid or accrued before January 1, 2008. I.R.C. § 163(h)(3)(E)(2007). For households with income greater than \$100,000, the amount of the deduction phases out.

39. I.R.C. § 164(a)(1) (2007).

40. Recently Congress enacted to phase-out the limits on itemized deductions that previously faced middle-and upper-income taxpayers under I.R.C. § 68 (2007). *See* Reed Shuldiner and David Shakow, *Lessons From The Limitation on Itemized Deductions*, 93 TAX NOTES 673, 679 (2001) (“The most important change in the 2001 Act affection section 68 is obviously the phasedown and repeal of the provision. The 2001 Act reduces the section 68 limitation by one-third for 2006 and 2007 and two-thirds for 2008 and 2009. The act repeals sections 68 for 2010 and reinstates section 68 as currently enacted for 2011 and beyond.”) In addition, although the mortgage interest deduction and real property tax deduction are itemized deductions, they are not subject to the 2 percent floor that most other itemized deductions are subject to. I.R.C. § 67 (2007).

41. I.R.C. § 121 (2007). (exclusion for gain up to \$500,000 for married couples filing a joint return and \$250,000 for everyone else) on sale of principal residence)

42. I.R.C. § 1221 provides that a personal residence is a capital asset. I.R.C. § 1222 provides that gain on the sale or exchange of a capital asset is capital gain. I.R.C. § 1(h) (2007). (reduced rate for capital gains)

43. I.R.C. § 165(c)(3) (2007); Treas. Reg. § 1.165-9.

44. STAFF OF THE JOINT COMM. ON TAXATION, 109TH CONG., ESTIMATES OF FEDERAL TAX EXPENDITURES FOR FISCAL YEARS 2005–2009, at 33 (Comm. Print 2005). (Author’s calculations: \$87.7 billion (mortgage interest); \$13.4 billion (real property taxes); and \$24.6 billion (exclusion of gain on sale of residence) for a total of \$125.7 billion.

45. *See* Gale et al, *supra* note 12, at 1174 n.5 (“The gross imputed rental value of owner-occupied housing was about \$900 billion in 2004 in the National Income and Product Accounts

C. *Tax Beneficiaries.*

Because the tax structure is a progressive rate structure, deductions are more valuable, the higher your taxable income.⁴⁶ For example a taxpayer in the 35 percent marginal tax bracket, saves 35 cents for every dollar of mortgage interest deduction. Her after tax costs of a \$1 mortgage payment would be 65 cents. On the other hand a taxpayer in the 15 percent marginal tax bracket, saves 15 cents for every dollar of mortgage interest deduction. Her after tax costs of a \$1 mortgage payment would be 85 cents. As income rises, homeownership rates increase.⁴⁷ Table 2.1 below provides a more complete picture.

TABLE 2.1⁴⁸
HOMEOWNERSHIP RATES BY ADJUSTED GROSS INCOME,
2003

Income Range	All Households
< \$5,000	48.9%
\$5-\$9,999	39.4
\$10-14,999	46.7
\$15-19,999	47.0
\$20-24,999	49.5
\$25-29,999	43.5
\$30-34,999	54.2
\$35-39,999	55.9
\$40-49,999	61.2
\$50-59,999	69.5
\$60-69,999	75.1
\$70-79,999	79.0

(Bureau of Economic Analysis 2005, Table 7.12).”)

46. See e.g. James R. Follain and David C. Ling, *The Federal Tax Subsidy to Housing and the Reduced Value of the Mortgage Interest Deduction*, 44 National Tax Journal, 147, 157 (2003) (“The distribution of the subsidy is highly skewed toward high income households. Those in the top three income classes, about 12 percent of the household population, receive about 54 percent of the subsidy to owner-occupants.”)

47. Gale, et al *supra* note 12, at 1172.

48. *Id.* at 1174.

\$80-99,999	85.0
\$100-119,999	88.7
> \$119,999	92.1

Table 2.1 shows that as income increases, homeownership rates increase. Once income reaches \$30,000, the majority of all households are homeowners. When income reaches \$80,000, the eighty-five percent of all households are homeowners and once income reaches \$120,000, ninety-two percent of all households are homeowners. Given that tax deductions benefit taxpayers with the highest marginal rates, high income households, which are most likely to be homeowners, are also the most likely to benefit from the tax subsidy.

Not everyone who owns a home, however, benefits from the tax deductions for homeownership. Only taxpayers who itemize their deductions are eligible to receive the mortgage interest and real property tax deductions and *two-thirds of taxpayers don't itemize*.⁴⁹ As a result, those eligible to receive housing tax benefits are more likely to be middle and

49. Nicolas P. Retsinas and Eric S. Belsky, Examining the Unexamined Goal, in *Low-Income Homeownership: Examining the Unexamined Goal 8* (Nicolas P. Retsinas & Eric S. Belsky eds., 2002) (Low-income homeowners “do not benefit from the deduction of mortgage interest payments and real estate taxes ... [because] the mortgages and property taxes of low-income [home] owners are often too small to make it pay to itemize their deductions, so they forgo itemizing them in favor of taking the standard deduction.”); Edward P. Lazear and James Poterba, *Reforming Taxes to Promote Economic Growth*, 110 TAX NOTES 387 (2006) (“Many homeowners who do not currently itemize their deductions will receive tax relief under [reform proposals].”); William G. Gale and Leonard E. Burman, A Preliminary Evaluation of the Tax Reform Panel’s Report, 109 Tax Notes 1349, 1354 (2005) Authors Gale and Burman provide:

Many middle-income homeowners do not itemize deductions, and even those who do itemize may receive less benefit because their itemized deductions scarcely exceed the standard deduction.” 1354 (citing the following example: For example, suppose a family donates \$ 1,000 to charity, pays \$ 3,000 in state and local taxes, and pays \$ 7,000 in mortgage interest. Because the family’s total itemized deductions of \$ 11,000 exceed the standard deduction of \$ 10,300, it would itemize, but owning the home reduces taxable income only by \$ 700 (\$ 11,000 minus the \$ 10,300 standard deduction that they could claim if they did not own a home). At a 15 percent marginal rate, the subsidy will amount to 1.5 percent of interest paid. By comparison, a taxpayer in the 35 percent bracket who would itemize even if he did not own a home (for example, because of state and local taxes) would receive a subsidy equal to 35 percent of interest paid, or more than 20 times as much as the moderate-income family.

But see Evelyn Brody, *Charities in Tax Reform, Threats to Subsidies Overt and Covert*, 66 TENN. L. REV. 687,716 (1999) (“In addition, those taxpayers most likely to itemize their personal deductions are homeowners who claim home mortgage interest expenses and property taxes, or those living in areas that adopt high state and local income taxes, namely, the more wealthy.”) (citation omitted)

upper-income homeowners.⁵⁰

Taxpayers who take the standard deduction on their tax returns reap no benefit from their mortgage interest payments, as the standard deduction is available for *all* taxpayers. Since the Tax Reform Act of 1986,⁵¹ low-income taxpayers are less likely to receive those benefits because they are less likely to itemize their deductions, but take the standard deduction because it is a larger amount than their deductions and may not benefit from their mortgage interest payments.⁵² New homeowners are generally in low or middle income households that don't itemize.⁵³ On the other hand middle and upper-income taxpayers may have their property tax deduction limited or eliminated by the alternative minimum tax⁵⁴ and be subject to the limitation on itemized deductions for higher-income households.⁵⁵

50. My previous scholarship has shown that certain provisions of the Internal Revenue Code disadvantages blacks, latinos, asians, and low-income taxpayers. *See e.g.* Dorothy A. Brown, *Race and Class Matters in Tax Policy*, 107 COLUM. L. REV. 790 (2007) (discussing discriminatory treatment received by low-income taxpayers regardless of race); Dorothy A. Brown, *The Tax Treatment of Children: Separate But Unequal*, 54 EMORY L. J. 755 (2005) (comparing the earned income tax credit and the child tax credit and showing how middle class white children receive tax benefits and low income children of all races do not)[hereinafter *Tax Treatment*]; Dorothy A. Brown, *Race, Class, and Gender Essentialism in Tax Literature: The Joint Return*, 54 WASH. & LEE L. REV. 1469 (1997) (showing that the marriage penalty disadvantages blacks and the marriage bonus advantages whites – except for white married couples earning \$60,000 - \$90,000 who are the most likely to pay the marriage penalty); Dorothy A. Brown, *Pensions, Risk and Race*, 61 WASH. & LEE L. REV. 1501 (2004)[hereinafter *Pensions*] (showing how blacks, latinos, and asians are less likely to participate in their employer provided pension plan and receive the tax benefits) [hereinafter *Pensions*]; Dorothy A. Brown, *Pensions and Risk Aversion: The Influence of Race, Ethnicity, and Class on Investor Behavior*, 11 LEWIS & CLARK L. REV. 385 (2007) (showing how blacks and latinos who participate in their defined contribution pension plans are significantly less likely to invest in the stock market than whites and as a result will retire with lower account balances at retirement.) [hereinafter *Risk Aversion*].

51. Pub. L. No. 99-514, 100 Stat. 2085.

52. James R. Follain, David C. Ling, and Gary A. McGill, *The Preferential Income Tax Treatment of Owner-Occupied Housing: Who Really Benefits?*, 4 HOUSING POLICY DEBATE 1, 21 (1993)(“[T]he mortgage interest deduction [is] worthless, or nearly so, for many low-and moderate-income households....”). *Cf* Gale, et al, *supra* note 12, at 1171 (“Most tax return filers, especially those with low or moderate incomes, do not itemize their deductions and therefore are not in a position to take advantage of the deduction if they were to buy a home.”)

53. Gale, et al, *supra* note 12, at 1179.

54. *See e.g.* Stewart E. Sterk and Mitchell L. Engler, *Property Tax Reassessment: Who Needs It?*, 81 NOTRE DAME L. REV. 1037, 1056 fn. 80 (2006) (“[T]he federal alternative minimum tax (AMT), which disallows the property tax deduction in certain cases.”)

55. *See* Reed Shuldiner and David Shakow, *Lessons From The Limitation on Itemized Deductions*, 93 TAX NOTES 673, 679 (2001) (“The most important change in the 2001 Act affection section 68 is obviously the phasedown and repeal of the provision. The 2001 Act reduces the section 68 limitation by one-third for 2006 and 2007 and two-thirds for 2008 and

Currently, only 54 percent of taxpayers who pay interest on their mortgages receive a tax benefit.⁵⁶ The Table below shows the percentage of homeowners who pay mortgage interest and receive a tax benefit by household adjusted gross income.⁵⁷

TABLE 2.2⁵⁸
 PERCENT OF HOMEOWNERS WHO RECEIVE A TAX
 BENEFIT FROM THE MORTGAGE INTEREST DEDUCTION BY
 ADJUSTED GROSS INCOME

Income Range	Percent
All	54%
0-\$15,000	2
\$15-30,000	16
\$30-40,000	34
\$40-50,000	49
\$50-60,000	58
\$60-75,000	71
\$75-100,000	90
\$100-200,000	97
\$200-500,000	99
\$500-1 million	98
> \$1 million	97

2009. The act repeals sections 68 for 2010 and reinstates section 68 as currently enacted for 2011 and beyond..”)

56. President’s Advisory Panel on Federal Tax Reform, *Simple Fair and Pro-Growth: Proposals to Fix America’s Tax System*, Final Report 134 (Nov. 2005) available at <http://www.taxreformpanel.gov/final-report/> (hereinafter “President’s Report”). One reason why taxpayers don’t receive a tax benefit from their mortgage interest payments is that they don’t itemize their deductions, but take the standard deduction, which in their circumstances would be greater. See I.R.C. §63 (2007)

57. Adjusted gross income is defined as gross income less certain deductions. I.R.C. §62 (2007).

58. President’s Report, *supra* note 56, at 134.

Table 2.2 shows that less than 20 percent of taxpayers earning less than \$30,000 (and only 2 percent of taxpayers earning less than \$15,000) receive a tax benefit from their mortgage interest payments. At income levels up to \$50,000 less than half of taxpayers receive a tax benefit from their mortgage interest payments. Put another way, the vast majority of homeowners earning \$50,000 or less do not receive tax benefits from their mortgage interest payments.

Table 2.2 shows that when adjusted gross income reaches \$75,000, however, 90 percent of taxpayers receive the tax benefit of their mortgage interest payments.⁵⁹ Once adjusted gross income reaches \$100,000, at least 97 percent of taxpayers receive a tax benefit from their mortgage interest payments. So taxpayers with adjusted gross incomes of \$100,000 as well as taxpayers with adjusted gross incomes in excess of \$1 million have the same percentage receiving tax benefits from their mortgage interest payments, namely 97 percent.

D. Summary.

In summary, the tax subsidy causes an over-investment in housing. People do not decide to buy a house because of the tax benefits, but they do decide to buy more expensive houses than they otherwise would because of the tax benefits.⁶⁰ In other words, the tax benefit encourages people to buy more expensive homes, but doesn't influence the initial decision of whether or not to buy. Middle and upper income taxpayers are most likely to be homeowners and most likely to take advantage of the tax deductions. The greatest benefit flows to those paying the highest marginal rates. Gains on the sales of personal residences are taxed at the lower preferential rate for capital gains, while losses are not deductible. Two-thirds of taxpayers don't itemize their deductions and if they're homeowners, do not receive the benefit of the deductions.

The tax subsidy benefits higher income taxpayers the most for two reasons. First, higher income taxpayers are the most likely to be able to purchase more expensive homes. Second, deductions are more valuable to those paying the highest marginal tax rates. Higher income taxpayers are

59. Cf. Steven Bourassa and William Grigsby, *Income Tax Concessions for Owner-Occupied Housing*, 11 Housing Policy Debate 531 (2000) ("Fully 90 percent of the benefit goes to homeowners with incomes over \$50,000 a year because most low-and moderate-income homeowners find that taking the standard deduction is more advantageous than itemizing."), available at: http://www.fanniemaefoundation.org/programs/hpd/pdf/hpd_1103_bourassa.pdf

60. *Id.*

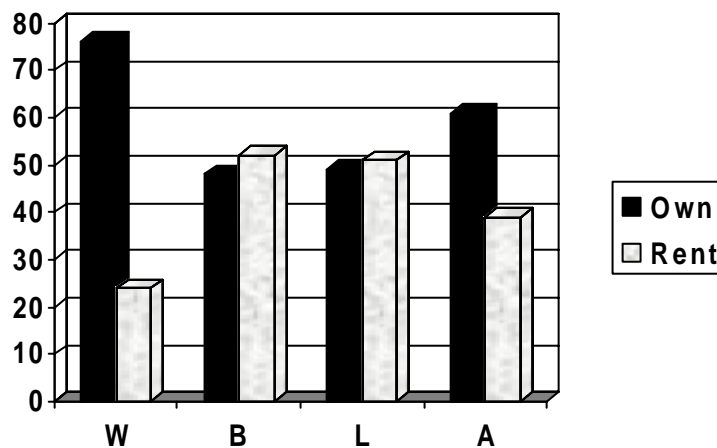
probably the most likely to become homeowners regardless of the tax benefits received and therefore the least in need of the tax subsidy. Finally, low income homeowners are the least likely to benefit from the tax subsidy because they are least likely to itemize their deductions.

III. Homeownership: A Race and Class Analysis

A. Today's Renters

In order to be eligible to receive housing subsidies for homeowners, one would have to become a homeowner. This section begins by looking at renters to consider those ineligible for the American Dream of homeownership.

Chart 3.1
Percentage Owner/Renter⁶¹



61. See U.S. Census Bureau, Series No. H-150-05, American Housing Survey for the United States: 2005, at 42, tbl. 2-1 (2006) available at <http://www.census.gov/prod/2006pubs/h150-05.pdf>. The categories are: (i) white, non-hispanic; (ii) black non-hispanic; (iii) hispanic of any race; and (iv) asian alone.

This Chart shows that the majority of whites (76 percent) and asians (61 percent) are homeowners, while the majority of blacks (52 percent) and latinos (51 percent) are renters. Renters have significantly less wealth than homeowners.⁶²

B. Today's Homeowners

Since World War II, homeownership has created a vibrant middle class.⁶³ The twenty-first century has seen homeownership reach an all time high with 69 percent of Americans owning their own home.⁶⁴ Homeowners can build up equity over time through appreciation⁶⁵ and receive significant tax subsidies along the way.

62. See Rakesh Kochhar, *The Wealth of Latino Households: 1996 to 2002*, PEW LATINO CENTER 20 (Oct. 18, 2004) (“The median net worth of non-Hispanic homeowners in 2002 was \$129,778. In contrast, the median net worth of non-Hispanic renters and others was only \$1,526, or just over 1 percent of the wealth of homeowners.... In 2002, the net worth of Hispanic renters and others was only \$762.... Hispanic homeowners had a net worth of \$62,839....”) (citations omitted).

63. See e.g. Note, Adam Gordon, *The Creation of Homeownership: How New Deal Changes in Banking Regulation Simultaneously Made Homeownership Accessible to Whites and Out of Reach for Blacks*, 115 YALE L.J. 186, 188 (2005) (“Through New Deal reforms, homeownership became the primary mechanism that middle-class Americans use to build assets. Today, 60% of the total assets of middle-class Americans are held in owner-occupied homes.”) (citations omitted); Shapiro, *supra* note 17, at 59 (“America has a high homeownership rate, with 69% of Americans owning homes. A series of federal policies that started in the 1930s made this high homeownership rate and subsequent middle-class wealth accumulation possible by creating a government-sponsored market.”) (citations omitted); Elizabeth Warren, *The Growing Threat to Middle Class Families*, 69 BROOKLYN L. REV. 401, 406 (2004) (“And if homeownership is the emblem of achieving middle class respectability, then two-thirds qualify as middle class.”) (citations omitted); Joan Williams, *The Rhetoric of Property*, 83 IOWA L. REV. 277, 328 (1998) (“During the post-World War II building boom, European countries generally built apartments, while the U.S. was transformed from a nation of renters to a nation of homeowners by massive tax subsidies to homeowners as well as the restructuring of home financing by FHA and VA mortgages.”) (citations omitted).

64. See Nicholas P. Retsinas, *The Endangered Land of Renter-World*, BOSTON GLOBE, May 5, 2006, at A19 (“Today 69 percent of households own a home an all-time high.”)

65. Elizabeth S. Anderson, *Integration, Affirmative Action, and Strict Scrutiny*, 77 N.Y.U.L. Rev. 1195, 1203 (2002) (“The middle class invests the largest share of its wealth in housing equity, which amounts to forty-three percent of white assets and sixty-three percent of black assets. Because blacks are confined to less-desired neighborhoods, on average the value of their housing grows less than that of whites. Consequently, blacks attain a substantially lower average rate of return on their housing investment than do whites.”)(citation omitted); Shapiro, *supra* note 17, at 68. (“Just as home ownership creates wealth for both whites and blacks, it simultaneously widens the racial wealth gap under current conditions.”).

Unlike the post-World War II housing boom,⁶⁶ this recent homeownership boom included low income Americans and Americans of color. Under President Clinton's administration, the increase in homeownership by people of color went from 42 percent to 48 percent.⁶⁷ Since 2002, the Bush Administration touts a net increase of "nearly 3 million minority homeowners."⁶⁸ Financial industry executives have launched a "with ownership, wealth" initiative to encourage homeownership among minorities.⁶⁹ Low-income homeownership rates increased as well. Between 1993 and 2000, the number of low-income homeowners grew by 79 percent.⁷⁰ Even though progress has been made, homeownership rates still differ by race and/or ethnicity, and class. A number of studies have documented racial differences in homeownership.⁷¹

As Chart 3.1 showed, whites are most likely to own their own homes (76 percent) followed by Asians (61 percent), blacks (48 percent) and latinos (49 percent).⁷² Race matters when it comes to being a homeowner.

66. See IRA KATZNELSON, *WHEN AFFIRMATIVE ACTION WAS WHITE* 57-80 (2005) (describing governmental housing benefits that excluded blacks post WWII from purchasing homes.); Daria Roithmayer, *Locked in Segregation*, 12 VA. J. SOC. POL'Y & L. 197 (2004)

67. See Moss and Jacobs, *supra* note 3 ("Indeed, encouraging homeownership is one of the few issues the Clinton and Bush administrations pursued with equal ardor.")

68. See US Fed News, *HUD Secretary Jackson Speaks on 'Revitalization of Uptown'*, Aug. 7, 2007 ("The President has also set a goal of 5.5 million new minority homeowners by decade's end. We're well on our way. Since 2002, there has been a net increase of nearly 3 million minority homeowners. A great success story.") See also Gary Martin, *Bush Makes a Push to Boost Minority Homeowners ; Blacks Lag in Buying*, L.A. TIMES, Oct. 16, 2002 ("Bush took time out of his busy tour of Republican fund-raisers and campaign appearances to attend a White House-sponsored Conference on Minority Homeownership here.")

69. See Wayne Washington, *Bridging the American Dream Gap: Blacks in Congress Nudge Lenders for Minority Buyers*; BOSTON GLOBE, Apr. 4, 2001, at A13 ("Financial industry officials and members of the caucus announced plans yesterday to address some of those problems. They have launched an initiative, "With Ownership, Wealth," that combines credit counseling with assistance for down payment and closing costs. Many mortgage lenders, including Wells Fargo Home Mortgage and Chase Manhattan Mortgage, will participate.")

70. See Anne B. Shlay, *Low-Income Homeownership: American Dream or Delusion?*, 43 URB. STUD. 511, 516 (2006).

71. See EMMA COLEMAN JORDAN and ANGELA P. HARRIS, *ECONOMIC JUSTICE: RACE, GENDER, IDENTITY AND ECONOMICS* 473-501 (2005) (describes wealth inequality in America); Keister, *supra* note 22, at 479 ("A number of studies have documented black-white differences in asset ownership, particularly homeownership.") (citations omitted); Spencer Overton, *But Some Are More Equal: Race, Exclusion, and Campaign Finance*, 80 TEX. L. REV. 987, 1004-1012 (2002) (discussing racial differences in homeownership).

72. See Martin, *supra* note 68, ("The homeownership rate for Anglos is 74.3 percent, compared to 48 percent for African Americans and 47.6 percent for Latinos. Some 53.7 percent

Being white makes you significantly more likely to own a home than if you are asian, black or Latino. (Although we will see later that low-income whites do not benefit to the extent of their middle-and upper-income counterparts.)

My earlier scholarship has documented how most blacks prefer to invest in real estate, while most whites prefer to invest in the stock market.⁷³ One would expect therefore to see a higher percentage of blacks as homeowners than whites. Barriers to entry are the primary reason we don't see greater rates of black homeownership. Chart 3.1 also raises the question of why we don't see homeownership rates among asians in even higher percentages than currently exist, given asian median income is higher than white median income.⁷⁴ Consider Table 3.1 which examined homeownership rates for immigrants and native born Asians and found vast differences between native born Asians and immigrants in their rates of homeownership.⁷⁵

TABLE 3.1⁷⁶
HOMEOWNERSHIP RATES FOR IMMIGRANTS AND NATIVE-
BORN ASIANS

of Asian Americans and other races owned their own homes, the Census data revealed.”); Kochhar, *supra* note 62, at 2 (“The percentage of White households who owned homes in 2002 was 74.3 percent. The homeownership rates for Latino and Black households were 47.3 percent and 47.7 percent respectively.”).

73. Brown, *Pensions*, *supra* note 50, at 1536 (“Black investors think that real estate is a better place to invest their money than either stocks or bonds.”). See also Anthony D. Plath and Thomas H. Stevenson, *Financial Services and the African-American Market: What Every Financial Planner Should Know*, 94 FINANCIAL SERVICES REVIEW 343, 357 (2000) (When compared with white households, black households “demonstrate a distinct preference for safety and security in their investment preferences, favoring life insurance and real estate assets over corporate debt and equity securities across all levels of household income and educational attainment.”)

74. See e.g. N. Edward Coulson, *Why Are Hispanic-and Asian-American Homeownership Rates So Low?: Immigration and Other Factors*, 45 J. URB. ECON. 209, 215 (1999) (“[T]he average Hispanic income is very slightly higher than the average Black income, yet this does not translate into even slightly higher ownership rates. Similarly, average Asian income is above average White income which is not consistent with their low ownership tendency.”)

75. Christopher E. Herbert, Donald R. Haurin, Stuart S. Rosenthal, and Mark Duda, *Homeownership Gaps Among Low-Income and Minority Borrowers and Neighborhoods* 126 (March 2005) (available at <http://www.huduser.org/Publications/pdf/HomeownershipGapsAmongLow-IncomeAndMinority.pdf>)

76. *Id.* (Source: 1996-1999 Current Population Survey)

Racial Group	All Households	Immigrants	Native Born
Japanese	63%	40%	82%
Mainland Chinese	55	53	68
South Asians ⁷⁷	43	44	27
'Dragons' ⁷⁸	39	39	29
Other Asians	57	56	61

Three observations are apparent from Table 3.1 – two of which are intra-racial and one is inter-racial. First, for Japanese, Mainland Chinese, and Other Asians, native borns have a higher homeownership rate than immigrants. Second, South Asians and 'Dragons' have a higher homeownership rate for immigrants than native borns. Third, when you compare the data from Table 3.1 with the data from Chart 3.1, you see that native born Japanese have a higher homeownership percentage (82) than whites (76).

Homeownership disparities by race and ethnicity are not solely attributable to differences in income. Even at high income levels, a smaller percentage of blacks and latinos are homeowners than whites. In 2005, for every income level, black homeownership rates were less than the overall homeownership rates by income.⁷⁹ As income increased, however, the disparities narrowed. For households with incomes of \$120,000 or greater, the gap was 4.8 percentage points, but for households with incomes of less than \$5,000, the gap was 17 percentage points.⁸⁰ That data is consistent with the results of another study based on 2003 homeownership rates.

77. South Asians include those from India, Pakistan, and Bangladesh. *Id.*

78. 'Dragons' include those from Korea, Singapore, Taiwan, and Hong Kong. *Id.*

79. Kenya Covington and Rodney Harrell, *From Renting to Homeownership: Using Tax Incentives to Encourage Homeownership Among Renters*, 44 HARV. J. ON LEGIS. 97, 101 (2007) ("The homeownership gap between whites and blacks is not solely attributable to racial disparities in income. In 2005, at every income level, homeownership rates for black households were lower than the overall rates for U.S. households with equivalent incomes.") (citation omitted)

80. *Id.* ("At the highest income levels, the gap was significantly narrower; for example, the gap was 17.1 percentage points for households with annual incomes of less than \$ 5000, but only 0.7 percentage points for households with incomes between \$ 100,000 and \$ 119,999, and 4.8 percentage points for households with annual incomes of \$ 120,000 or more.") (citation omitted)

TABLE 3.2⁸¹
 HOMEOWNERSHIP RATES BY RACE/ETHNICITY AND
 INCOME, 2003

Income Range	Non-Hispanic White	Non-Hispanic Black	Hispanic
< \$5,000	61.9%	27.5%	28.3%
\$5-\$9,999	48.8	32.8	22.2
\$10-14,999	60.2	33.0	28.7
\$15-19,999	63.1	37.5	26.2
\$20-24,999	65.0	37.4	32.9
\$25-29,999	68.0	43.5	41.5
\$30-34,999	69.2	43.8	36.8
\$35-39,999	69.2	50.4	48.8
\$40-49,999	73.5	57.4	48.6
\$50-59,999	78.9	57.2	59.7
\$60-69,999	82.1	70.6	66.2
\$70-79,999	85.1	73.2	71.3
\$80-99,999	89.0	76.5	74.7
\$100-119,999	92.6	80.7	78.4
> \$119,999	93.1	87.6	83.5

Five general observations can be made from the data presented in Table 3.2. First, with the exception of whites in the \$5-9,999 households, at every other household income level, the majority of whites are homeowners. Second, not until black household income is at least \$35,000 are the majority of blacks homeowners. Third, not until latino household income is at least \$50,000 are the majority of latinos homeowners. Fourth, at no level of income are the homeownership rates equal by race and/or ethnicity, but the differences shrink considerably at the higher income levels. Fifth, only at two different household income levels (lowest and \$50-59,999) is there a greater percentage of latino homeowners than black homeowners. At all other income levels, a greater percentage of blacks are homeowners than are latinos, although in several instances, the differences

81. Gale et. al. *supra* note 12, at 1174.

are minimal. Perhaps black preferences for buying real estate are a factor here as well. Even after controlling for a large number of observable factors, the black-white homeownership gap is smaller than just differences by income, but still existed.⁸² The gap was between five and ten percentage points.⁸³

Table 3.2 shows that as income rises, so do homeownership rates – regardless of race - which means that class matters. Table 3.2 shows that even at the same income levels there are significant differences in homeownership rates by race – which means that race matters more. Wealth is a factor as well. One study found large homeownership rate differences between black and white households with low wealth, although no racial differences in home ownership rates among households with higher wealth.⁸⁴

C. Unequal Access to Credit

Equal access to credit regardless of race and class has been an elusive goal for decades.⁸⁵ There are two concerns relevant here. The first is with the increased rejection rates of mortgage applications received by blacks and the increased interest expense paid by black and latino homeowners. Numerous studies have documented racial differences in mortgages, very few have controlled for creditworthiness.⁸⁶ One study which did control for creditworthiness found large and statistically significant differences in the probability of having a loan approved when comparing black and white

82. Gale, et al, *supra* note 12, at 1172 (“Studies suggest that, after controlling for a large number of observable characteristics, the unexplained black-white homeownership gap is smaller than just differences by income class would suggest....”)

83. *Id.* (“...[the gap] still ranges between 5 and 10 percentage points....” (citations omitted).

84. Charles and Hurst, *supra* note 17, at 282 (“Gyourko et al. (1999)... find no racial differences in home ownership rates among households with large enough wealth to meet down-payment and closing-cost requirements. However, they do find large ownership differences between black and white households with low wealth.”)

85. MELVIN OLIVER AND THOMAS SHAPIRO, *BLACK WEALTH/WHITE WEALTH* (1996) (race based discrimination); Baher Azmy, *Squaring the Predatory Lending Circle: A Case for States As Laboratories of Experimentation*, 57 FLA. L. REV. 295 (2005) (class and race discrimination).

86. Charles and Hurst, *supra* note 17, at 283 ([T]he failure of many previous studies to control for applicant credit worthiness makes it difficult to attribute the differences in acceptance rates to discrimination rather than unmeasured differences across races in factors that could affect the profitability of the loan.”)

households.⁸⁷

Data show that black renters are more likely *not* to apply for a mortgage than white renters.⁸⁸ Part of the explanation that has been proffered is that blacks fear rejection and therefore self-select not to apply for mortgages.⁸⁹

White homeowners are more likely to receive better financial terms in their mortgages than black homeowners.⁹⁰ Black homeowners are far more likely to be rejected by financial institutions for mortgages than white homeowners.⁹¹ Blacks who are approved for a mortgage are more likely to pay higher interest rates than whites.⁹² Middle income blacks and latinos are more likely to receive a subprime loan than the typical middle and upper income white household.⁹³ Further, blacks in high income

87. *Id* (citing Munnell et al (1996)). The authors point out two criticisms of this study. First, it was limited geographically to data collected by the Boston Federal Reserve on mortgage loan applications made by Boston area banks in 1990. Second, that it is possible that an individual may be responsible for more than one application in the data which could mistakenly lead to the analysis that blacks are more likely to be rejected if for example if the same black applicant submitted many applications all of which were rejected.

88. *Id* at 288 (“[W]hite renters were more than twice as likely than black renters to apply for a mortgage.”)

89. *Id* at 293 (“Because of what we have called the *discouragement effect*, there may also be an indirect feedback effect in that anticipating being rejected makes one less likely to apply in the first place.”) (emphasis added)

90. Lisa Keister, *supra* note 22, at 480 (“...that resale values of homes are greater for whites than for blacks, and that whites typically receive more favorable terms in home mortgage lending than blacks....”) (citations omitted.)

91. Shapiro, *supra* note 17, at 66-67. (“First, financial institutions reject African-Americans for home mortgages at considerably higher rates - about a 60% higher rejection rate - than whites, even when white and black families are equally creditworthy.... As sanctioned community redlining diminishes under pressure from the civil rights movement, community organizations, the Community Reinvestment Act and other fair-lending and fair-housing laws, it appears that financial institutions re-create similar results by constructing “objective” criteria of creditworthiness in such a way that individual minority families fall short far more often than white families, thereby re-drawing redlines by family instead of by community.”)(citations omitted)

92. *Id.* at 67 (“Second, blacks approved for home mortgages often pay higher interest rates on home loans. Blacks pay interest rates of approximately one third of a percent higher than whites, or about \$ 12,000 more for the average American home over a 30-year mortgage. Part of this is due to the greater ability of white families to provide larger down payments and even to pay higher service fees for lowered interest rates.”)(citations omitted)

93. Elizabeth Warren, *The Economics of Race: When Making it to the Middle is Not Enough*, 61 WASH. & LEE L. REV. 1777, 1794-1798 (2004); Manny Fernandez, *Racial Disparity Found Among New Yorkers With High-Rate Mortgages*, N.Y. TIMES, Oct. 15, 2007, at B1 (“In Jamaica, Queens, for example, where the majority is black and the median household income was \$45,000 in 2005, 46 percent of the mortgages were issued by lenders who specialize in subprime loans, the second highest rate in the city. In Bay Ridge, Brooklyn, which had a

neighborhoods are far more likely to use subprime refinancing than low-income white households.⁹⁴ Low-income families regardless of race are also subjected to unfair lending practices,⁹⁵ as are recent immigrant populations.⁹⁶ Lawsuits have recently been filed on behalf of blacks and latinos arguing that they have been purposely targeted and charged higher interest rates.⁹⁷

Professor Elizabeth Warren has performed an analysis of bankruptcy filings and shown that black and latino homeowners are more likely than white homeowners to file for bankruptcy.⁹⁸ She also attributes this

median income of \$50,000 and is mostly white, the rate was among the lowest in the city, with 3.6 percent of home loans coming from subprime lenders.”)

94. Kurt Eggert, *Held Up in Due Course: Predatory Lending, Securitization, and the Holder in Due Course Doctrine*, 35 CREIGHTON L. REV. 503, 574 (2002) Professor Eggert describes the problem as follows:

Subprime lending is disproportionately prevalent in low income and minority neighborhoods, being three times more likely in low-income than high-income neighborhoods, and with subprime refinancing five times more likely in predominantly black neighborhoods than in predominantly white neighborhoods. Worse yet, the disparity between the use of subprime lending in black and white neighborhoods is so great that borrowers in high income black neighborhoods relied on subprime refinancing twice as much as borrowers in low income white neighborhoods, with thirty-nine percent of high income homeowners in black neighborhoods using subprime financing compared to only eighteen percent of low income homeowners in white neighborhoods.

95. See e.g. Azmy, *supra* note 85, at 297-298 (2005) (“Reports of predatory lending emerged first anecdotally, as a shadowy practice of a particularly unscrupulous set of mortgage brokers and finance companies to manipulate vulnerable low-income, elderly, and minority homeowners into accepting mortgage products that would quickly and inevitably result in devastating home foreclosures.”)(citation omitted). Cf. Kathleen C. Engel and Patricia A. McCoy, *The CRA Implications of Predatory Lending*, 29 FORDHAM URB. L.J. 1571, 1578 (2002) (“One of the most troubling conclusions to emerge from the research on the subprime market is that substantial numbers of customers who qualify for prime loans are steered to costlier subprime loans that should be reserved for customers with weak credit ratings.”) (citation omitted)

96. See e.g. N. Edward Coulson, *Why Are Hispanic-and Asian-American Homeownership Rates So Low?: Immigration and Other Factors*, 45 J. URB. ECON. 209, 216 (1999)(“There may be also an unwillingness on the part of financial institutions to lend to recent immigrants.”)

97. Cf. Vikas Bajaj and Miguel Helft, *The Loan That Keeps On Taking*, N.Y. TIMES, Sept. 25, 2007, at A1 (“describing a lawsuit where the claim is made that “the defendants sought out Hispanics, violating a federal housing law.”); Fernandez, *supra* note 93, (“The N.A.A.C.P. filed a lawsuit in federal court in Los Angeles this year against 12 mortgage lenders. The lawsuit accuses the companies of steering black borrowers into subprime loans.”)

98. Warren, *supra* note 93, at 1789 (“[Bankruptcy] filing rates among white homeowners are about 6.1 per thousand. Latino homeowners are nearly three times more likely to file for bankruptcy, filing at a rate of about 16.4 per thousand. Black homeowners are at even greater risk. About 31.7 per thousand black homeowners file for bankruptcy in a single year....”)

phenomenon to predatory lending.⁹⁹

In summary, low-income homeowners, and homeowners of color are more likely to pay higher interest rates than middle- and upper-income white homeowners. That increased interest expense results in little or no accumulation of housing wealth.

D. Housing Wealth Disparities by Race and Class

Racially based wealth disparities in America, is widely known, and has been the subject of intense scrutiny.¹⁰⁰ Numerous proposals have been made seeking to encourage people of color to buy homes as a way to decrease that wealth disparity. Yet those proposals often ignore the barriers faced by people of color in the housing market.¹⁰¹

Blacks are more likely to buy homes that don't appreciate as much as do white homes.¹⁰² The same holds true for low-income homeowners.¹⁰³ In addition, the resale value of white homes is greater than for black homes.¹⁰⁴ The reasons for this phenomenon are complicated.

Homes lose about sixteen percent of their value when more than 10 percent of the neighborhood is black.¹⁰⁵ The point at which the black

99. *Id.* at 1794-1798.

100. *See e.g.* OLIVER AND SHAPIRO, *supra* note 85, at (1996) (analyzing the wealth disparity between blacks and whites at all income levels); Edward N. Wolff, Recent Trends in Wealth Ownership, from 1983 to 1998, in *ASSETS FOR THE POOR* 34, 46 (Thomas M. Shapiro & Edward N. Wolff eds., 2001).

101. *Cf.* Maruy Gittleman and Edward N. Wolff, *Racial Differences in Patterns of Wealth Accumulation*, 39 J. OF HUM. RES. 193, 200 (2004) ("Implicit in proposals to shift the portfolios of African Americans toward assets such as homes and businesses is that African Americans face barriers to the acquisition of these assets, owing to discrimination in mortgage and small business credit markets, customer discrimination, limited access to information about investment opportunities and other factors.")

102. *See supra* note 22 and accompanying text.

103. *Cf.* Deborah Kenn, *Paradise Unfound: The American Dream of Housing Justice For All*, 5 B.U. PUB. INT. L. J. 69, 84 (1995) ("The american dream of homeownership is premised upon a significant return on investment and appreciation of housing dollars. Limiting the appreciation, therefore, limits a homeowner's ability to improve his own housing situation and generates a second class form of homeownership for the poor.")

104. Keister, *supra* note 22, at 480 ("...that resale values of homes are greater for whites than for blacks, and that whites typically receive more favorable terms in home mortgage lending than blacks....") (citations omitted.).

105. *See supra* note 23 and accompanying text. *Cf.* Richard D. Alba, John R. Logan, and Brian J. Stults, *How Segregated are Middle-Class Americans?*, 47 SOC. PROB. 543, 552 (2000) ("This picture is consistent with the conclusion of Massey and Denton (1993) that whites at all socioeconomic levels avoid residence in neighborhoods that have more than very small percentages (5-10 percent seems typical) of African Americans.")

percentage of residents becomes too high for white comfort is called the “tipping point.”¹⁰⁶

Whites don’t want to live in neighborhoods with blacks, unless the percentage of blacks is very low.¹⁰⁷ Studies have not documented the same reaction by whites regarding asians or latinos.¹⁰⁸ Most whites prefer to live in overwhelmingly white neighborhoods, with only token representation by minorities, while most blacks prefer to live in 50/50 racially diverse neighborhoods.¹⁰⁹ As Nathan Glazer has noted “the neighborhood that

106. David P. Kasakove, *New York State Association of Realtors, Inc. v. Shaffer: When the Second Circuit Chooses Between Free Speech and Fair Housing, Who Wins?*, 61 BROOKLYN L. REV. 397, 422 (1995) (“Tipping” is the sociological term used to refer to the critical point at which whites, either a single family or collectively, leave a community, because of black entry into the neighborhood.”)

107. See e.g. Gregory D. Squires, *Housing Market Discrimination as a Contributor to Labor Market and Economic Inequality*, 609 ANNALS 200, 206 (2007) As Professor Squires has written:

African Americans have been particularly affected as several studies have found them to be the most disfavored minority group by whites as well as other racial and ethnic groups (Charles 2005). Evidence indicates that it is the presence of blacks, and not just neighborhood conditions often associated with black neighborhoods (e.g., bad schools, high crime) that accounts for white aversion to such areas. In one survey, whites reported that they would be unlikely to purchase a home that met their requirements in terms of price, number of rooms, and other housing characteristics in a neighborhood with good schools and low crime rates if there was a substantial representation of African Americans. The presence of Hispanics or Asians had no such effect (Emerson, Chai, and Yancey 2001).

See also Banks, *supra* note 22, at 686 (“The most charitable explanation for whites’ intolerance of more than a few black neighbors is that whites believe that as more blacks move into an area, property values will decline. thus, investment-sensitive whites look to a community’s racial composition as a barometer of its financial prospects.”) (citation omitted); Reynolds Farley and Maria Krysan, *The Residential Preferences of Blacks: Do They Explain Persistent Segregation?*, 80 SOC. FORCES 937 (2002) (demonstrating that blacks prefer to live in diverse, 50-50 communities, whereas whites prefer to live in homogenous white areas).

108. Squires, *supra* note 107, at 206 (“The presence of Hispanics or Asians had no such effect...” (citation omitted))

109. See e.g. Reynolds Farley and Maria Krysan, *The Residential Preferences of Blacks: Do They Explain Persistent Segregation?*, 80 SOC. FORCES 937 (2002) (demonstrating that blacks prefer to live in diverse, 50-50 communities, whereas whites prefer to live in homogenous white areas); john a. powell, *Government Tax and Housing Policies* 104, TAXING AMERICA (Karen B. Brown and Mary Louise Fellows, ed.) (NYU Press 1996) (“Although the preferred neighborhood composition of all whites is all, or predominantly, white, the expressed preference of most Blacks is for a neighborhood that is half-black, half-white.”) (citation omitted). Cf John O. Calmore, *Race/ism Lost and Found: The Fair Housing Act at Thirty*, 52 U. MIAMI L. REV. 1067, 1130 (1998) (“For many whites, this is another way of saying, ‘We’re sick of the whole issue’ (‘race fatigue’ is the term some social scientists use to describe this spreading feeling).”)

blacks would like, 50 percent black, is one that most whites would move away from, making it close to 100 percent black.”¹¹⁰

White preferences will only allow a limited percentage of blacks (no more than 10 percent) to be eligible for the greatest housing appreciation.¹¹¹

Similarly, black preferences will result in blacks living in neighborhoods with a greater than 10 percent minority population and result in their being ineligible for the greatest housing appreciation. Black preferences in this regard manifest a kind of “race fatigue” whereby many blacks make a conscious decision to not live in overwhelmingly white communities.¹¹²

There are primarily two explanations for why whites prefer not to live with blacks and they may operate individually or in tandem.¹¹³ The first is white aversion to minorities generally and the second is white fear that when minorities move into the neighborhood, their property values will decline.¹¹⁴

To compound the problem, realtors are reluctant to facilitate blacks buying homes in predominantly white neighborhoods where appreciation potential is great, for fear of the reaction of the existing white homeowners – their client base.¹¹⁵

Numerous studies have documented the black disadvantage in housing quality,¹¹⁶ and housing values.¹¹⁷ Blacks remain the most segregated group in America.¹¹⁸ This has translated into different housing conditions for

110. Peter H. Schuck, *Judging Remedies: Judicial Approaches to Housing Segregation*, 37 HARV. C.R.-C.L. L. REV. 289, 298 (2002).

111. Cf. Alba et. al, *supra* note 105, at 552 (“[white homeowners] usually live with very few black neighbors, in any event.... whites at all socioeconomic levels avoid residence in neighborhoods that have more than very small percentages (5-10 percent seems typical) of African-Americans.”)

112. Cf. Calmore *supra* note 109, at 1130.

113. See e.g. Bell and Parchomovsky, *supra* note 23, at 1981-82 (“A review of the literature on housing segregation reveals two main hypotheses as to why white homeowners in segregated neighborhoods are averse to minority entry. The first, and more straightforward one, is aversion to minorities per se. The second is fear of adverse economic effects associated with minority entry.”) (citations omitted)

114. *Id.*

115. See T. Alexander Aleinikoff, Note, *Racial Steering: The Real Estate Broker and Title VIII*, 85 YALE L.J. 808, 824 (1976) (arguing that residents of white areas are likely to prefer to list their homes with brokers who will steer black buyers to other neighborhoods).

116. Hayward Derrick Horton and Melvin E. Thomas, *Race, Class, and Family Structure: Differences in Housing Values for Black and White Homeowners*, 68 SOC. INQ. 114, 117 (1998) (citing Bianchi, Farley, and Spain 1982; Amin and Marian 1987).

117. *Id.* at 118 (citing Kain and Quigley 1975; Jackman and Jackman 1980; Lake 1981; Oliver and Shapiro 1995).

118. *Id.* at 118 (citing Massey, Condrayn, and Denton 1987; Denton and Massey 1988;

black homeowners when compared with white homeowners of comparable income levels.¹¹⁹ Blacks who own homes are more likely to live in communities with fewer whites, while white homeowners are more likely to live with more whites once they become homeowners.¹²⁰ White homeowners live with very few black neighbors.¹²¹

Blacks of higher socioeconomic levels have not gained parity with their higher socioeconomic white counterparts.¹²² The inequality in housing values between middle-class blacks and middle-class whites is greater than the housing inequality between their lower-status counterparts.¹²³ One possible explanation for this phenomenon is that blacks with high levels of income and education are unable to convert these attributes into a home in a desirable neighborhood with high appreciation value potential because of discrimination they face in the housing market.¹²⁴

Nevertheless, the benefits of homeownership to middle-class blacks are significant when compared to black renters. Blacks are not buying homes because homes are such a good investment, but homes afford blacks certain amenities.

Middle class black homeowners are able to send their children to better schools and are subject to lower crime rates.¹²⁵ Even so, middle-class blacks tend to live with white neighbors who are less affluent than they are.¹²⁶ Put another way, middle-class blacks live in neighborhoods that are not equal in affluence with their middle-class white counterparts.¹²⁷ Similarly situated white homeowners live in more affluent communities and

Massey and Denton 1989; Alba and Logan 1991)

119. *Id.* at 132 (“Black homeowners had housing values that were significantly lower than those of their White counterparts. This was the case despite control for age, social class, central city residence, household structure, and region.”)

120. Alba et. al, *supra* note 105, at 550.

121. *Id.* at 552.

122. Horton and Thomas, *supra* note 116, at 126.

123. *Id.* at 126.

124. *Id.* at 133.

125. Alba et. al, *supra* note 105, at 556 (“Middle-class African-Americans do, indeed, experience improvements in their residential location by comparison with their poorer co-ethnics...[T]he affluence of their neighborhoods, which is undoubtedly correlated with many other neighborhood characteristics from the quality of schools or housing to the risks of criminal victimization, goes up sharply in association with higher household income, personal educational attainment, home ownership, and suburban location.”).

126. *Id.* at 544 (However, their [middle class blacks’] white neighbors tend to have lower incomes than they do; consequently, middle-class blacks live in less affluent communities than do whites with the same socioeconomic characteristics.”).

127. *Id.* at 554.

suffer less crime than their black counterparts. So even though middle class black homeowners may fare better than black renters, they don't fare as well as middle class white homeowners.¹²⁸

Whites and blacks experience homeownership very differently. While neighborhoods of black homeowners generally are better off than neighborhoods of black renters, neighborhoods of white homeowners are *significantly* better than neighborhoods of white renters.¹²⁹

Many low-income homeowners sell their homes for less than what they paid for them.¹³⁰ Low-income homeowners do not remain homeowners like their higher-income counterparts and return to renting at extremely high rates.¹³¹ Homeownership may be a poor asset for low-income individuals to invest the bulk of net worth into because of its low return when compared with other investments.¹³² Gaining wealth from homeownership occurs from the sale of the second house (and subsequent houses).¹³³ Low-income homeowners who sell their first house and return to renting, do not reap significant benefits from homeownership.¹³⁴

To summarize, the upside potential for wealth appreciation from housing exists to a far greater extent for middle- and upper- income white homeowners than low-income white homeowners and homeowners of color. This is due to several factors. First, blacks and latinos receive mortgages with unfavorable terms. Second the value of homes decrease any time there are more than 10 percent of black homeowners in a particular neighborhood. Third, whites prefer to live in overwhelmingly white neighborhoods and blacks prefer to live in racially diverse neighborhoods. Fourth low-income homeowners are most likely to sell their homes at a loss and return to renting. Each of these factors guarantee that homeownership from a wealth accumulation perspective will be a relatively poor investment for low-income homeowners and black and

128. *Id.* at 556 (“At no point do blacks attain residential parity with whites – that is, the communities in which they reside have less affluence and other less desirable characteristics (e.g. more crime) than the communities where whites with similar personal and household characteristics are found.”).

129. Shlay, *supra* note 70, at 520 (emphasis added).

130. *Id.* at 519.

131. *Id.* at 519-20.

132. *Id.* at 520. (“Encouraging homeownership among low-income families will only increase the wealth gap in the United States.”)

133. *Id.*

134. *Id.*

latino homeowners when compared with the wealth accumulation prospects of middle and upper income white homeowners.

IV. Race and Class Impact of Federal Tax Subsidies for Homeownership

A. Non-deductibility of Rent.

Because rent payments are not deductible, those most likely to pay rent won't benefit. The majority of blacks and latinos are renters, and therefore are the most likely to be harmed by the lack of deductibility of rent payments. Whites and asians are most likely to be homeowners and not renters, and therefore don't pay the same "penalty." Also, those at the low-income levels would be most helped by a rent deduction, because they are the most likely not to itemize their deductions otherwise. Therefore low-income taxpayers regardless of race, and black and latino renters are the most likely to be harmed by the non-deductibility of rent provisions in existing federal tax policy.

B. Mortgage Interest Deduction and Real Property Tax Deduction.

The mortgage interest deduction and real property tax deduction benefit itemizers who are most likely to be middle and upper income taxpayers. In addition upper income taxpayers benefit the most because the tax deductions are worth more to those taxpayers. The President's Advisory Panel on Federal Tax Reform showed that taxpayers in the highest income group – those who made more than \$200,000 – received more than 8 times the benefit as those in the group making between \$50,000 and \$75,000.¹³⁵

Previous scholars have argued that because so many blacks and latinos purchase homes, they benefit significantly from the tax subsidies for housing, even though whites benefit more.¹³⁶ What is important to a determination of whether black and latino homeowners benefit from the housing tax subsidies is whether they are more likely to itemize. If they are

135. Gale, et al. *supra* note 12, at 1178.

136. See e.g. Moran and Whitford, *supra* note 14, at 780 ("Unlike the tax benefits that apply primarily to other forms of wealth, from which few blacks gain, many blacks benefit from the tax benefits of homeownership...But while blacks benefit, whites benefit even more."); Mann *supra* note 8, at 1365 ("Blacks and Hispanics derive less benefit from the home mortgage interest deduction because they tend to have lower incomes than whites.") (citation omitted).

not, then even though a significant percent are homeowners they will not benefit from the tax subsidies for housing.

For homeowners who do itemize, however, the argument could be made that subprime lending affords a higher interest deduction and thereby helps those taxpayers that the market disadvantages. Therefore black and latino homeowners who receive supprime or predatory loans benefit from the mortgage interest deduction – as do low-income white homeowners.¹³⁷ There are two responses to that argument. While it's true that increased deductible expenses provide a tax benefit, the increased interest payments equals slower wealth accumulation which more than offsets the increased interest payments. The “cost” of the increased deduction would be too high to result in any overall benefit.

An alternative argument could be made that since medical expenses are deductible¹³⁸ it's “good” to have lots of medical expenses to decrease your tax liability. In fact, a catastrophic illness not covered by insurance would be “ideal” because the taxpayer would have high medical expenses thereby lowering their taxable income. The “cost” however of getting additional medical expenses – is being extremely sick. Yet no one wishes for catastrophic illness, and no one wants to pay higher interest rates in order to get reduced taxable income. The lower the interest rate, the better the investment because the taxpayer can accumulate wealth at a faster rate thereby enhancing their overall net worth – even though the lower interest rate results in a reduced tax deduction and higher taxable income.

Given that only taxpayers who itemize deductions receive the benefit of the deductions, since there is a greater percentage of white middle- and upper-income homeowners than black, or latino middle- and upper-income homeowners, white homeowners are most likely to benefit from the mortgage interest deduction.

Real property tax deductions similarly only benefit taxpayers who itemize and the greater the income, the greater the tax benefit received. Although at the higher income levels, the alternative minimum tax (and the limit on itemized deductions generally) take back some of the tax subsidy for the real property tax deduction. Interestingly, a few geographically

137. Lest you think I'm making the argument in jest, I was once told that the progressive tax rate was good for blacks since they're poor and don't pay taxes. My response was if that was correct, then what we wanted to do was grow up to be poor so we don't have to pay taxes. But of course that isn't our response, what we really wanted was to be “a trust fund beneficiary with income excluded from taxation and not subject to the alternative minimum tax.”) Brown, *Tax Treatment*, *supra* note 50, at 805.

138. See I.R.C. §213 (2007).

targeted studies have shown that homes in majority/minority neighborhoods are assessed at higher effective rates than similar property in majority/white neighborhoods.¹³⁹ If those findings were ever replicated on a nationwide scale, then once again we would see blacks and latinos paying more for their housing costs than whites.

C. Exclusion for Imputed Rent.

The exclusion for imputed rent benefits high-income households the greatest for two reasons. First, those at the highest marginal tax rate receive the greatest benefit from the exclusion (as they did from the deduction). Second, one would expect the imputed rent to be the greatest for the most expensive homes, which would be those owned by high-income homeowners. While all homeowners benefit regardless of race or class, those in the most desirable neighborhoods benefit the most – and those are most likely to be middle and upper-income white homeowners. Those who benefit the least (or would have less income excluded) are those in the least desirable neighborhoods which are likely to be low-income white homeowners and homeowners (most likely black and latino) living in any neighborhood with more than 10 percent black neighbors.

D. Exclusion from Gain on Sale.

Housing appreciation upon sale is excluded up to a maximum of \$500,000 and amounts in excess are taxed at the lower capital gains rate. Because black homes are less likely to appreciate as much as white homes, black homeowners are far less likely to receive the full benefit of this exclusion and white homeowners are more likely to pay the preferential capital gains rate because their gain may exceed the exclusion amount. In fact, even if blacks wanted to live in white neighborhoods, only a token percentage would be “permitted” to do so. Therefore the majority of blacks will never be able to purchase homes with the most upside appreciation potential – because those houses are in overwhelmingly white neighborhoods that wish to remain overwhelmingly white. Again, the argument can be made that having gain that’s excluded is better than having

139. See Lee Harris, *Assessing’ Discrimination: The Influence of Race in Residential Property Tax Assessments*, 20 J. LAND USE & ENVTL. LAW 1 (2004) (describing author’s study of homes in New Haven, Connecticut).

so much gain that it is taxed, but that argument is unpersuasive. With the reduced capital gains rate applicable to any such gain, it is a small price for whites to pay for increasing their overall net worth. Low-income homeowners who are most likely to sell their homes at a loss won't receive this benefit.

E. Non-deductible Loss on Sale of Home.

Further, because low-income homeowners are most likely to sell their homes at a loss and losses on the sale of personal residences are not deductible, they receive no tax benefit from the sale of their home. Because gains are excluded and then taxed at a lower rate and losses are not taken into account in calculating taxable income, low-income homeowners who are most likely to sell their homes at a loss will not be able to get a tax break.

F. Wealth Building Aspects of the Tax Subsidy.

The economic literature that shows how the tax deduction encourages homeowners to buy a more expensive house has not been broken down by race. I argue that the tax subsidy is not working to encourage black and latino taxpayers to buy larger homes.¹⁴⁰ Assume the mortgage amount that a lender will approve is a function of the interest rate, the higher the interest rate, the lower the amount of the mortgage that will be approved. Blacks and latinos are charged higher interest rates which makes their mortgage amounts smaller than they would be if they were charged a lower interest rate. Add to that the fact that whites are more likely to receive down payment assistance from family members than blacks.¹⁴¹ It is highly likely that the tax subsidy is not operating in the same way for those subject to predatory lenders than those who are not.

140. Cf Mann *supra* note 8, at 1365 (“[I]t is unlikely that minority home ownership is facilitated or motivated by the tax benefits of the home mortgage deduction.”)

141. THOMAS SHAPIRO, *THE HIDDEN COSTS OF BEING AFRICAN AMERICAN: HOW WEALTH PERPETUATES INEQUALITY* 5 (Oxford University Press 2004); Charles and Hurst, *supra* note 17, at 284 (“[B]lacks may be less able to rely on their friends, parents, and other loved ones than their white counterparts for assistance in generating these down payments.”); Kerwin Charles and Erik Hurst, *Intergenerational Correlations in Wealth*, University of Chicago working paper (April 2000) (Study which showed that at any given wealth level, black households more likely had parents with lower net worth levels than white households.)

Purchasing more expensive homes – to the extent they are in neighborhoods with appreciation potential – will result in the highest appreciation and greatest wealth. Middle and upper income white homeowners are receiving the benefits of tax subsidized housing wealth. To the extent that subprime lending places a cap on the amount of the mortgage that homeowners could be qualified for, in the case of black and latino homeowners who are targeted by subprime lenders, the tax subsidy could be operating differently by race. In that instance, the tax subsidy may not be encouraging blacks and latinos to purchase more expensive homes.

G. Summary.

Federal tax policy encourages homeownership. Most blacks and latinos are renters and ineligible for any tax subsidies for their housing. Most whites and Asians are homeowners, and therefore eligible to receive tax subsidies. The tax subsidies tend to benefit more expensive homeowners and taxpayers subject to the highest marginal tax rates. Those homeowners are largely middle and upper white income homeowners. Low income homeowners and homeowners of color are least likely to benefit from the tax subsidies and least likely to accumulate wealth than their white counterparts.

The exclusion from income of imputed rental value benefits those who live in the most expensive homes – largely middle and upper income white homeowners. In addition, since whites are more likely to have the greatest housing appreciation, they are more likely than blacks to benefit from the exclusion from income on gain from the sale of their home. To the extent that low-income homeowners may be more likely to have a loss upon the sale of their home, their losses will not be deductible. Finally, blacks and latinos who are subject to higher interest rates may not be purchasing more expensive homes. They are not receiving the benefit of tax subsidized housing wealth appreciation. Federal tax policy does not treat all taxpayers the same regardless of race and/or class. Federal tax policy can and should do better.

V. Race and Class-Based Solutions: Disrupting Marketplace Discrimination

A. Introduction

For most Americans their homes are the single greatest contributor to their net worth.¹⁴² All homeowners have 48 percent of their net worth represented by their homes, while low-income homeowners have 80 percent of their net worth represented by their homes and upper income homeowners have 26 percent of their net worth represented by their homes.¹⁴³ When you examine the data by race, black and latino homeowners hold between 61 and 63 percent of their net worth in their homes and whites hold 38.5 percent of their net worth in their homes.¹⁴⁴

Homeowners of color and low-income homeowners currently face marketplace discrimination. At present, federal tax policies reinforce the race and class based discrimination faced by homeowners and contributes significantly to the wealth disparities in America. This section proposes changes to federal tax policy, which if adopted, would disrupt the race and

142. Cf. Shapiro, *supra* note 17, at 65 (“Homeownership is the largest component of the wealth portfolios of both white and black families. In 2002, housing wealth accounted for 63% of all wealth in African-American families.”) (citations omitted). The flip side of this point, however, is that renters have significantly less wealth than homeowners. See e.g. Lee Anne Fennell, *Book Review: Homes Rule: The Homevoter Hypothesis: How Home Values Influence Local Government Taxation, School Finance, and Land-Use Policies*, 112 YALE L.J. 617, 627 (2002) (“In 1998, the median family income of renters was less than half that of homeowners, and the median family net worth of renters was less than one-thirtieth that of homeowners.”) (citation omitted); Stephen G. Gilles, *The Judgment-Proof Society*, 63 WASH & LEE L. REV. 603, 715 fn 300 (2006) (“According to a 2004 study of census data by the Pew Hispanic Center, the median net worth of renters is only 1% of the median net worth of homeowners.”); Molly S. McUsic, *Looking Inside Out: Institutional Analysis and the Problem of Takings*, 92 NW. U.L. REV. 591, 664 fn 167 (1998) (“...[T]he median net worth of owner-occupiers is \$ 77,183 compared to \$ 2203 median net worth for renters.”); Warren, *supra* note 93, at 1790 (“The other side of the data showing that most Americans have their wealth tied up in their homes is that most renters have far lower total net worth than their home-owning counterparts. The differences are not confined only to homes. Renters have fewer assets of every kind—stocks, bonds, retirement accounts, cars, personal property, small businesses, and so on.”) (citation omitted).

143. See Michael A. Stegman, Allison Freeman, and Jong-Gyu Paik, *Home Equity and Other Differences in the Wealth of Low-and Moderate-Income Homeowners: A Work in Progress*, 4 (September 2006) available at <http://www.frbsf.org/community/research/assets/HomeEquityandOtherDifferencesinWealth.pdf> (“Among [lowest income households], home equity accounted for 80-percent of their net worth, compared to 48-percent for owners in the middle quintile and 26-percent for those in the highest quintile.”).

144. Kochhar, *supra* note 62, at 19.

class based discrimination faced by homeowners in the housing market and minimize housing wealth disparities.

B. Solutions to End Race and Class Discrimination.

This section provides four different proposals which are designed to decrease the race and class discrimination currently experienced by homeowners in the housing market and the latter two also seek to decrease existing housing wealth disparities. The first proposal would change existing deductions into refundable credits. The second would allow losses on the sale of homes for low-income taxpayers to be deductible. The third would only allow future deductions for homeownership to be received by homeowners in “racially diverse” neighborhoods. The fourth would tax subprime lenders who discriminate on the basis of race in their loan products. This section concludes by arguing that federal tax policy which is currently discriminating against low-income homeowners and middle and upper income black and latino homeowners must be changed.

1. Convert the Deduction into a Refundable Credit.

The President’s Advisory Panel on Federal Tax Reform suggested that the mortgage interest deduction be changed to a credit which would make it available to taxpayers who don’t itemize.¹⁴⁵ However, the fact that the credit would not be refundable would mean that it would not be available to very low-income homeowners who otherwise have no income tax liability. In addition, the proposal does nothing to address the racial disparities faced by taxpayers in the homeownership market.

Converting the deduction into a refundable credit responds to the class based discrimination faced in the market. In that way, low-income taxpayers who did not itemize, but had an income tax liability would benefit from the credit. Further, low-income taxpayers who did not have income tax liability (but paid social security taxes) would receive a refund from the government, allowing them the full benefits which their middle and upper-income counterparts already enjoy.¹⁴⁶

145. President’s Report, *supra* note 56, at 73-75.

146. Cf. Lily L. Batchelder, Fred T. Goldberg, Jr., and Peter Orszag, *Efficiency and Tax Incentives: The Case for Refundable Tax Credits*, 59 STAN. L. REV. 23, 28-29 (2006) (“Under current law, more than 35% of tax units during any given year have no income tax liability, and these tax units are home to almost half of all American children. Deductions, exclusions, and non-refundable credits are typically worthless to them.”)

As I have written elsewhere, making a credit refundable is politically perilous.¹⁴⁷ The earned income tax credit, which is a refundable credit has been analogized to “welfare” and the attendant racial politics that accompany that debate could become a part of this debate.¹⁴⁸ To increase the likelihood of success, what would have to be emphasized is that the overwhelming majority of homeowners are white and benefits for homeowners are likely to be received by whites. The difficulty then arises, because the poor are typically perceived as black. The interesting question would be whether the typical poor homeowner would be automatically presumed to be black or white. If the perception would be that the typical homeowner is white, the politics could work out favorably for the proposal.¹⁴⁹

2. Allow Losses to be Deductible.

Low-income homeowners are most likely to sell their homes at a loss and return to renting without receiving any wealth accumulation. This proposal would allow losses to be deducted on personal residences for low-income homeowners. Generally the loss on a sale of a personal residence would be characterized as a capital loss but not recognized. If recognized, the rules on capital loss deductions is that they are only allowed to the extent of capital gains and after all the gains are exhausted are only allowed to the extent of \$3,000 of ordinary income. Assuming that these households are less likely to have capital gains, allowing the loss won't help taxpayers very much. Therefore I'd allow the loss to offset ordinary income to a greater extent than just \$3,000 of current law. This proposal similar to the last one, does not address the race based market discrimination faced by black and latino homeowners.

3. Allow Credit for Racially Diverse Neighborhoods.

This solution would address the market premium placed on homogeneous white neighborhoods and the market penalty placed on neighborhoods with more than ten percent black homeowners. The

147. Brown, *Race and Class Matters*, *supra* note 50, at 816-819 (describing how EITC recipients are viewed as receiving “welfare” because of the refundable nature of the EITC).

148. *Id.*

149. *Id.* at 819-30 (describing how once public realized that majority of EITC claimants are white, support for the EITC would increase).

refundable credit would only be available to homeowners who purchased homes after the proposal was enacted, in neighborhoods with more than 10 percent black homeowners. Any homeowner, regardless of their race would be eligible for the credit. The market placed discrimination which currently penalizes homeowners where their neighbors are more than 10 percent black would be minimized if not eliminated. Therefore those homes should be priced at a premium if this proposal were adopted.

In addition, the tax provision would sunset in 25 years with a statutory requirement to study the market place impact of the credit every five years.

Twenty-five years was selected because Justice O'Connor in upholding Michigan Law School's use of race as a factor in admissions decisions, writing for the court wrote "We expect that 25 years from now, the use of racial preferences will no longer be necessary to further the interest approved today."¹⁵⁰ Many commentators have suggested that Justice O'Connor was stating that the constitutionality of race-based remedies turns upon whether they are time limited.¹⁵¹

The question is raised whether such a proposal would pass constitutional muster especially in light of recent Supreme Court precedent.¹⁵² (I would argue that even if it were determined that the proposal would be unconstitutional this should still be considered as a possible solution because race based wealth disparities has been an intractable problem and a solution which is unconstitutional could lead us to a solution which would be constitutional.) This proposal seeks to remedy the anti-integration bias currently existing in the home buying market. Does *Parents Involved* hold that anti-integration plans are per se unconstitutional, or does Justice Kennedy's concurrence suggest that a properly constructed plan would pass constitutional muster? As Justice Kennedy acknowledged in *Parents Involved* "neighborhoods in our communities do not reflect the diversity of our Nation as a whole."¹⁵³

This proposal would seek to encourage communities to become more racially diverse by minimizing the existing market place penalty currently

150. *Grutter v. Bollinger*, 539 U.S. 306, 343 (2003).

151. See e.g. J. Harvie Wilkinson III, *The Rehnquist Court at Twilight: The Lures and Perils of Split-the-Difference Jurisprudence*, 58 STAN. L. REV. 1969, 1974-75 (2006) (The Court also split the difference temporally, indicating that in twenty-five years, race-conscious admissions policies may no longer be narrowly tailored to a compelling state interest.) (citation omitted).

152. *Parents Involved in Community Schools v. Seattle School District No. 1*, 127 S. Ct. 2738 (2007).

153. *Id.* at 2797. I thank Professor Sam Bagenstos for suggesting that I look to Justice Kennedy's concurrence for support for my proposal.

placed on homes in neighborhoods with more than 10 percent black homeowners. If however one were to conclude that it would be unconstitutional to encourage racial integration it would suggest far greater reasons for concern than the tax policy considerations expressed in this paper.¹⁵⁴

Finally, an additional argument in support of the proposal's constitutionality would be that this simply remedies past governmental race based discrimination – the effects of which are ongoing. Racially restrictive covenants were legal until 1948.¹⁵⁵ The Federal Housing Administration and Veteran's Administration policies excluded blacks from benefiting from homeownership for decades.¹⁵⁶

Turning to the proposal's impact, it must be considered how it would effect existing homes. Although there are obviously no studies on this, one could predict that homes in "racially diverse" neighborhoods would increase in value and homes in non-racially diverse neighborhoods may decrease in value.¹⁵⁷ Even though I am not suggesting the repeal of the current deductions for existing homes, their homes would no longer be as attractive to new purchasers since new purchasers could not receive tax benefits except if they moved into "racially diverse" communities.

154. A constitutional analysis of this suggestion is outside the scope of this paper. The proposal is intended as an attempt to think about how tax policy could be designed if as a society we had as a goal the creation of wealth for all taxpayers regardless of race or class. A determination that this proposal is unconstitutional would end the discussion prematurely.

155. *Shelly v. Kraemer*, 334 U.S. 1 (1948).

156. See e.g. Jack Greenberg, *Affirmative Action in Higher Education: Confronting the Condition and Theory*, 43 B.C. L. Rev 521, 593 (2002). As Professor Greenberg has written:

The 'greatest mass-based opportunity for wealth accumulation in American history,' investing in a home during the 1950s and later, was also off limits to blacks. The Federal Housing Administration (FHA) and the Veteran's Administration (VA), which administered the mortgage insurance programs that made possible buying a home at reasonable mortgage rates, explicitly refused to insure mortgages for blacks in white neighborhoods. Huge housing developments, like Levittown, would not sell to blacks. Nothing comparable was built by or for blacks. They were tightly concentrated in the ghetto where property values not only did not soar, but suffered in value because of the ambient social pathology. In contrast, the value of homes purchased under FHA-insured and VA-insured mortgage arrangements has increased spectacularly and constitutes many families' largest asset.(citations omitted)

157. I will point out that white homeowners are most likely to be able to absorb such a loss in net wealth, because they are most likely to have net worth from a variety of different sources. See Kochhar, *supra* note 62, at 19 (showing that while 61 percent of mean net worth is found in latinos' homes and 63 percent is found in black homes, only 38.5 percent is found in white homes with 21.9 percent of white mean net worth coming from stock ownership.)

That would mean middle and upper income white homes would decrease in value – along with the homes of any blacks or latinos who lived in those neighborhoods. Yet the value decline would not have to be permanent. Homogeneous neighborhoods could become “racially diverse” neighborhoods if they managed to attract prospective black homeowners to their neighborhoods. The impact on low-income neighborhoods would probably be negligible given the fact that low income taxpayers don’t itemize deductions and don’t receive the tax benefit. However, if it were found that the value of low income homes were reduced, they too could seek to become “racially diverse” by attracting prospective black homeowners perhaps a more arduous task than that faced by higher income white neighborhoods.

4. Tax on Subprime Lenders

To penalize lenders who target subprime loans to homeowners of color, a new “subprime tax” would need to be enacted. Lenders who charge higher interest rates to homeowners of color when compared with their similarly situated white counterparts would pay the additional tax. Lenders who after the date of the enactment of the tax decided to only make loans to white homeowners as a means of avoiding the subprime tax would also be required to pay an additional tax.

Conclusion

Wealth building for communities of color is an important issue for the 21st century.¹⁵⁸ Federal tax policies that “support homeownership” should be examined from a race and class perspective in order to understand which demographic groups such policies are actually helping. This Article has shown that those policies have a race and class based discriminatory impact and contribute to the wealth disparities in this country. Those policies must be eliminated and in their place, rules should be enacted, which seek to empower all homeowners regardless of their race and class an equal opportunity to benefit from their American Dream.

158. Shapiro, *supra* note 17, at 65 (“This is not simply a story about counting money; families think about using wealth first as a private safety net, and second as a vehicle to launch mobility into middle-class status, homeownership, business development, or a more secure retirement.”) (citations omitted)