The Mortgage Interest Deduction: Oregon's Biggest (and Ineffective) Housing Subsidy

Costing about one billion dollars, Oregon's mortgage interest deduction is the state's biggest housing subsidy. The greatest beneficiaries of this housing subsidy are those who least need help owning a home: Oregonians at the top of the income ladder.

This fact sheet explains the basics of Oregon's mortgage interest deduction.

What is the mortgage interest deduction?
The mortgage interest deduction is a tax subsidy for some homeowners. It allows some taxpayers who own a home to reduce their taxable income by the amount of interest paid on their mortgage.

Is the mortgage interest deduction a federal or state program?
Both. Oregon households claiming the deduction can do so on their federal and state tax returns.

Why is the mortgage interest deduction a housing subsidy?
The mortgage interest deduction lowers the cost of owning a home for those who can claim the deduction, typically higher-income households.

Is the mortgage interest deduction Oregon's biggest housing subsidy?
Yes. Oregon's mortgage interest deduction is projected to cost the state close to $1 billion in the upcoming (2015-17) budget cycle.[1] To put that in perspective, it is more than the entire budget of the Oregon Housing and Community Services Department ($678 million) in the current budget period.[2] It is about 10 times the size of Governor Brown's proposal to use $100 million of Lottery- and General Fund-backed bonds to build an estimated 3,000 to 4,000 units of affordable housing.[3]

Could the money be better spent to promote housing?
Oregon could chose to use those tax dollars differently. For example, the state could use those tax dollars to build affordable housing or provide a tax credit to low- and middle-income first-time homeowners.

Who can use the mortgage interest deduction?
To claim the deduction, a taxpayer must own a home, have mortgage interest expenses and enough other deductible expenses to itemize deductions on the federal and state tax return. By definition, the housing subsidy excludes Oregonians who rent a place to live or who do not itemize deductions.

How many Oregonians benefit from the housing subsidy?
Only one-third (33 percent) of Oregon taxpayers claimed the mortgage interest deduction in 2011.[4]

Does it subsidize someone who purchases a mansion?

Taxpayers can deduct interest paid on a mortgage debt of up to $1 million on a principal home, mortgage debt up to $1 million on a second home, and up to $100,000 on a home equity loan.[5] In other words, taxpayers subsidize people who can afford payments on a $1 million mortgage.

Who benefits the most from the mortgage interest deduction?

The mortgage interest deduction mainly benefits the well-off. If you divide all Oregon taxpayers into five groups according to income, then the highest-earning fifth together collected 61 percent of all the tax savings from the mortgage interest deduction in 2011. The bottom two-fifths (the lowest-earning 40 percent of all taxpayers) together received less than 3 percent of the tax benefits.

Why do most of the benefits go to the well-off?

There are several reasons. First, the mortgage interest deduction only helps homeowners, and higher-income earners are more likely to own a home than lower-income earners.[6] Second, the subsidy only helps those who itemize deductions and they are disproportionately higher-income earners.[7] And third, because it is a deduction from taxable income (not a credit against taxes), it is more valuable to those with more income in the top tax brackets — the wealthy. In other words, a high-income household with the same mortgage payment as a middle-income household will get a greater subsidy from the deduction because the high income household pays taxes at a higher tax rate. Dollar-for-dollar of interest the deduction is worth more to high-income households.

Does the mortgage interest deduction promote home ownership?

No. The home mortgage interest deduction does not promote home ownership.[8] Among the ten states with an income tax that do not offer a mortgage interest deduction, eight had homeownership rates higher than the national rate in 2013.[9] Oregon, despite its expensive subsidy program, ranked below the national average and below all but one of the states that levy an income tax but offer no mortgage interest deduction.[10] This finding makes sense, considering that the subsidy is structured to primarily benefit those who do not need help affording a home, the well-off.

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Endnotes

[1] 2015-17 Oregon Tax Expenditure Report, p. 91.

[2] Legislative Fiscal Office, Analysis of the 2013-15 Legislatively Adopted Budget, p. 183.

[3] Proposed $100 Million Family Affordable Housing, Presentation to Ways and Means Subcommittee on Transportation and Economic Development, Margaret S. Van Vliet, Director, April 8, 2015, available at https://olis.leg.state.or.us/liz/2015R1/Downloads/CommitteeMeetingDocument/61778.

[4] OCPP analysis of Oregon Department of Revenue data.

[5] See IRS Publication 936.

[6] Jason Fichtner and Jacob Feldman, *Reforming the Mortgage Interest Deduction, Mercatus Center*, George Mason University, June 2014, p. 8.

[7] Of the top fifth of Oregon earners, 88 percent itemized their deductions on their Oregon tax return in 2013. Of the bottom four fifths of earners, just 36 percent itemized. OCPP analysis of Oregon Department of Revenue data.

[8] See, e.g., Christian A. L. Hilber and Tracy M. Turner, *The Mortgage Interest Deduction and Its Impact on Homeownership*, Spatial Economics Research Center, September 2010; Edward L. Glaeser and Jesse M. Shapiro, *The Benefits of the Home Mortgage Interest Deduction*, National Bureau of Economic Research, January 2003.

[9] OCPP analysis of 2013 American Community Survey data. The 10 states that levy a personal income tax but offer no mortgage interest deduction are Connecticut, Illinois, Indiana, Massachusetts, Michigan, New Jersey, Ohio, Pennsylvania, Rhode Island, and West Virginia. All but Massachusetts and Rhode Island had home ownership rates higher than the national average. Only Rhode Island had a home ownership rate lower than Oregon.

[10] Ibid.