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Shades of the American Dream

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SHADES OF THE AMERICAN DREAM

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ABSTRACT

Federal tax policies such as the mortgage interest deduction do not generally encourage anyone to become a homeowner, yet they do increase the cost of housing. Low-income homeowners regardless of race are least likely to be able to take advantage of the mortgage interest deduction. They pay for a benefit that they cannot receive. Middle- and upper-income black homeowners are less likely than middle- and upper-income white homeowners to benefit from federal tax laws supporting homeownership in different ways. The appreciation of most middle- and upper-income black homes is significantly less than the appreciation of middle- and upper-income white homes. As a result, those black homeowners will not benefit as much as white homeowners from the tax provisions that exclude from income gain on the sale of their homes. This Article suggests three solutions which, if enacted, would cause the tax benefits to be more equitably distributed and no longer concentrated in the hands of higher income, white taxpayers.

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> *I will give you an example of how race affects my life. I live in a place called Alpine, New Jersey. . . . My house costs millions of dollars. . . . In my neighborhood, there are four black people. Hundreds of houses, four black people. Who are these black people? Well, there's me, Mary J. Blige, Jay-Z and Eddie Murphy. Only black people in the whole neighborhood. . . . Do you know what the white man that lives next door to me does for a living? He's a . . . dentist!*
>
> *—Chris Rock, Kill the Messenger (HBO Home Video 2009)*

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I. INTRODUCTION

If Chris Rock is right, and there are only four blacks in his neighborhood, then Chris Rock's home is an excellent financial investment.[1] Home ownership in Alpine, New Jersey, is an excellent financial investment precisely because very few blacks live there. Chris Rock and all other blacks in America are subject to the reality that once a neighborhood has more than 10% black homeowners, the home values decline.[2] While recent events show the downside of homeownership for many Americans,[3] for African-Americans generally, homeownership has always been a mixed blessing.

Unlike Chris Rock, most African-Americans do not live in overwhelmingly white, wealthy neighborhoods.[4] For the majority of

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1. *Cf.* Glenn Beck, *Media Attacks Sarah Palin; Can Palin Win Over Clintonites?; What is Troopergate?* (CNN television broadcast Sept. 3, 2008) ("Alpine, New Jersey, which only has a population of 1.5% that is black.").

2. Abraham Bell & Gideon Parchomovsky, *The Integration Game*, 100 COLUM. L. REV. 1965, 1984 (2000) (noting that 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%."); Nancy A. Denton, *The Role of Residential Segregation in Promoting and Maintaining Inequality in Wealth and Property*, 34 IND. L. REV. 1199, 1207–08 (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 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.

Id. (citations omitted); Thomas M. Shapiro, *Race, Homeownership and Wealth*, 20 WASH. U. J.L. & POL'Y 53, 68 (2006) ("Moreover, homes lose about 16% of their value when located in neighborhoods that are more than 10% black.") (citation omitted).

3. *See, e.g.*, 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."); 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."); Alexandra Marks & Ron Scherer, *As Foreclosures Mount, States Step In*, CHRISTIAN SCI. 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 S. 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 [sic] home than ever before.").

4. *See, e.g.*, David Rusk, *The "Segregation Tax": The Cost of Racial Segregation to Black*

blacks, homeownership is a poor financial investment.[5] To be sure, there are other non-financial benefits received by black homeowners, including better neighborhoods, better schools, and less crime.[6] But the vast majority of whites receive better neighborhoods, better schools, less crime and a good financial investment when they become homeowners.[7]

Homeownership in America has historically been viewed as a solid investment both financially[8] and as a means of living the American Dream.[9] This Article will show that homeownership has never been a good financial investment for either the vast majority of African-American homeowners or for low-income homeowners. Government subsidies for homeownership, especially federal tax subsidies, create winners and losers generally along race and class lines.

Homeowners, BROOKINGS INST. SURVEY SERIES, Oct. 2001 at 4 ("[T]he typical black resident lived in a neighborhood that was 50 percent black, and almost two-thirds of black residents would have to move in order for every neighborhood to be 13 percent black.").

5. *See infra* Part IV.D.

6. *See infra* note 128 and accompanying text.

7. *See infra* notes 128–32 and accompanying text.

8. *See* Rusk, *supra* note 4, at 2 ("Home equity is the typical American family's most important financial asset, and an important vehicle for transmitting wealth from generation to generation."). The flip side of this point, however, is that renters have significantly less wealth than homeowners. *See, e.g.*, Stephen G. Gilles, *The Judgment-Proof Society*, 63 WASH. & LEE L. REV. 603, 670 n.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.") (citations omitted); Molly S. McUsic, *Looking Inside Out: Institutional Analysis and the Problem of Takings*, 92 NW. U. L. REV. 591, 627 n.167 (1998) ("[T]he median net worth of owner-occupiers is $77,183 compared to $2203 median net worth for renters."); Shapiro, *supra* note 2, 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); Elizabeth Warren, *The Economics of Race: When Making it to the Middle is Not Enough*, 61 WASH. & LEE L. REV. 1777, 1790 (2004) ("[M]ost 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); Lee Anne Fennell, *Homes Rule*, 112 YALE L.J. 617, 627 (2002) (reviewing WILLIAM A. FISCHEL, THE HOMEVOTER HYPOTHESIS: HOW HOME VALUES INFLUENCE LOCAL GOVERNMENT TAXATION, SCHOOL FINANCE, AND LAND-USE POLICIES (2001)) ("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).

9. *See* Douglas G. Baird, *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.") (citation 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.").

Middle- and upper-income taxpayers who are overwhelmingly white benefit the most from federal tax subsidies for housing.[10] On the other hand, the majority of low-income taxpayers, regardless of race, and the majority of African-American taxpayers, regardless of class, are the least likely to benefit from federal tax subsidies for housing.[11] Given the near collapse of our housing industry, now may be the time to re-think the government's generous federal tax subsidies for homeownership.

It is estimated that for fiscal year 2009, the loss in tax revenue from the tax subsidies for housing will be in excess of $207 billion.[12] Adding insult to injury, economists agree that virtually no one buys a house because of those tax subsidies, but the subsidies do increase the cost of housing.[13] Federal tax subsidies for homeownership are expensive and inefficient, with race and class key determinants of their receipt. Finally, homeownership increases wealth disparities by race in America.[14] Therefore, the current subsidies for homeownership are too costly to retain in their present form.

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10. *See infra* Part IV.E. This is true because middle- and upper-income taxpayers are most likely to be homeowners than any other racial or ethnic group and eligible to itemize their deductions.

11. *See infra* Part III.C. This is true because low-income homeowners are most likely to sell their homes for a non-deductible loss, blacks are more likely to be renters ineligible for federal tax subsidies, and blacks who are homeowners are less likely to benefit from tax provisions that reward valuable homes with significant equity appreciation.

12. OFFICE OF MGMT. & BUDGET, ANALYTICAL PERSPECTIVES, BUDGET OF THE UNITED STATES GOVERNMENT, FISCAL YEAR 2007, 288 (Author's calculations: $94.5 billion (mortgage interest); $12.8 billion (real property taxes); $59.9 billion (exclusion of gain on sale of residence); and $40.6 (exclusion for net imputed rental income) for a total of $207.8 billion.).

13. *See, e.g.*, William G. Gale, Jonathan Gruber & 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."); Edward L. Glaeser & Jesse M. Shapiro, *The Benefits of the Home Mortgage Interest Deduction*, 17 TAX POL'Y & 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."); 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, 1391 (2000) ("None of the evidence from economists or from other countries suggests that the repeal of the home mortgage interest deduction would reduce demand for owner occupied housing or home ownership rates."); Roger Lowenstein, *Who Needs the Mortgage-Interest Deduction?*, N.Y. TIMES, Mar. 5, 2006, § 6 (Magazine), at 78 ("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 . . . .").

14. *Cf.* Kerwin Kofi Charles & Erik Hurst, *The Transition to Home Ownership and the Black-White Wealth Gap*, 84 REV. ECON. STAT. 281, 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."); Shapiro, *supra* note 2, at 68 ("Just as home ownership creates wealth for both whites and blacks, it simultaneously widens the racial wealth gap under current conditions.").

Part II begins by discussing the literature demonstrating that tax subsidies encourage virtually no one to purchase a house. The tax subsidies benefit those who were already going to buy homes. The literature does conclude, however, that tax benefits increase the cost of housing and taxpayers purchase more expensive homes than they would without the tax benefits. Part II then briefly describes the well-known federal tax benefits associated with homeownership: deductions for mortgage interest and real property taxes,[15] an exclusion from income of the imputed rental value of our homes,[16] and an exclusion from income of the gain on the sale of our personal residence.[17]

Part III provides a class-based analysis of federal tax benefits for homeownership. Most low-income taxpayers are not homeowners and are not eligible for federal tax benefits. For those low-income taxpayers who are homeowners, many do not itemize deductions and thus cannot receive the benefits of the mortgage interest deduction, which has been included in the price of the asset that they have purchased. Increased housing costs caused by the tax subsidy make it more difficult for low-income taxpayers to buy homes. In addition, low-income homeowners often sell their homes at a loss and cannot deduct that loss. On the other hand, middle- and upper-income taxpayers—regardless of race—are most likely to become homeowners and most likely to itemize deductions; however, they may be subject to the alternative minimum tax and lose a portion of their real property tax deductions. Further, upper-income taxpayers are most likely to benefit from the exclusion of imputed rental income as well as the exclusion from gain on the sale of their personal residence.

Part IV provides a race-based analysis of federal tax benefits for homeownership. Tax laws disadvantage black taxpayers and other taxpayers of color in three different ways.[18] First, tax laws only benefit homeowners, and whites are far more likely to be homeowners than any other racial or ethnic group.[19] Second, the housing market penalizes neighborhoods where more than 10% of the homeowners are black, while the housing market gives a bonus to neighborhoods where homeowners

15. *See infra* Part II.B.

16. *Id.*

17. *Id.*

18. The Article attempts to address the racial and ethnic effects of federal tax law on all racial and ethnic groups. In certain instances, the Article focuses on black and white taxpayers because of the wealth of empirical data that exists for black and white homeowners that does not exist for other groups.

19. *See infra* Part IV.B.

are at least 90% white.[20] Most black homeowners live in majority black neighborhoods, and most white homeowners live in majority white neighborhoods.[21] As a result, there is an effective cap on the appreciation for black homes when compared with their white counterparts living in 90% white neighborhoods.[22] Federal tax policy's exclusion from income for the gain on the sale of their homes will always disadvantage blacks who, unlike Chris Rock, do not live in 90% white neighborhoods when compared to their white counterparts who do. Finally, the exclusion for imputed rent will similarly be worth more the more the home is worth. Given that there is an effective cap on the value of black homes that are not in overwhelmingly white neighborhoods when compared to white homes that are, the exclusion will be worth more to middle- and upper-income white homeowners who live in overwhelmingly white neighborhoods than middle- and upper-income black homeowners who do not. This Part also discusses blogosphere comments about earlier drafts of the Article.

Part V provides three solutions to the race- and class-based problems identified herein. It begins with a critique of prior articles that have analyzed housing tax subsidies from a race[23] and/or class[24] perspective. The critique shows that proposed solutions either ignore the race-based discrimination faced by homeowners of color, or would make things worse for black homeowners. Part V then offers three different solutions which

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20. *See supra* note 2 and accompanying text. This 10% cap only seems to apply to the percentage of blacks living in the neighborhood and not to Hispanics, Asians, or Native Americans. *See* Rusk, *supra* note 4, at 4 (Table 2 showing no statistical significance in the differences in racial neighborhood composition except for blacks.).

21. *See supra* note 2.

22. *See* Katherine A. Kiel & Jeffrey E. Zabel, *House Price Differentials in U.S. Cities: Household and Neighborhood Racial Effects*, 5 J. HOUSING ECON. 143, 156 (1996) (authors studied housing appreciation in Chicago, Denver, and Philadelphia and found housing appreciation was limited for minority homeowners in Chicago and Philadelphia, but not Denver); Sunwoong Kim, *Race and Home Price Appreciation in Urban Neighborhoods: Evidence from Milwaukee, Wisconsin*, 28 REV. BLACK POL. ECON. 9, 9 (2000) ("In this paper, we provide strong empirical evidence that the neighborhoods that are heavily resided in by racial minorities experience low appreciation rates in the long run.").

23. *See, e.g.*, Mann, *supra* note 13, at 1365–66 (2000) (describing race and class impact of the mortgage interest deduction); Beverly I. Moran & William Whitford, *A Black Critique of the Internal Revenue Code*, 1996 WISC. L. REV. 751, 780 (describing racial impact of the mortgage interest deduction); Mylinh Uy, Comment, *Tax and Race: The Impact on Asian Americans*, 11 ASIAN L.J. 117, 124–27 (2004) (describing racial impact of the mortgage interest deduction).

24. *See, e.g.*, Mann, *supra* note 13, at 1360–62 nn.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.").

will better target reform to those low-income and black middle- and upper-income homeowners currently disadvantaged by federal tax policies.

First, refundable credits should be available for housing to insure low-income homeowners who have purchased an asset with the tax deduction built into the price will be able to receive a tax benefit. Second, losses on the sale of personal residences for low-income homeowners should be allowed to offset ordinary income. Third, housing tax benefits should only be allowed for homes in "racially diverse" neighborhoods. Instead of reinforcing the race-based discrimination currently existing in the housing market, tax law should counteract it. A tax subsidy for homeowners in "racially diverse" neighborhoods would make homes in those neighborhoods more valuable as compensation for the earlier market penalty. The Article concludes by noting that, to the extent that tax policies are imposing a barrier to homeownership on the basis of race and/or class, those policies must change. These extreme financial times call for extreme reform measures.

II. FEDERAL TAX SUBSIDIES FOR HOUSING

A. *Tax Benefits Increase the Cost of Homeownership, But Do Not Impact the Decision to Purchase A Home*

Numerous articles have examined the tax benefits associated with housing.[25] Since the beginning of our income tax until the Tax Reform Act of 1986, all interest was deductible.[26] While the legislative history on the allowance of personal interest is sparse, when Congress amended the Internal Revenue Code to continue to allow the mortgage interest deduction in 1986, while disallowing, for example, a deduction for credit card interest payments, it cited encouraging homeownership as justification[27] notwithstanding the empirical data that shows that tax

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25. *See, e.g.*, Mann, *supra* note 13, at 1361 ("The home mortgage interest deduction thus constitutes an upside-down subsidy—the greater the need, the smaller the subsidy.") (citation omitted); William T. Mathias, *Curtailing the Economic Distortions of the Mortgage Interest Deduction*, 30 U. MICH. J.L. REFORM 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).

26. Mathias, *supra* note 25, 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, 436–38 (1992) (describing the Tax Reform Act changes to interest deductions).

27. *See* STAFF OF J. COMM. ON TAXATION, 100TH CONG., GENERAL EXPLANATION OF THE TAX

benefits generally do not encourage taxpayers to purchase homes, but encourage taxpayers to purchase bigger, 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 of housing by 10%.[28] The price increase will be greatest in areas with high tax rates and high housing prices.[29] Generally, it is believed that the deductions for mortgage interest and property taxes are built into the price thus increasing the costs of housing.[30] The market, however, has trouble distinguishing between taxpayers who receive different tax benefits from the mortgage interest deduction and increases the cost based on the highest benefit that could be received.[31]

Time-series studies in the United States show that the mortgage interest deduction does not influence the decision to purchase a home.[32] Even though the last forty years have presented a significant fluctuation in the inflation rate and tax rates, the homeownership rate has moved very little.[33] Nevertheless, homeownership is a tax-favored investment in America.

REFORM ACT OF 1986 263–64 (Comm. Print 1987) ("Congress nevertheless determined that encouraging home ownership is an important policy goal, achieved in part by providing a deduction for residential mortgage interest."); Mathias, *supra* note 25, at 73 ("When Congress fashioned the current rules for the mortgage interest deduction, its stated goal was to foster home ownership.") (citation omitted).

28. *See* Gale et al., *supra* note 13, 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 about 10 percent.").

29. *Id.* ("The increases are greatest in areas with high tax rates and house prices.").

30. *See* Mathias, *supra* note 25, at 64 ("[T]here seems to be general agreement that some portion of the mortgage interest deduction is capitalized into the market price of owner-occupied housing, there is no agreement on the extent to which the deduction is capitalized."); *see also* Eric Kades, *Windfalls*, 108 YALE L.J. 1489, 1501 n.20 (1999) ("[T]he mortgage interest deduction has made homes more valuable and has undoubtedly been capitalized into home prices."). *Cf.* Martin J. McMahon, Jr., *Individual Tax Reform for Fairness and Simplicity: Let Economic Growth Fend for Itself*, 50 WASH. & LEE L. REV. 459, 486 (1993) (suggesting that the mortgage interest deduction is mostly capitalized into the price of a home).

31. Mathias, *supra* note 25, at 64 ("The market has trouble distinguishing between taxpayers who receive different levels of benefit from the mortgage interest deduction based on their marginal tax rate and so the market price for housing tends to reflect the highest benefit received from the deduction.").

32. *See* Gale et al., *supra* note 13, at 1180 ("Time-series evidence in the U.S. provides little reason to believe that the [mortgage interest deduction] has a substantial influence on homeownership.").

33. *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 . . . .").

B. Federal Tax Laws Significantly Subsidize Homeownership

Homeowners are allowed to deduct from their income their mortgage interest expenses[34] and real property taxes[35] in computing their tax liability,[36] yet imputed rental income (the income the homeowner would receive if she rented her house to a tenant at fair market value) is excluded from income.[37] If the imputed rental income were taxable, then taxpayers would be taxed on amounts they never actually receive. In addition, the more valuable the home, the higher the imputed income taxes due.

The mortgage interest deduction is allowed on a primary and/or secondary home as long as the mortgage does not exceed $1 million. Although mortgage interest is deducted in computing taxable income, rent is not deductible.[38] When we sell our homes, some (or all)[39] of the gain is

34. I.R.C. § 163(h) (2007). Generally, personal interest cannot be deducted; however, there is an exception for "qualified residence interest." The interest can be deducted on a mortgage (or mortgages) not to exceed $1 million and a home equity loan (or loans) not to exceed $100,000. *Id.* In addition, taxpayers with adjusted gross incomes of $100,000 or less 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 adjusted gross incomes greater than $100,000, the amount of the deduction phases out. I.R.C. § 163(h)(3)(E)(ii).

35. I.R.C. § 164(a)(1) (2007).

36. Recently, Congress phased out the limits on itemized deductions that previously faced middle- and upper-income taxpayers under I.R.C. § 68 (2007). *See* Reed Shuldiner & David Shakow, *Lessons From The Limitation on Itemized Deductions*, 93 TAX NOTES 673, 679 (2001) ("The most important change in the 2001 Act affecting 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% floor that most other itemized deductions are subject to. I.R.C. § 67 (2007). They may be on their way back given the Obama administration's budget proposal to limit the tax benefit for itemized deductions to families earning more than $250,000 and singles earning more than $200,000. Jackie Calmes and Robert Pear, *Obama to Call for Higher Tax on Top Earners*, N.Y. TIMES, Feb. 26, 2009, at A1 ("President Obama will propose further tax increases on the affluent . . . calling for stricter limits on the benefits of itemized deductions taken by the wealthiest households . . . .").

37. *See, e.g.*, Joseph Bankman & Thomas Griffith, *Social Welfare and the Rate Structure: A New Look At Progressive Taxation*, 75 CAL. 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." (citing 1 B. BITTKER, FEDERAL TAXATION OF INCOME, ESTATES AND GIFTS ¶ 5.3.3 (1981))); Mann, *supra* note 13, at 1348–49 ("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. *See* Treas. Reg. § 1.262-1(b)(3) ("Expenses of maintaining a household, including amounts paid for rent . . . are not deductible.").

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

excluded from our income, and—if any of the gain is taxed—it is taxed at the lower capital gains rate.[40] If we sell our homes at a loss, however, that loss is not recognized.[41] In addition, the alternative minimum tax can operate in a way that takes away certain housing benefits. It is estimated that for fiscal year 2009, the loss in tax revenue from those tax advantages exceeded $207 billion.

III. CLASS AND HOMEOWNERSHIP TAX BENEFITS

A. Introduction

This part makes two primary points. First, who is a homeowner is a function of class. Second, who receives tax benefits for homeownership is a function of class. The greater a taxpayer's income, the more beneficial any tax deduction. The greater a taxpayer's income, the higher the likelihood that the taxpayer will be a homeowner. As we saw earlier, because the price of the tax deduction is included in the price of housing, federal tax policies, by increasing housing costs, make it harder for low-income taxpayers to become homeowners.

B. Homeownership Rates by Income Levels

Low-income homeownership rates have increased over the last decade. Between 1993 and 2000, the number of low-income homeowners grew by 79%.[42] As income rises, homeownership rates also rise.[43] Table 3.1 below provides a more complete picture.

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40. I.R.C. § 1221(a) 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) provides reduced rates for capital gains.

41. I.R.C. § 165(c)(3) (2007); Treas. Reg. § 1.165-9(a); *see* Treas. Reg. § 1.262-1(b)(4) (as amended in 1972).

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

43. Gale et al., *supra* note 13, at 1172.

TABLE 3.1[44]
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
$80–99,999	85.0
$100–119,999	88.7
> $119,999	92.1

Table 3.1 shows that once income reaches $30,000, the majority of all households are homeowners. When income reaches $80,000, 85% of all households are homeowners, and once income reaches $120,000, 92% of all households are homeowners. Given that tax deductions benefit taxpayers with the highest marginal tax rates, high-income households, which are most likely to be homeowners, are also the most likely to benefit from the tax subsidy. Homeownership has wealth implications as well.

All homeowners have 48% of their net worth represented by their homes. Low-income homeowners have 80% of their net worth represented by their homes and upper-income homeowners have 26% of their net worth represented by their homes.[45] Home equity, therefore, is a

44. *Id.* at 1174.

45. *See* Michael A. Stegman, Allison Freeman & Jong-Gyu Paik, Home Equity and Other Differences in the Wealth of Low-and Moderate-Income Homeowners: A Work in Progress 4 (Sept. 19–21, 2006) (draft Prepared for Presentation and Discussion at Federal Reserve Bank/CFED Asset Learning Conference, *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.").

significant part of low-income net worth, less significant for the typical non-low-income homeowner, and a very insignificant part of upper-income net worth. Put another way, low-income homeowners have virtually all of their net worth tied up in their homes, while upper-income homeowners have very little net worth tied up in their homes.

C. Tax Benefits and Class

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% 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% 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. This is true of every tax deduction; however, this is especially troublesome in the area of homeownership because, as we have just seen, owning a home is itself skewed by class.

All homeowners benefit from the exclusion from income for the rental value of their homes. But the higher your marginal tax rate, the greater your benefit. Low-income homeowners do not benefit as much as higher income homeowners. Deductions for housing tell a different story.

However, not everyone who owns a home benefits from the tax deductions for homeownership. Only taxpayers who itemize their deductions are eligible to receive the mortgage interest and real property deductions and *two-thirds of taxpayers do not itemize*.[47] Moreover, the mortgage interest deduction disadvantages low-income homeowners.[48]

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46. *See, e.g.*, James R. Follain & David C. Ling, *The Federal Tax Subsidy to Housing and the Reduced Value of the Mortgage Interest Deduction*, 44 NAT'L TAX J. 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. Richard Davies, *Standard Deduction Vs. Itemizing*, ABCNEWS.COM, Mar. 9, 2004, http://abcnews.go.com/Business/Taxguide/story?id=86114&page=1 ("If you're among the two-thirds of taxpayers who do not itemize . . ."); *see also* William G. Gale & 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." *Id.* They cite the following example:

> [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

Taxpayers who take the standard deduction on their tax returns reap no benefit from their mortgage interest payments, even though they have "paid" for them in the purchase price of their homes. The standard deduction is available for *all* taxpayers—regardless of whether they own homes. Since the Tax Reform Act of 1986,[49] low-income taxpayers are less likely to receive those benefits because they are less likely to itemize their deductions. Instead, these taxpayers take the standard deduction because it is a larger amount than their deductions and may not benefit from their mortgage interest payments.[50] Itemization is a function of how

> 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.

Id. at 1354 n.8; *see also* Edward P. Lazear & 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]."); NICOLAS P. RETSINAS & 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."). *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).

48. My previous scholarship has shown that certain provisions of the Internal Revenue Code disadvantage 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, *Pensions and Risk Aversion: The Influence of Race, Ethnicity, and Class on Investor Behavior*, 11 LEWIS & CLARK L. REV. 385 (2007) [hereinafter *Risk Aversion*] (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); Dorothy A. Brown, *Tax Treatment of Children: Separate But Unequal*, 54 EMORY L.J. 755 (2005) [hereinafter *Tax Treatment*] (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); 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); 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).

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

50. James R. Follain, David C. Ling & Gary A. McGill, *The Preferential Income Tax Treatment of Owner-Occupied Housing: Who Really Benefits?*, 4 HOUSING POL'Y 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 13, 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."); Francine J. Lipman, *Taxing Undocumented Immigrants: Separate, Unequal, and Without Representation*, 59 TAX LAW. 813, 839 n.187 (2006)

much the taxpayer actually spends versus how much the standard deduction is. The taxpayer will choose the greater amount, and—at lower income levels—it is typical that taxpayers spend less than the standard deduction. New homeowners are generally in low- or middle-income households that do not itemize.[51] On the other hand, middle- and upper-income taxpayers may have their mortgage interest and/or property tax deduction limited or eliminated by the alternative minimum tax.[52]

The two-thirds of taxpayers who do not itemize, however, is not what is important for our purposes. The percentage of taxpayers who are homeowners and still paying mortgage interest is the relevant taxpayer group. Slightly more than half (54%) of taxpayers who pay interest on their mortgages receive a tax benefit.[53] That means just under half (46%) of homeowners who pay mortgage interest do not receive a tax benefit from their interest payments. Yet, because the mortgage interest deduction is at least in part built into the price of the home, many low-income homeowners are paying for a tax benefit that they never receive.[54] The vast majority of taxpayers receiving the tax benefit are higher income taxpayers as table 3.2 below demonstrates.[55]

(citing WEST FEDERAL TAXATION: COMPREHENSIVE VOLUME 2–7 (Eugene Willis et al. eds., 2005) ("Although taxpayers can make an election to itemize their deductions in lieu of the standard deduction, approximately 70% of all taxpayers, including almost all low-income taxpayers, take the standard deduction.")).

51. Gale et al., *supra* note 13, at 1179.

52. *See, e.g.*, Linda M. Beale, *Congress Fiddles While Middle America Burns: Amending the Amt (And Regular Tax)*, 6 FLA. TAX REV. 811, 856 (2004) ("Various items must be recomputed for AMT purposes, including home mortgage interest . . . ."); Stewart E. Sterk & Mitchell L. Engler, *Property Tax Reassessment: Who Needs It?*, 81 NOTRE DAME L. REV. 1037, 1057 n.80 (2006) ("[T]he federal alternative minimum tax (AMT), which disallows the property tax deduction in certain cases."). The extent of the limitation is dependent upon a number of factors and is beyond the scope of this Article.

53. PRESIDENT'S ADVISORY PANEL ON FED. TAX REFORM, SIMPLE, FAIR, AND PRO-GROWTH: PROPOSALS TO FIX AMERICA'S TAX SYSTEM, FINAL REPORT 74 (2005), *available at* http://govinfo.library.unt.edu/taxreformpanel/final-report/index.html [hereinafter PRESIDENT'S REPORT]. One reason why taxpayers do not receive a tax benefit from their mortgage interest payments is because they do not itemize their deductions but take the standard deduction, which in their circumstances would be greater. *See* I.R.C. § 63 (2007).

54. Mathias, *supra* note 25, at 64 ("[T]he mortgage interest deduction is over-capitalized for some taxpayers . . . .").

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

TABLE 3.2[56]
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

Table 3.2 shows that only 2% of taxpayers with adjusted gross income (AGI) less than $15,000 receive a tax benefit from their mortgage payments. That means that 98% of taxpayers with an AGI less than $15,000 receive no tax benefit from homeownership. Furthermore, only 16% of taxpayers with an AGI between $15,000 and $30,000 receive a tax benefit from their mortgage interest payments. Similarly, 84% of taxpayers with an AGI between $15,000 and $30,000 receive no tax benefit from homeownership.

Only 34% of taxpayers earning between $30,000 and $40,000 receive a tax benefit from homeownership, which means 66% do not receive a tax benefit. For taxpayers with income levels between $40,000 and $50,000, 49% of taxpayers receive a tax benefit from homeownership, which means 51% also receive no benefit. Put another way, the vast majority of

56. PRESIDENT'S REPORT, *supra* note 53, at 74 (see figure 5.7). Similar results were obtained from a study based on nonfarm households in the 2004 Survey of Consumer Finances. *See* James Poterba & Todd Sinai, *Tax Expenditures for Owner-Occupied Housing: Deductions for Property Taxes and Mortgage Interest and the Exclusion of Imputed Rental Income*, 98 AMER. ECON. REV. 84, 85 (2008) (study shows: (i) 23% of homeowners in households with less than $40,000 of household income itemize; (ii) 66% of homeowners in households $40,000–74,999 itemize; (iii) 86% of homeowners in households $125,000–250,000 itemize; and (iv) 99.9% of homeowners in households greater than $250,000 itemize).

homeowners earning $50,000 or less do not receive tax benefits from their mortgage interest payments.

Table 3.2 shows that when AGI reaches $75,000, however, 90% of taxpayers receive the tax benefit of their mortgage interest payments.[57] Once AGI reaches $100,000, at least 97% of taxpayers receive a tax benefit from their mortgage interest payments. So taxpayers with AGIs of $100,000 as well as taxpayers with AGIs in excess of $1 million have the same percentage receiving tax benefits from their mortgage interest payments, namely 97%. Tax benefits for housing are overwhelmingly received by higher AGI households.[58]

Another way in which low-income homeowners do not benefit from federal tax policies that encourage homeownership is the way in which losses from the sale of personal residences are treated. Losses from the sale of personal residences are not allowed as deductions from income, the way losses from the sales of capital assets can be deducted—albeit to a limited extent—against ordinary income.[59] Many low-income homeowners sell their homes for less than what they paid for them.[60] Low-income homeowners do not remain homeowners like their higher-income counterparts and return to renting at extremely high rates.[61] Homeownership may be a poor asset for low-income individuals to invest in because of its low return when compared with other investments.[62] Gaining wealth from homeownership occurs from the sale of the second house (and subsequent houses).[63] Low-income homeowners who sell their first house and return to renting do not reap significant benefits from homeownership.[64] Low-income homeowners also do not benefit significantly from the exclusion from income for gain from the sale of their personal residences because they do not receive significant gains from these sales.[65]

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57. *Cf.* Steven Bourassa & William Grigsby, *Income Tax Concessions for Owner-Occupied Housing*, 11 HOUSING POL'Y DEBATE 521, 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 expenses.").

58. Gale et al., *supra* note 13, at 1177–78 (Study shows that "households in the lowest 60 percent of the income distribution obtain only 3 percent of the [mortgage interest deduction tax] benefits.").

59. *See* I.R.C. §§ 1211, 1212, 165(c) (2007).

60. Shlay, *supra* note 42, at 519.

61. *Id.* at 519–20.

62. *Id.* at 520 ("[E]ncouraging homeownership among low-income families will only increase the wealth gap in the United States.").

63. *Id.*

64. *Id.*

65. *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

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. (However, as described below, a tax deduction for rent would most likely result in higher rental prices).[66] Therefore, low-income taxpayers, regardless of race, are the most likely to be harmed by the non-deductibility of rent provisions in existing federal tax policy.

Finally, the exclusion for imputed rent benefits high-income households the most for two reasons. First, those at the highest marginal tax rate receive the greatest tax benefit from the exclusion (as they did from the deduction). Second, one would expect the amount of the imputed rent to be the greatest for the most expensive homes, which would be those owned by high-income homeowners.

D. Summary

Tax benefits are skewed towards higher-income taxpayers who would buy houses even without the tax subsidies. One reason is a function of our progressive tax rate structure, which makes deductions more valuable as income rises. Thus, there is more incentive for higher-income taxpayers to find deductions which federal tax laws permit. (Of course there is also an incentive for taxpayers to find exclusions which federal tax laws permit.) For example, the exclusion for imputed rental income significantly benefits higher-income taxpayers who are excluding more imputed rental income than their lower-income counterparts.

The most important way in which tax benefits discriminate against low-income homeowners is by disallowing deductions for mortgage interest if the taxpayer does not itemize. The low-income homeowner has purchased a home that is priced higher because the deduction is built into its price, yet he or she is prevented from taking the deduction because the tax laws do not permit non-itemized deductions for mortgage interest or property tax deductions.

Tax subsidies also benefit higher-income taxpayers because only homeownership is encouraged—not housing more generally. Homeownership has a built-in class bias: the more income you earn, the more likely you are to be able to afford and own a house. Therefore, tax policies for housing significantly benefit higher-income taxpayers. The

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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.").

66. *See infra* Part V.B.4.

overwhelming majority of low-income taxpayers who pay mortgage interest are not able to receive a tax benefit from homeownership. 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 eight times the benefit as those in the group making between $50,000 and $75,000.[67] Similarly, real property tax deductions only benefit taxpayers who itemize, and the greater their income, the greater the tax benefit received. However, at the higher income levels, the alternative minimum tax takes back some of the tax subsidy for the real property tax deduction.

Tax benefits exclude gains, but prohibit losses on the sale of homes. Low-income homeowners are most likely to sell their homes at a non-deductible loss. This is another way that housing tax benefits are skewed towards higher-income taxpayers.

IV. RACE AND HOMEOWNERSHIP TAX BENEFITS

A. Introduction

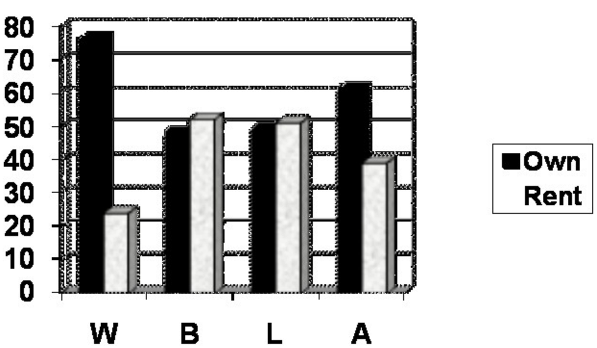
This part illustrates how being a homeowner is also a function of race, and in many instances, how race matters more than class. In order to be eligible for housing tax subsidies, a taxpayer must first be a homeowner. Data show that at every income level there is a greater percentage of white homeowners than black homeowners—even for middle- and upper-income black homeowners. Tax benefits that support homeownership benefit middle- and upper- income whites far more than middle- and upper-income blacks. This part will also show that most blacks live in majority/minority neighborhoods, which means that their homes are worth less than their white counterparts' homes. Further, black homes are generally older and of lower quality than their white counterparts' homes. This makes it likely that they will not receive the potential upside for appreciation that their middle- and upper-income white counterparts receive—unless they choose to live in overwhelmingly white neighborhoods.

67. Gale et al., *supra* note 13, at 1178.

B. Homeownership Rates by Race

Federal tax policy does not have as a goal the support and/or encouragement of affordable housing. If it did, there would not be a $1 million cap on mortgages, a subsidy for two homes, and rent would be deductible. Federal tax policy only encourages one type of housing—homeownership. (I am excluding from this discussion tax benefits for commercial real estate). This part begins by looking at renters by race/ethnicity to consider those ineligible for the tax benefits associated with homeownership.

CHART 4.1
PERCENTAGE OWNER/RENTER[68]



This chart shows that the majority of whites (76%) and Asians (61%) are homeowners, while the majority of blacks (52%) and Latinos (51%) are not. Therefore, the majority of blacks and Latinos are renters.[69]

68. *See* U.S. CENSUS BUREAU, SERIES NO. H-150-05, AMERICAN HOUSING SURVEY FOR THE UNITED STATES: 2005 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.

69. *Id.* Renters have significantly less wealth than homeowners. *See* RAKESH KOCHHAR, PEW HISPANIC CTR., THE WEALTH OF LATINO HOUSEHOLDS: 1996 TO 2002 20 (2004), *available at* http://pewhispanic.org/files/reports/34.pdf ("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).

Data show that black renters are more likely *not* to apply for a mortgage when compared with white renters.[70] Part of the explanation that has been proffered is that blacks fear rejection and therefore self-select not to apply for mortgages.[71]

Federal tax laws that disallow deductions for rent disadvantage blacks and Latinos because the majority of blacks and Latinos are renters. Federal tax laws (which benefit homeowners) advantage whites and Asians because the majority of those group members are homeowners. Housing is raced, therefore the tax benefits associated with housing are raced.

C. Homeownership by Race and Income

Since World War II, homeownership has created a vibrant middle class.[72] The twenty-first century has seen homeownership reach an all-time high with 69% of Americans owning their own homes.[73] Homeowners can build up equity over time through appreciation[74] and receive significant tax subsidies along the way.

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70. Charles & Hurst, *supra* note 14, at 288 ("[W]hite renters were more than twice as likely than black renters to apply for a mortgage.").

71. *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.").

72. *See, e.g.*, Shapiro, *supra* note 2, 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.") (citation omitted); Elizabeth Warren, *The Growing Threat to Middle Class Families*, 69 BROOK. 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); Adam Gordon, Note, *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).

73. *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.").

74. Elizabeth S. Anderson, *Integration, Affirmative Action, and Strict Scrutiny*, 77 N.Y.U. L. REV. 1195, 1203 (2002). Professor Anderson describes as follows:

> 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.

Unlike the post-World War II housing boom,[75] this recent homeownership boom included Americans of color. Black and Latino homeowners hold between 61% and 63% of their net worth in their homes and whites hold 38.5% of their net worth in their homes.[76]

President Clinton and President Bush encouraged homeownership opportunities for all.[77] Since 2002, the Bush administration touted a net increase of "nearly 3 million minority homeowners."[78] Financial industry executives have launched a "with ownership, wealth" initiative to encourage homeownership among minorities.[79] 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.[80]

Id. (citation omitted); Shapiro, *supra* note 2, at 68 ("Just as home ownership creates wealth for both whites and blacks, it simultaneously widens the racial wealth gap under current conditions.").

75. *See* IRA KATZNELSON, WHEN AFFIRMATIVE ACTION WAS WHITE 113–41 (2005) (describing governmental housing benefits that excluded blacks post-World War II from purchasing homes); Daria Roithmayer, *Locked in Segregation*, 12 VA. J. SOC. POL'Y & L. 197 (2004).

76. KOCHHAR, *supra* note 69, at 19.

77. *See* Michael Moss & Andrew Jacobs, *Blue Skies and Green Yards, All Lost to Red Ink*, N.Y. TIMES, Apr. 11, 2004, at N1, 34–35 ("Indeed, encouraging homeownership is one of the few issues the Clinton and Bush administrations pursued with equal ardor.").

78. *See* Alphonso Jackson, U.S. Sec'y of Housing & Urban Dev., Revitalization of Uptown (Aug. 7, 2007), http://www.nls.gov/news/speeches/2007-08-07.cfm ("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, Latinos Lag in Buying*, SAN ANTONIO EXPRESS-NEWS, 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.").

79. *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.").

80. *See* EMMA COLEMAN JORDAN & ANGELA P. HARRIS, ECONOMIC JUSTICE: RACE, GENDER, IDENTITY AND ECONOMICS 473–501 (2005) (describes wealth inequality in America); 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) ("A number of studies have documented black-white differences in asset ownership, particularly homeownership."); Spencer Overton, *But Some Are More Equal: Race, Exclusion, and Campaign Finance*, 80 TEX. L. REV. 987, 1004–12 (2002) (discussing racial differences in homeownership).

As chart 4.1 showed, whites are most likely to own their own homes (76%), followed by Asians (61%), Latinos (49%), and blacks (48%).[81] Race matters when it comes to being a homeowner. Being white makes you significantly more likely to own a home than if you are Asian, black, or Latino. (We saw in Part III that not all homeowners benefit. Low-income homeowners do not benefit to the extent of their middle- and upper-income counterparts).

Several studies show that most blacks prefer to invest in real estate, while most whites prefer to invest in the stock market.[82] One might expect, therefore, to see a higher percentage of blacks as homeowners than whites—yet we do not.

Even though Asians are more likely to be homeowners than blacks and Latinos, given that Asian median income is higher than white median income, we might expect to see even higher homeownership rates for Asians than whites—yet we do not.[83] Consider table 4.1 below, which examines homeownership rates for immigrants and native-born Asians and found vast differences between native-born Asians and immigrants in their rates of homeownership.[84]

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81. *See* Martin, *supra* note 78 ("The homeownership rate for Anglos is 74.3 percent, compared to 48 percent for African Americans and 47.6 percent for Hispanics. Some 53.7 percent of Asian Americans and other races owned their own homes, the Census data revealed."); KOCHHAR, *supra* note 69, 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.").

82. Brown, *Pensions*, *supra* note 48, at 1536 ("Black investors think that real estate is a better place to invest their money than either stocks or bonds.") (citations omitted); *see also* Anthony D. Plath & Thomas H. Stevenson, *Financial Services and the African-American Market: What Every Financial Planner Should Know*, 94 FIN. SERVICES REV. 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.").

83. *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.").

84. CHRISTOPHER E. HERBERT, DONALD R. HAURIN, STUART S. ROSENTHAL & MARK DUDA, U.S. DEP'T OF HOUS. & URBAN DEV., HOMEOWNERSHIP GAPS AMONG LOW-INCOME AND MINORITY BORROWERS AND NEIGHBORHOODS 126 (2005), *available at* http://www.huduser.org/Publications/pdf/HomeownershipGapsAmongLow-IncomeAndMinority.pdf.

TABLE 4.1[85]
HOMEOWNERSHIP RATES FOR IMMIGRANTS AND NATIVE-BORN ASIANS
(%)

Racial Group	All Households	Immigrants	Native Born
Japanese	63	40	82
Mainland Chinese	55	53	68
South Asians[86]	43	44	27
Koreans et al.[87]	39	39	29
Other Asians	57	56	61

Three observations are apparent from table 4.1—two of which are intra-racial and one is interracial. First, for Japanese, Mainland Chinese, and Other Asians, native-borns have a higher homeownership rate than immigrants. Second, South Asians and Koreans have a higher homeownership rate for immigrants than native-borns. Third, when the data from table 4.1 is compared with the data from chart 4.1, 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.[88] 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.[89] That data is consistent with the results of another study based on 2003 homeownership rates. Consider the data in table 4.2 below.

85. *Id.* (Source: 1996–1999 Current Population Survey).

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

87. This group includes those from Korea, Singapore, Taiwan, and Hong Kong. *Id.*

88. Kenya Covington & 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).

89. *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 4.2[90]
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 4.2. First, with the exception of whites in the $5,000–$9,999 households, at every other household income level, *the majority of whites are homeowners*. Perhaps one explanation for this is that whites are more likely to receive down payment assistance from family members than blacks.[91]

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

90. Gale et al., *supra* note 13, at 1174.

91. THOMAS SHAPIRO, THE HIDDEN COSTS OF BEING AFRICAN AMERICAN: HOW WEALTH PERPETUATES INEQUALITY 114 (Oxford University Press 2004); Charles & Hurst, *supra* note 14, 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 Kofi Charles & Erik Hurst, *The Correlation of Wealth across Generations*, 111 J. POL. ECON. 1155 (2003) (referring to study which showed that at any given wealth level, black households more likely had parents with lower net worth levels than white households).

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 are minimal. Perhaps black preferences for buying real estate are a factor here as well.

Latinos lag considerably behind blacks and significantly behind whites in their homeownership rates. For example, until household income reaches $25,000, whites were more than twice as likely as Latinos to be homeowners, but only at income levels of $5,000 or less were whites more than twice as likely as blacks to be homeowners. Even after controlling for a large number of observable factors, the black-white homeownership gap is smaller as income rises, but is never eliminated.[92] The gap was between five and ten percentage points.[93]

Table 4.2 shows that as income rises, so do homeownership rates—regardless of race—which means that class matters. Table 4.2 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, but no racial differences in homeownership rates among households with higher wealth.[94] Wealth may be the great equalizer to differences in homeownership rates, but the quality of housing is another question and the topic of the next part.

D. Homeownership Quality: The Ten Drop Rule[95]

This part will show that not all homeownership is created equal. Racially based wealth disparities in America are widely known and have been the subject of intense scrutiny.[96] Numerous proposals have been

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92. Gale et al., *supra* note 13, 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 . . . .").

93. *Id.* ("[the gap] still ranges between 5 and 10 percentage points . . . .") (citations omitted).

94. Charles & Hurst, *supra* note 14, 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.").

95. *Cf.* Ariela J. Gross, *Litigating Whiteness: Trials of Racial Determination in the Nineteenth-Century South*, 108 YALE L.J. 109, 178 (1998) ("Whereas most states before the Civil War had defined 'negro' according to fractions of 'blood'—usually one-eighth or one-fourth—many moved to one-drop-of-blood rules.").

96. *See, e.g.*, MELVIN OLIVER & THOMAS SHAPIRO, BLACK WEALTH/WHITE WEALTH: A NEW

made seeking to encourage blacks to buy homes as a way to decrease those wealth disparities. This Article argues that homeownership is increasing wealth disparities, in part due to federal tax policies.[97]

Blacks are more likely to buy homes that do not appreciate as much as white homes.[98] In addition, the resale value of white homes is greater than for black homes.[99] The reasons for this phenomenon are complicated.

Homes lose about 16% of their value when more than 10% of the neighborhood is black.[100] Blacks are more likely to live in majority/minority neighborhoods, and whenever a neighborhood is more than 10% black, property values decline.[101] The point at which the black percentage of residents becomes too high for white comfort is called the "tipping point."[102]

Whites do not want to live in neighborhoods with blacks, unless the percentage of blacks is very low.[103] Studies have not documented the same

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PERSPECTIVE ON RACIAL INEQUALITY (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).

97. *Cf.* Maury Gittleman & Edward N. Wolff, *Racial Differences in Patterns of Wealth Accumulation*, 39 J. 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.") (citations omitted).

98. *See* Rusk, *supra* note 4, at 2 ("In effect, for a dollar of income, black homeowners were getting only 70 percent of the home value that white homeowners received.").

99. Keister, *supra* note 80, at 479 ("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).

100. *See supra* note 2 and accompanying text. *Cf.* Richard D. Alba, John R. Logan & 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.").

101. *See supra* note 2 and accompanying text.

102. 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 BROOK. 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.").

103. *See, e.g.*, Gregory D. Squires, *Demobilization of the Individualistic Bias: Housing Market Discrimination as a Contributor to Labor Market and Economic Inequality*, 609 ANNALS AM. ACAD. POL. & SOC. SCI. 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

reaction by whites regarding Asians or Latinos.[104] 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.[105] As Nathan Glazer has noted, "the neighborhood that blacks would like, 50 percent black, is one that most whites would move away from, making it close to 100 percent black."[106]

White preferences will only allow a limited percentage of blacks (no more than 10%) to be eligible for the greatest housing appreciation.[107] Similarly, black preferences will result in blacks living in neighborhoods with a greater than 10% minority population and result in their being ineligible for the greatest housing appreciation. Research indicates that blacks prefer to live in integrated neighborhoods and not predominantly white neighborhoods because of racial prejudice and fears of white hostility.[108]

> there was a substantial representation of African Americans. The presence of Hispanics or Asians had no such effect (Emerson, Chai, and Yancey 2001).

Id.; *see also* R. Richard Banks, *"Nondiscriminatory" Perpetuation of Racial Subordination*, 76 B.U. L. REV. 669, 686–87 (1996) ("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); Maria Krysan & Reynolds Farley, *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).

104. Squires, *supra* note 103, at 206 ("The presence of Hispanics or Asians had no such effect . . . .") (citation omitted).

105. *See, e.g.*, John A. Powell, *Government Tax and Housing Policies*, *in* TAXING AMERICA 104 (Karen B. Brown & Mary Louise Fellows eds., 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.") (citations omitted). *Cf.* John O. Calmore, *Race/ism Lost and Found: The Fair Housing Act at Thirty*, 52 U. MIAMI L. REV. 1067, 1086 n.106 (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)." (quoting Martin Duberman, *Promised Land*, L.A. TIMES, Oct. 12, 1997, at 11 (book review))).

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

107. *Cf.* Alba et al., *supra* note 100, 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.").

108. Camille Zubrinsky Charles, *Neighborhood Racial-Composition Preferences: Evidence from a Multiethnic Metropolis*, 47 SOC. PROBS. 379, 380 (2000) ("Some research suggests that active racial prejudice plays a role in reproducing racial residential segregation.") (citations omitted); Maria Krysan & Reynolds Farley, *The Residential Preferences of Blacks: Do They Explain Persistent Segregation?*, 80 SOC. FORCES 937, 969–70 (2002). Authors Krysan and Farley draw the following four conclusions about why most blacks live in majority minority neighborhoods:

> First, the residential preferences of African Americans play a role in maintaining neighborhood segregation. . . . The preferred neighborhood for the typical black is one that is

There are primarily two explanations for why whites prefer not to live with blacks, and they may operate individually or in tandem.[109] The first is white aversion to minorities generally and the second is white fear (which given the data provided herein is rational) that when minorities move into the neighborhood, their property values will decline.[110] 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.[111]

Numerous studies have documented the black disadvantage in housing quality,[112] and housing values.[113] Blacks are more likely to purchase

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> about 50–50. Most American neighborhoods are overwhelmingly white, and so they are not considered attractive to many blacks.
>
> Second . . . African Americans are highly reluctant to buy or rent in largely white neighborhoods neither because they feel a strong allegiance to black communities nor because they wish their children to attend schools in a black environment. Rather, they want to live with other African Americans because they fear that they if they are one among many whites, whites will be hostile, blame them for any troubles that arise, and treat them as unwelcome intruders. . . .
>
> Third, . . . Blacks wish to reside in 50–50 neighborhoods, but that is far too high a density of African Americans for all but a handful of whites. Few blacks have the option to buy a home in a 50–50 place. . . .
>
> . . . .
>
> Finally, our findings emphasize the crucial role that white preferences continue to play in maintaining segregation. Whites' willingness to enter neighborhoods is strongly linked to the density of blacks there. As the suburbanization of African Americans continues, it is inevitable that some, perhaps many, neighborhoods will be written off by white home seekers as "too black."

Id.

109. *See, e.g.*, Bell & Parchomovsky, *supra* note 2, 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).

110. *See id.*

111. Richard Thompson Ford, *The Boundaries of Race: Political Geography in Legal Analysis*, 107 HARV. L. REV. 1843, 1854 n.24 (1994) ("Real estate brokers accused of steering prospective black buyers away from white neighborhoods consistently cite fear of reprisal by white property owners as the reason for the practice."); *see also* 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 away from the neighborhoods.").

112. Hayward Derrick Horton & Melvin E. Thomas, *Race, Class, and Family Structure: Differences in Housing Values for Black and White Homeowners*, 68 SOC. INQ. 114, 117 (1998) (citing Susan M. Bianchi, Reynolds Farley & Daphne Spain, *Racial Inequalities in Housing: An Examination of Recent Trends*, 19 DEMOGRAPHY 37–51 (1982)).

113. *Id.* at 118 (citing John F. Kain & John M. Quigley, *Housing Markets and Racial Discrimination: A Microeconomic Analysis*, NAT'L BUREAU OF ECON. RES. (1975); Marty R. Jackman & Robert W. Jackman, *Racial Inequality in Home Ownership*, 58 SOC. FORCES 1221 (1980); Robert

homes which are less valuable than their white counterparts.[114] That blacks fare less favorably from homeownership than whites is well-known and largely uncontested.

Typical studies show that value of black homes is smaller than the value of white homes.[115] White homes appreciate more quickly than black homes.[116] Black couples own less housing wealth due to low market values.[117] Blacks are often steered to buy homes in areas with declining home equity.[118] Professor Shapiro, a leading scholar on racial disparities in homeownership in America has said "[o]n average, homes owned by whites appreciate in value approximately $28,000 more than those owned by blacks."[119] On the other hand, real estate more quickly appreciates in overwhelmingly white neighborhoods than 20% black neighborhoods.[120]

Lake, *The New Suburbanites: Race and Housing in the Suburbs*, Rutgers Univ. Ctr. for Urban Policy Research (1981); MELVIN OLIVER & THOMAS SHAPIRO, BLACK WEALTH/WHITE WEALTH: A NEW PERSPECTIVE ON RACIAL INEQUALITY (1996)).

114. *See, e.g.*, Banks, *supra* note 103, at 686 ("It is well established that the slower appreciation rate of property in black areas disadvantages black homeowners.") (citations omitted); Francine D. Blau & John W. Graham, *Black-White Differences in Wealth and Asset Composition*, 105 Q. J. ECON. 321, 333 (1990) (discussing study showing "homes in black neighborhoods have much lower rates of appreciation than those in white neighborhoods."); *see also supra* notes 111–13, and *infra* notes 115–16.

115. *See* Charles & Hurst, *supra* note 14, 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.").

116. *See* Keister, *supra* note 80, at 479 ("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.").

117. *See* Mann, *supra* note 13, 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. INQ. 83, 95–97 (1992)).

118. *See* 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.") (citations omitted).

119. *See* Shapiro, *supra* note 2, at 68.

120. *See* 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.") (citation omitted). Further, Professor Strahilevitz states: "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." *Id.*

Blacks remain the most segregated group in America.[121] This has translated into different housing conditions for black homeowners when compared with white homeowners of comparable income levels.[122] 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.[123] White homeowners live with "very few black neighbors."[124]

Blacks of higher socioeconomic levels have not gained parity with their higher socioeconomic white counterparts.[125] The inequality in housing values between middle-class blacks and middle-class whites is greater than the housing inequality between their lower-status counterparts.[126] 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 potential because of discrimination they face in the housing market.[127]

Nevertheless, the benefits of homeownership to middle-class blacks are significant when compared to black renters. The data show that blacks are not buying homes because homes are a good financial investment, but rather because 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.[128] Even so, middle-class

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121. Horton & Thomas, *supra* note 112, at 118 (citing Douglas S. Massey, Gretchen A. Condran & Nancy A. Denton, *The Effect of Residential Segregation on Black Social and Economic Well-Being*, 66 SOC. FORCES 29 (1987); Nancy A. Denton & Douglas S. Massey, *Racial Segregation of Blacks, Hispanics, and Asians by Socioeconomic Status and Generation*, 69 SOC. SCI. Q. 797 (1988); Douglas S. Massey & Nancy A. Denton, *Hypersegregation in the U.S. Metropolitan Areas: Black and Hispanic Segregation along Five Dimensions*, 26 DEMOGRAPHY 373 (1989); Richard Alba & John Logan, *Variations on Two themes: Racial and Ethnic Patterns in the Attainment of suburban Residence*, 28 DEMOGRPAHY 431 (1991)).

122. *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.").

123. Alba et al., *supra* note 100, at 550.

124. *Id.* at 552.

125. Horton & Thomas, *supra* note 112, at 126.

126. *Id.*

127. *Id.* at 133.

128. Alba et al., *supra* note 100, at 556. Consider the following:

> 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.

Id.

blacks tend to live with white neighbors who are less affluent than they are (recall the Chris Rock story at the introduction).[129] Put another way, middle-class blacks live in neighborhoods that are not equal in affluence with their middle-class white counterparts.[130] Similarly situated white homeowners live in more affluent communities and suffer less crime than their black counterparts and even though middle-class black homeowners may fare better than black renters, they do not fare as well as middle-class white homeowners.[131] 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 off than neighborhoods of white renters.[132]

To summarize, the upside potential for housing appreciation exists to a far greater extent for middle- and upper-income white homeowners than the majority of black homeowners who live in majority/minority neighborhoods. This is due to several factors. First, the value of homes decrease any time there is more than 10% of black homeowners in a particular neighborhood. Second, whites prefer to live in overwhelmingly white neighborhoods. Third, blacks prefer to live in racially diverse neighborhoods.

E. Tax Benefits and Race

Federal tax subsidies for housing leave the majority of blacks and Latinos out because they rent and do not own their homes. Because rent payments are not deductible, those most likely to pay rent will not benefit. The majority of blacks and Latinos are renters, and therefore, are the most likely to be harmed by the disallowance of rent payment deductions. Whites and Asians are most likely to be homeowners and not renters, and therefore do not pay the same "penalty."

Previous scholars have argued that blacks and Latinos benefit significantly from the tax subsidies for housing (even though whites

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129. *Id.* at 544 ("However, [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.").

130. *Id.*

131. *Id.* at 556 ("[A]t 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.").

132. Shlay, *supra* note 42, at 520.

benefit more).[133] 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 and/or exclude gain. If they are not, then even though a significant percent are homeowners, they will not benefit from the tax subsidies for housing.

Given that only taxpayers who itemize deductions receive the benefit of the deductions, and since there is a greater percentage of white middle- and upper-income homeowners than black or Latino middle- and upper-income homeowners, I would predict that white homeowners are more likely to benefit from the itemized deduction associated with the mortgage interest deduction than blacks or Latinos.

Interestingly, a few geographically targeted studies have shown that homes in majority/minority neighborhoods are assessed at higher effective rates for property tax purposes than similar property in majority/white neighborhoods.[134] If those findings were replicated on a nationwide scale, then once again we would see blacks and Latinos paying more for their housing costs than whites.

Housing appreciation upon sale is excludable up to $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. 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 without risking the potential for housing appreciation for everyone.

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 must remain overwhelmingly

133. *See, e.g.*, Mann *supra* note 13, 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); Moran & Whitford, *supra* note 23, 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.").

134. *See* Lee Harris, *'Assessing' Discrimination: The Influence of Race in Residential Property Tax Assessments*, 20 J. LAND USE & ENVTL. L. 1 (2004) (describing author's study of homes in New Haven, Connecticut). *Cf.* Richard Delgado, *Home-Grown Racism: Colorado's Historic Embrace—and Denial—of Equal Opportunity in Higher Education*, 70 U. COLO. L. REV. 703, 720–22 (1999) (describing events from the early twentieth century in Colorado). "Mexican Americans lost eighty percent of their original land grants, some to conniving lawyers and land developers, others because of high property taxes imposed on Mexican-American owners—in some cases five times higher than those paid by their Anglo neighbors." *Id.* at 721 (citations omitted).

white. Put another way, there is a cap on the percent of black homeowners who can live in substantially white neighborhoods and benefit the most from housing (Not everyone can be Chris Rock—in fact according to him, only three others are like him in his neighborhood). The argument can be made that having gain that is excluded is better than having 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 significant appreciation.

While all homeowners benefit from the exclusion for imputed rent, regardless of race, those in the most desirable neighborhoods benefit the most. These homeowners 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. These homeowners (most likely black and Latino) are likely to be living in any neighborhood with more than 10% black neighbors—mainly black homeowners.

F. Blogosphere Attention

In the course of presenting earlier drafts at numerous venues, there have been blog postings about this Article. This part will describe the posts and my reactions in turn.

The first blog post was a result of my serving as a panelist at the Section on Taxation's program at the Association of American Law Schools' annual convention in San Diego on Thursday, January 8, 2009.[135] The blog entry was written by Professor Neal Buchanan and entitled "Helping the Non-Rich, by Accident."[136] Professor Buchanan observes that homeownership is a very bad way to save money. He, of course, ignores how the white middle class was created post-World War II in part due to homeownership. He also ignores the very real advantages of homeownership, which flow from having home equity.

Home equity can be used to send your children to college or provide them with a down payment for their own home, or, at death, it can provide them with a home outright, perhaps mortgage-free. Professor Buchanan

135. *See* Audio recording: The Family and Taxation, American Association of Law Schools, AALS 2009 Annual Meeting (Jan. 8, 2009), http://www.aals.org/events_am2009.php (follow "-Podcasts-" hyperlink; then follow "Sessions" hyperlink; then follow "Taxation" hyperlink). The panelists were, in addition to myself: Anthony Infanti; Lily Kahng; Marjorie Kornhauser (moderator) and Dennis Ventry.

136. *See* Posting of Neal H. Buchanan to Dorf on Law, http://michaeldorf.org/2009/01/helping-non-rich-by-accident.html (Jan. 15, 2009, 12:01 EST).

also ignores the forced savings function of having a mortgage. Each of these benefits is available to whites in a way currently unavailable to blacks, and tax laws make things worse not better. Yet, Professor Buchanan's paternalistic argument is that the extent to which low-income homeowners are disadvantaged under the current law is acceptable because "a tax system that leaves out the low-income taxpayers is actually doing them a favor by not encouraging them to own a home."[137]

The fallacy of Buchanan's argument is that since Congress says that tax subsidies are designed to encourage homeownership, then we cannot exclude low-income taxpayers who are striving for a better life for their families, nor can we exclude blacks who have been excluded from homeownership by the government for far too long. The government should provide help for all and be a hindrance for none.

The second post was a result of my participation in New York University School of Law's Spring 2009 Tax Policy Colloquium co-organized by Professors Daniel Shaviro and Alan Auerbach on February 12, 2009. The post occurred the next day.[138] Professor Shaviro argues that whites do not benefit from homeownership because tax subsidies are built into the price of their homes, which are then deducted.[139] In effect, all homeowners, regardless of race, get what they pay for. They have received no benefit. This argument, however, misses the mark on several fronts.

First, Professors Shaviro and Auerbach missed a key point I tried to make in the draft; namely, the racial disparity in housing appreciation received by black and white homeowners. Their primary critique was based on the assumption that all tax subsidies are built into the purchase price. Professor Shaviro then states that whites are only getting what they pay for after tax and are not receiving a benefit.[140] Professor Auerbach similarly assumes that in this instance housing depreciation is built into the price. He also states that blacks are getting a greater exclusion for imputed rental income as a percent of purchase price when compared with their white counterparts who actually paid more money for their homes. I will respond to each in turn.

I have never seen any study suggesting that future housing appreciation (or depreciation) from a future sale is built into the purchase price the way the tax deductions for the mortgage interest are, nor have Professors

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137. *Id.*

138. *See* Posting of Dan Shaviro to Start Making Sense, http://danshaviro.blogspot.com/2009/02/tax-policy-colloquium-on-dorothy-browns.html (Feb. 13, 2009, 8:28 EST).

139. *Id.*

140. *Id.*

Shaviro or Auerbach cited to any such study. Given market fluctuations, I would be curious as to how this would even be possible. There is no serious basis for assuming that housing appreciation (or depreciation) is built into the purchase price and, as a result, whites who get more appreciation have in fact received something they did not pay for. In reality, they receive untaxed wealth that their black counterparts do not have access to simply because their neighbors are white. Given the uncontroverted evidence that housing appreciation in predominantly black neighborhoods is significantly less than housing appreciation in overwhelmingly white neighborhoods, whites benefit from homeownership appreciation in ways that blacks do not.

Professor Auerbach suggests that the lack of housing appreciation may lower the purchase price, which would enable the homeowner to receive a higher exclusion for the imputed rental value than if the higher appreciation were built into the price. Again, Professor Auerbach is making the argument that the market prices homes with the appreciation—or depreciation—built into the price without a single citation in support of his assertion. What is all the more bothersome about this line of argument is the notion that it is somehow a good thing that the price of a home in a predominantly black neighborhood is lower relative to their white counterparts. The price is lower, but the value of the exclusion for imputed rental income is a greater percentage of the purchase price when compared with the value of the same exclusion for a white homeowner in a higher-valued home. Therefore, blacks benefit more than whites from the exclusion. If Professor Auerbach is right, then we should see a rush to the market to buy older homes in predominantly black neighborhoods. I should want to buy the worst house on the worst block, in a predominantly black neighborhood so my purchase price would be really low, because then the exclusion for the rental value would be a huge percentage of the purchase price. Yet, the reality is, all other things being equal, we do not want to buy that house. We want the homes with the most appreciation possible, because up to $500,000 of the appreciation is excluded. Although the imputed rental income may be a higher percentage of the purchase price for the typical black homeowner, the Internal Revenue Code does not exclude imputed rental income based on its percentage of the purchase price, but value of the home. Thus, Professor Auerbach's argument is unpersuasive. Whites' homes are more valuable and the exclusion is worth more to those homeowners because the imputed rental income is higher.

I never cease to be amazed at the mental gymnastics tax law scholars go through in their quest to show that the tax laws do not benefit whites when they obviously do.[141] For instance, Professor Zelenak argues that blacks benefit from tax law because welfare benefits are excluded from taxation.[142] (To the extent that there are more whites than blacks on welfare, whites will benefit more from the exclusion.) Professor Zelenak and others argue that the progressive tax rate structure is anti-white (or pro-black).[143] Something happens to reasonably intelligent tax academics when race is thrown into the mix.

Professor Livingston describes tax professors as conservative.[144] Who can seriously argue that because welfare is not taxed, the poor receive a tax benefit and are the beneficiaries of a progressive tax rate? Would you rather be poor and pay very little in taxes or be rich and pay very little in taxes? In other words, would you rather be Warren Buffett (even when he is having his worst year ever[145]) or poor? In 2006, Warren Buffet noted that his tax rate was 17.7% on $46 million of income. He did not pay tax at the maximum 35% on the majority of his income. He is the typical, rich beneficiary of our progressive tax rate structure. So, if I have the choice between being poor and paying less in taxes or being Warren Buffet and paying less in taxes, I would want to be Warren Buffet.

141. *See* Brown, *Tax Treatment*, *supra* note 48, at 808–17 (describing race and gender composition of tax law professors at American law schools and their difficulty dealing with race questions). The disparity in treatment between wages and payments to hedge fund managers could change as the Obama administration's recent budget included a plan to tax hedge fund managers at the maximum progressive tax rate.

142. *Id.* at 804 ("Professor Zelenak continues by speculating about 'other likely candidates' in the tax code that are pro-Black. They include the exclusion from income of welfare-type benefits.") (citation omitted).

143. *Id.* (Zelenak writes about "tax code provisions that are anti-White . . . includ[ing] . . . 'progressive marginal rates' . . . . Professor Bryce states '[t]he Code discriminates against whites. The progressive rate structure results in whites paying most of the federal income tax."). I was once told, in an audience of my peers, at the Annual Meeting of the Association of Law Schools that my work was irrelevant because everyone knows that blacks benefit from the progressive tax rate structure because they are poor and do not pay a lot of taxes.

144. *See* Michael A. Livingston, *Reinventing Tax Scholarship: Lawyers, Economists, and the Role of the Legal Academy*, 83 CORNELL L. REV. 365, 393 (1998) ("[T]ax professors have always been a conservative lot.").

145. David Segal, *In Letter, Buffett Accepts Blame and Faults Others*, N.Y. TIMES, Mar. 1, 2009, at A16 ("The renowned investor Warren E. Buffett chided himself and the business world at large in his annual letter to shareholders of his holding company on Saturday as he sifted through the wreckage of his worst year in four decades.").

G. Summary

Federal tax laws that encourage homeownership benefit whites. The overwhelming majority of whites at virtually every income level (with the exception of $5,000–9,999) are homeowners. Most blacks and Latinos are renters and thus ineligible for any tax subsidies for their housing expenses. Most whites and Asians are homeowners and therefore eligible to receive tax subsidies. The tax subsidies tend to benefit more expensive homes and taxpayers subject to the highest marginal tax rates. Those homeowners are largely middle- and upper-income white homeowners.

Finally, 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.

V. RACE- AND CLASS-BASED SOLUTIONS: ENCOURAGING HOMEOWNERSHIP FOR ALL

A. Introduction

At present, federal tax policies reinforce the race- and class-based discrimination faced by homeowners. This part proposes changes to federal tax policy, which, if adopted, would disrupt this race- and class-based discrimination.

Previous scholars have addressed the race and/or class aspects of mortgage interest deductions—some more successfully than others. However, no proposal addresses both the race and class dimensions of the problem. One proposal would convert real property and mortgage interest deductions into a credit which would begin to be phased out when income on a joint return reaches $50,000.[146] That amount was chosen because "most black families earn less than $50,000."[147]

That the credit proposal was nonrefundable means it will not be available to blacks with no income tax liability, but will be available to

146. Moran & Whitford, *supra* note 23, at 781. The authors, however, retain the exclusion from gain. This seems consistent: they would have a limitation on gain that is excluded the same way they propose to phase out the mortgage interest and real property deductions once joint income reaches $50,000.

147. *Id.* at 781 n.110 ("Only six percent of black families have incomes greater than $50,000.") (citation omitted).

those who are subject to significant social security withholding. Even if there is a minority of blacks earning more than $50,000, according to table 4.2 *supra*, only at income levels above $60,000 do significant percentages of blacks (70%) become homeowners. So while the $50,000 income level may tell us something about most blacks, it does not tell us much about most black *homeowners*. To take away the mortgage interest deduction would be to take away tax benefits from a significant percentage of black homeowners.[148]

Another proposal would create a credit called the shelter credit.[149] It leaves open the possibility that the credit would be refundable.[150] The shelter credit would have two parts. The first part would "encourage the purchase of a median-priced home."[151] The second part would increase the amount of the credit for homes located close to public transportation as a way of reducing sprawl.[152] That the proposal leaves open the possibility of a refundable credit would benefit low-income homeowners; however, the proposal did not address racial disparities in the homeownership market.

While the proposals are novel in that they attempted to address race or class disparities in the tax laws, which support homeownership, I do not believe either was truly comprehensive. Class reform can only be addressed with a refundable credit. Nonrefundable credits will not be available to low-income taxpayers whose income tax liability is completely offset by the earned income tax credit (EITC). Also, limiting the deduction for blacks who make more than $50,000 seems unhelpful given the data presented in table 4.2 showing the high percentages of blacks and Latinos who are homeowners once household income reaches $50,000.

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148. *Cf.* Wilton Hyman, *Race, Class, and the Internal Revenue Code: A Class Based Analysis of* A Black Critique of the Internal Revenue Code, 35 CAP. U. L. REV. 119, 150 (2006). Professor Hyman wrote:

> Professors Moran and Whitford's recommendation to eliminate the home mortgage interest and property tax deductions and replace them with a tax credit would harm the interests of middle-income taxpayers . . . . [F]or blacks and whites with household income greater than $50,000, their home ownership rates were seventy-five percent and eighty-five percent, respectively, reflecting the relationship between rising incomes and home ownership rates. Eliminating the home ownership tax provisions would harm the interests of those blacks most able to utilize them and would impair the ability of many blacks to acquire their most significant asset.

Id. (citations omitted).

149. Mann, *supra* note 13, at 1394–96.

150. Another proposal by Professor Peter Dreier would call for converting the mortgage interest deduction into a refundable homeowner tax credit. Mann, *supra* note 13, at 1394.

151. *Id.* at 1394.

152. *Id.* at 1395.

B. Solutions to End Race and Class Discrimination

This part provides three different proposals (however, the refundable credit solution is similar to that discussed above), which are designed to decrease the race and class discrimination experienced by homeowners under current tax law. The first two proposals address the class-based discrimination and the third proposal addresses the race-based discrimination currently operating in the housing market.

The first proposal would change existing deductions into refundable credits. Then-Senator Obama's Tax Plan provided for a refundable credit in place of the mortgage interest deduction, which is designed to benefit low- and middle-income homeowners who cannot currently itemize their deductions.[153]

The second proposal 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. This part concludes by arguing that federal tax policy—which is currently discriminating against low-income homeowners and middle- and upper-income black 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 do not itemize.[154] 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

153. BOB WILLIAMS, LEN E. BURMAN, SURACHAI KHITATRAKUN, JEFF ROHALY, GREG LEISERSON & ERIC TODER, TAX POL'Y CTR., AN UPDATED ANALYSIS OF THE 2008 PRESIDENTIAL CANDIDATES' TAX PLANS: REVISED AUGUST 15, 2008, UPDATED SEPTEMBER 12, 2008 (2008), http://www.taxpolicycenter.org/publications/url.cfm?ID=411749.

154. PRESIDENT'S REPORT, *supra* note 53, at 73–75.

from the government, allowing them the full benefits that their middle- and upper-income counterparts already enjoy.[155]

As I have written elsewhere, making a credit refundable is politically perilous.[156] The earned income tax credit, a refundable credit that has been analogized to "welfare," and the attendant racial politics that accompany that debate could become a part of this discussion.[157] 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,

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155. *Cf.* Lily L. Batchelder, Fred T. Goldberg, Jr. & 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.") (citations omitted).

156. Brown, *Race and Class Matters*, *supra* note 48, at 816–19 (describing how earned income tax credit (EITC) recipients are viewed as receiving "welfare" because of the refundable nature of the EITC). *But see* Dennis J. Ventry, Jr., *Welfare By Any Other Name: Tax Transfers and the EITC*, 56 AM. U.L. REV. 1261, 1274 (2007) (author argues that "[t]hese attacks on low-income taxpayers and their tax-transfer benefits are serious. But doomsayers overstate the threat. The EITC is neither in danger of being 'repealed outright' nor 'headed for extinction.' This is not 1994 when the Republican Contract with America explicitly associated the EITC with the old welfare regime.") (citations omitted). What Professor Ventry ignores, however, is the cyclical nature of the racial politics surrounding welfare discourse in America. For example, in the 2008 presidential campaign there were numerous examples where refundable credits proposed by Senator Obama were referred to as welfare. *See, e.g.*, E.J. Dionne Jr., *Bottom-Up? The Campaigns Finally Begin A Serious Debate On The Economy*, PITTSBURGH POST-GAZETTE, Oct. 31, 2008, at B7 ("Mr. McCain has argued that Mr. Obama's refundable tax credits amount to 'welfare.' That, too, is a strange claim, since Mr. McCain favors refundable credits as part of his health plan. But the whole idea is to persuade voters such as Emily Daywalt that Mr. Obama really is just out to help those 'who don't do anything.'"); Steven Greenhouse, *For Incomes Below $100,000, a Better Tax Break in Obama's Plan*, N.Y. TIMES, Oct 31, 2008, at A14 ("Helped by the emergence of Joe the Plumber and using Mr. Obama's own words, Mr. McCain has insisted that Mr. Obama's tax policies would hurt small businesses and upwardly mobile individuals, while providing welfare for low-income Americans."); Janet Hook, *A liberal use of the word?; McCain's Efforts to portray Obama as far left obscure subtleties in the Democrat's policies*, L.A. TIMES, Oct. 24, 2008, at A1 ("About 40% of workers do not make enough to pay income taxes. Obama argues that they deserve relief because they pay other levies, such as payroll taxes, which fund Social Security and Medicare. McCain says the cash payments to these earners would be tantamount to welfare. A recent campaign Internet ad charges: 'Obama raises taxes on seniors, on hard-working families, to give 'welfare' to those who pay none.'"); Jeanne Kilgore, *Most people don't know what 'socialism' is*, THE CINCINNATI ENQUIRER, Nov. 3, 2008, at 6B ("It is Obama who says he wants to give 95 percent of the taxpayers a tax cut. But if 40 percent don't pay taxes, how can they get money? By increasing the rate on top earners and sending that money to those that pay nothing is his plan. Not a one-time stimulus bonus, but an every year payment. That is welfare, that is adjusting the wealth, that is socialism."); Debra J. Saunders, *Questions About Obama*, S.F. CHRONICLE, Oct. 30, 2008, at B7 ("The Tax Policy Center also estimates that, under Plan Obama, 49 percent of Americans will not pay federal income taxes. So when Obama talks up his plan to send a $500 to $1,000 "rebate" to American taxpayers, he is talking welfare."). The racial politics surrounding the word "welfare" ebbs and flows over time and it is overly optimistic for anyone to declare victory.

157. Brown, *Race and Class Matters*, *supra* note 48, at 816–19.

because the poor are typically perceived as black.[158] 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.[159]

This proposal is especially important to the extent that low-income taxpayers are purchasing homes and not benefiting from the mortgage interest deduction, even though the tax benefit is included in the price of the homes they are purchasing. Put another way, the call to convert deductions into refundable credits is especially strong here—where assets are priced assuming a tax deduction, which is not available to a significant percentage of low-income homeowners.

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 the sale of personal residences by 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, capital loss deductions 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.[160] Assuming that low-income households are less likely to have capital gains, allowing the loss only to offset gains will not help these taxpayers very much. Therefore, I would allow the loss to offset ordinary income to a greater extent than just $3,000, as provided by current law.[161] During the 2008 presidential campaign, Senator McCain suggested increasing the amount of loss on the

158. *Id.* at 813 ("American opposition to welfare is due to the public perception that the typical welfare recipient is undeserving. They are undeserving because Americans believe that most welfare recipients are black . . . .").

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

160. *See* I.R.C. §§ 1211 and 1212 (2007).

161. Professor Richard Epstein suggested years ago that the proper way to account for losses on the sale of a personal residence would be to reduce the basis by the amount of allowable depreciation (if depreciation were permitted on personal residences) and calculate the difference between that basis and the amount realized to determine if there was a loss on sale and to recognize that loss. Richard Epstein, The *Consumption and Loss of Personal Property Under the Internal Revenue Code*, 23 STAN. L. REV. 454, 457–62 (1971). Professor Epstein did not limit his suggestion to low-income homeowners, however. I would like to thank Professor Dan Shaviro for referring me to this article.

sale of stock that could be used to offset ordinary income to $15,000.[162] That may be a place to start in thinking through this proposal.

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 10% black homeowners. This is not a solution designed to encourage integration but one designed to address the market penalty paid by all homeowners in neighborhoods with more than 10% black neighbors. This solution would not be required if the market placed a premium on segregation where black majority neighborhoods were worth what white majority neighborhoods are worth—a form of "separate but equal" housing price discrimination.

But how the housing market operates is that black majority neighborhoods are penalized simply because "too many" blacks live there. This proposal seeks to compensate homeowners regardless of race in majority/minority neighborhoods for the market rate penalty they face. This proposal is not intended to encourage anyone to move. It is solely designed to compensate homeowners currently subject to the "cap" on appreciation and not to encourage integration.

The credit would apply to both mortgage interest deductions and real property tax deductions. The refundable credit would only be available to homeowners who purchased homes after the proposal was enacted, in neighborhoods with more than 10% black homeowners.[163] Any homeowner, regardless of race, would be eligible for the credit. The market discrimination—which currently penalizes homeowners where their neighbors are more than 10% black—would be minimized, if not eliminated. Therefore, homes in neighborhoods with more than 10% black neighbors should be priced at a premium if this proposal were adopted. This proposal would also encourage whites who were not interested in

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162. *See, e.g.*, Jane Sasseen, Moira Herbst, Phil Mintz, Catherine Arnst & Theo Francis, *Election 2008: McCain on the Economic Issues; Republican Presidential nominee Senator John McCain on taxes, jobs, education, health care, the financial crisis, and retirement*, BUS. WK. ONLINE, Oct. 28, 2008 ("[McCain] proposed raising the amount investors can deduct from $3,000 of capital losses to $15,000 for 2008 and 2009.").

163. *Cf.* John Charles Boger, *Toward Ending Residential Segregation: A Fair Share Proposal For The Next Reconstruction*, 71 N.C. L. REV. 1573, 1574 (1993) ("As a disincentive, this legislation would modify the federal tax code so that property holders in municipalities that choose to ignore their prescribed housing goals would progressively lose their mortgage interest and property tax deductions."). I thank Dean Boger for referring me to his prior article.

living in homogeneous communities to move to racially diverse areas who do not do so for fear of a drop in their home property values.

In addition, the tax provision would sunset in twenty-five years with a statutory requirement to study the marketplace impact of the credit every five years. A sunset of twenty-five years was selected because Justice O'Connor, in upholding the University of Michigan Law School's use of race as a factor in admissions decisions, wrote, "We expect that 25 years from now, the use of racial preferences will no longer be necessary to further the interest approved today."[164] Many commentators have suggested that Justice O'Connor was stating that the constitutionality of race-based remedies turns upon whether they are time limited.[165]

The question must be addressed whether such a proposal would pass constitutional muster especially in light of recent Supreme Court precedent.[166] A full-blown constitutional analysis is not only beyond the scope of this Article, it is beyond the scope of my expertise. My initial thoughts, however, follow.

This proposal seeks to remedy the raced-based market penalty for majority black neighborhoods that do not exist in majority white neighborhoods. As Justice Kennedy acknowledged in *Parents Involved*, "neighborhoods in our communities do not reflect the diversity of our Nation as a whole."[167]

The strongest argument in favor of the proposal's constitutionality is that it is a remedy to the federal government's past history of intentional race-based discrimination in the housing market. Current market conditions are a direct result of government discrimination. During the 1940s and 1950s, the Federal Housing Administration issued mortgage insurance on about a third of new homes and the rate of home ownership increased from 44% in 1940 to 62% in 1960.[168] Until 1950, however, both the FHA and the Veterans Administration required that neighborhoods be racially segregated in order to receive mortgage insurance.[169] The FHA's

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

165. *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).

166. *See, e.g.*, Parents Involved in Cmty. Schools v. Seattle School Dist. No. 1, 551 U.S. 701 (2007).

167. *Id.* at 2797 (Kennedy, J., concurring). I thank Professor Sam Bagenstos for suggesting that I look to Justice Kennedy's concurrence for support for my proposal.

168. *See* ANDREW WIESE, PLACES OF THEIR OWN: AFRICAN AMERICAN SUBURBANIZATION IN THE TWENTIETH CENTURY 100–01 (2004).

169. *Id.* at 101 ("As late as 1950, however, both agencies required that neighborhoods be racially

Underwriting Manual included samples of racially restrictive covenants.[170] Only 2% of the homes built with FHA support since World War II were occupied by minorities, by the late 1950s.[171]

Racially restrictive covenants were legal until 1948.[172] The FHA and Veteran's Administration policies excluded blacks from benefiting from homeownership for decades.[173] The FHA did not offer full-throated support for integrated housing until after the passage of the Fair Housing Act in 1968.[174] Although the government may have stopped actively discriminating on the basis of race, they did nothing to compensate blacks and other minority group members for the consequences of decades of intentional governmental race-based discrimination. Government action not only denied prospective homeowners of color the ability to buy a home because of their race, it resulted in housing wealth not being accumulated by those families, and that wealth disparity continues until this very day.

While a full-blown constitutional analysis is outside the scope of this Article (even were we to find it constitutional), there are still several questions that remain. Is it politically viable? What is a neighborhood? How do we treat cities or states with overwhelmingly white populations? What does a racially diverse neighborhood look like? Should it be any neighborhood where more than 10% of blacks own homes—including a 100% minority neighborhood?

Turning to the proposal's impact, one could predict that homes in "racially diverse" neighborhoods would increase in value and homes in non-racially diverse neighborhoods would decrease in value.[175] Even

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segregated in order for homes to qualify.").

170. *Id.*

171. *Id.*

172. Shelley v. Kraemer, 334 U.S. 1 (1948).

173. *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.

Id. (citations omitted).

174. *See* WIESE, *supra* note 168, at 129.

175. I will point out that white homeowners are most likely to be able to absorb such a loss in net

though I am not suggesting the repeal of the current deductions for existing homes, these homes would no longer be as attractive to new purchasers since new purchasers could not receive tax benefits unless they moved into "racially diverse" communities. The price—which previously included the tax deduction—would at least fall by that amount, because the house was no longer eligible for the tax deductions.

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, e.g., Chris Rock. 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. Low-income, overwhelmingly white neighborhoods might have a more arduous task than that faced by higher-income, homogeneous white neighborhoods because of the differences in neighborhood amenities.

Perhaps one alternative scenario is that whites decide to forego their tax benefits as the price they pay to live in homogeneous communities. I am reminded of Derrick Bell's fictional Racial Preference Licensing Act, which would permit whites to discriminate, but they would have to pay "a tax" for the ability to do so.[176] Whites would make the conscious choice to purchase homes in overwhelmingly white neighborhoods—which would now be less valuable because they no longer include the benefit of the tax deduction. If that were the outcome, then we certainly would not be any worse off than we are under current circumstances; however, the majority of black homeowners would be better off.

4. Solutions Rejected

If I were writing on a clean slate, my preference might be to repeal the deductions and exclusions for housing. My hesitation is due to the race and class impact that repeal may have on the net worth of existing low-income and black and Latino homeowners.

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wealth because they are most likely to have net worth from a variety of different sources. *See* KOCHHAR, *supra* note 69, at 19 (showing that while 61% of mean net worth is found in Latinos' homes and 63% is found in black homes, only 38.5% is found in white homes with 21.9% of white mean net worth coming from stock ownership.).

176. *Cf.* DERRICK BELL, FACES AT THE BOTTOM OF THE WELL: THE PERMANENCE OF RACISM 47–64 (1992).

CHART 5.1 MEAN NET WORTH BY SELECTED ASSET TYPE[177]

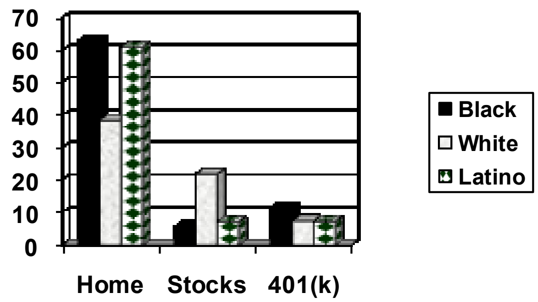

Chart 5.1 tells us that 61% of the value of mean net worth is found in Latinos' homes, while 63% is found in black homes, but only 38.5% is found in white homes. The total mean net worth for whites is $221,871, followed by $65,371 for Latinos, and $45,711 for blacks.[178] So, even though the greatest percentage of homeownership net worth is found in the black community, blacks have the lowest mean housing net worth.

Chart 5.1 also shows that a significantly larger percentage of white mean net worth is found in their ownership of stocks (and mutual funds) than that found in black and Latino households. Whites have 21.9% of their mean net worth coming from stock ownership, whereas Latinos have 7.2% of their mean net worth and blacks have 5.6% of their mean net worth coming from stock ownership. Finally, chart 5.1 shows us that blacks have 11.5% of their mean net worth coming from 401(k) accounts, followed by whites with 7.4%, and Latinos with 7.3%. The data on 401(k) accounts should not be confused with employer-provided pension plans, which are not covered in this chart. As I have written previously, blacks, Latinos, and Asians are less likely to participate in employer-provided pension plans[179]—and if they do participate, more likely to have lower balances at retirement.[180]

177. KOCHHAR, *supra* note 69, at 2 ("The percentage of White households who owned homes in 2002 was 74.3 percent. The homeownership rates for Hispanic and Black households were 47.3 percent and 47.7 percent respectively.").

178. *Id.* at 19.

179. Brown, *Pensions*, *supra* note 48; Brown, *Risk Aversion*, *supra* note 48.

180. Brown, *Pensions*, *supra* note 48; Brown, *Risk Aversion*, *supra* note 48.

The stock market is considered, over the long term, to be the investment with the greatest returns.[181] While this may seem largely academic in the current market, the point is not to be missed. Over the long term, returns on investing in the stock market have proven to be greater than all other alternative investments.

To the extent that blacks and Latinos invest less in the stock market than whites do, their wealth will differ significantly—regardless of income level.[182] Black investors think that real estate is a better place to invest their money than either stocks or bonds.[183] Blacks also think insurance policies are good investment vehicles.[184]

One study shows that, for the lowest-income homeowners, home equity accounted for 80% of their net worth, compared to 48% for middle-income homeowners and 26% of high-income homeowners.[185] Chart 5.2 shows the class dimension to this dilemma. Low-income homeowners have a higher percentage of their net worth tied up in housing than high-income homeowners.

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181. Brown, *Pensions*, *supra* note 48, at 1536 (citing Martha N. Ozawa & Yat-Sang Lum, *Taking Risks in Investing in the Equity Market: Racial and Ethnic Differences*, 12 J. AGING & SOC. POL'Y 1, 3 (2001); James M. Poterba et al., *401(k) Plans and Future Patterns of Retirement Saving*, 88 AM. ECON. REV. 179, 181 (1998)).

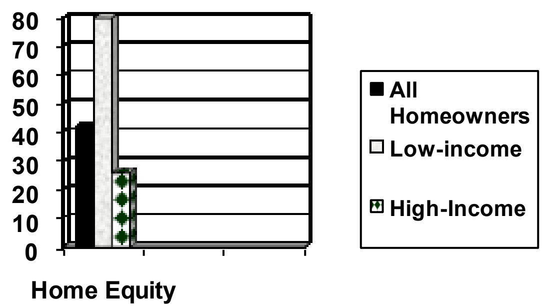
182. *Cf.* Kathryn L. Moore, *Partial Privatization of Social Security: Assessing Its Effect on Women, Minorities, and Lower-Income Workers*, 65 MO. L. REV. 341, 366 (2000).

183. Brown, *Risk Aversion*, *supra* note 48, at 399 (citing Luisa Beltran, *Many Black Investors Back in Market*, S. FLA. SUN-SENTINEL, June 28, 2004, at 21 ("[T]he study found that 61 percent of blacks and 51 percent of whites believe that real estate is the best investment overall."); Sandra Block, *African-American Investors Catching Up*, USA TODAY, June 24, 2004, at 2B ("[M]ost black investors believe real estate is the best overall investment . . . ."); Francine Knowles, *African Americans Exit Stocks*, CHI. SUN-TIMES, June 25, 2003, at 65 ("Fifty percent of blacks viewed real estate as the best investment . . . ."); Tristan Mabry, *Black Investors Shy Away from Stocks: Women in Particular are Afraid to Trust Brokerage Firms*, WALL ST. J., May 14, 1999, at A2 ("Blacks . . . tend to favor much more conservative investment vehicles, including real estate and insurance."); Sheila Muto, *The Property Report: Plots & Ploys*, WALL ST. J., June 23, 2004, at B6 ("Black investors continue to think real estate is a better place to invest their money than stocks, bonds or mutual funds, according to a survey of black and white households earning more than $50,000 a year.")).

184. *See* Mabry, *supra* note 183, at A2.

185. *See* Stegman et al., *supra* note 45, at 4.

CHART 5.2 PERCENTAGE NET WEALTH IN HOME EQUITY BY CLASS



If repeal of the mortgage interest deduction reduces the value of housing as many suggest, it would disproportionately decrease the net worth of low-income, black and Latino homeowners—the very groups this author is trying to assist. For example, all homeowners have approximately 40% of their net worth tied up in their homes while high-income homeowners have slightly more than 25%. Low-income homeowners have close to 80% of their net worth tied up in their homes. Any repeal of the mortgage interest deduction would reduce the price of housing. Although experts do not agree on how much the reduction would be, or even whether it would last long-term, most agree that initially the price of housing would fall. High-income homeowners with the lowest amount of net worth in their homes would be best able to weather that event, and low-income homeowners would be least able. Charts 5.1 and 5.2 show that repeal of the mortgage interest deduction is likely to negatively impact low-income, black and Latino homeowners. As a result, without further research, I hesitate to make such a radical proposal.

Another alternative that I have considered and rejected is to allow a deduction for rent. One reservation is that landlords would generally use the deduction to increase rental prices, which would not support the goal of affordable housing. This is a different problem from the mortgage interest deduction increasing the price of housing. In that instance, it is the homeowner who has the potential to receive that benefit—here it is not the renter, but the landlord. In order to address the class problems as well, such a deduction, if enacted, would have to be in the form of a refundable credit for all the reasons previously discussed.

CONCLUSION

Wealth building for communities of color is an important issue for the twenty-first century.[186] 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 disadvantage low-income homeowners regardless of race because they are often unable to benefit from existing tax law.

This Article has also shown that federal tax provisions supporting homeownership disadvantage middle- and upper-income blacks because the majority are renters and not homeowners. Middle- and upper-income black homeowners, however, are disadvantaged when compared with their white counterparts because of the quality of the housing they live in and because of a race-based penalty in the housing market, which limits their ability to receive significant appreciation upon sale—as their white counterparts do. Current federal housing tax policies (which disadvantage taxpayers on the basis of race and class) must be eliminated and, in their place, rules should be enacted that seek to afford all an equal opportunity to benefit from the American Dream of homeownership.

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186. Shapiro, *supra* note 2, 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.") (citation omitted).