Options to Reform the Deduction for Home Mortgage Interest

Daniel Baneman, Hang Nguyen, Jeffrey Rohaly, and Eric Toder
Urban-Brookings Tax Policy Center
August 16, 2011

ABSTRACT

Currently, taxpayers can deduct interest on up to $1 million in acquisition debt used to buy, build, or improve their primary residence or a second designated residence. In addition, taxpayers can deduct interest on up to $100,000 in home equity loans or other loans secured by their properties regardless of the loans' purpose. We consider a proposal that would limit the amount of deductible interest to the amount incurred on the first $500,000 of debt on a primary residence only, and would replace the itemized deduction with a nonrefundable tax credit equal to 15 percent of eligible home mortgage interest.

This research was performed under a contract with the National Low Income Housing Coalition.

Options to Reform the Deduction for Home Mortgage Interest

This analysis estimates the revenue and distributional implications of reforming the federal individual income tax treatment of home mortgage interest. Currently, taxpayers can claim an itemized deduction for interest on up to $1 million in acquisition debt used to buy, build, or improve their primary residence or a second designated residence. In addition, taxpayers can deduct the interest on up to $100,000 in home equity loans or other loans secured by their properties regardless of the purpose of the loans.[1] The $1 million and $100,000 amounts are not indexed for inflation.

We consider a proposal that: (a) would limit the amount of deductible interest to the amount incurred on the first $500,000 of debt on a primary residence only, not indexed for inflation; and (b) would replace the itemized deduction with a nonrefundable tax credit equal to 15 percent of eligible home mortgage interest.[2] Under current law, the value of the itemized deduction for mortgage interest depends on a taxpayer's marginal tax rate. For example, a taxpayer in the top 35 percent tax bracket would save $35 from an additional $100 of mortgage interest whereas someone in the 15 percent bracket would save only $15.[3] In addition, many lower-income taxpayers do not benefit directly from the mortgage interest deduction because they claim the standard deduction instead. In contrast, the proposed 15 percent nonrefundable credit for mortgage interest would provide the same percentage tax savings regardless of tax bracket and would be available in addition to the standard deduction.

We examine five variants of this proposal. The first option would enact the full proposal, effective January 1, 2012. The other options would phase down the value of the current deduction over time before eliminating it entirely and would immediately provide taxpayers with a choice between the new credit and the phased-down deduction.[4] Two of the other options would also gradually phase in the stricter limitation on the amount of deductible interest.

We estimate the revenue and distributional effects of the proposals against two baselines: current law and current policy. “Current law” is the standard baseline that official revenue estimators at the Joint Committee on Taxation use to score tax proposals. It assumes that tax law plays out as it is currently written. Most important, that means that the 2001–2010 income and estate tax cuts expire as scheduled at the end of 2012 and that temporary relief from the alternative minimum tax (AMT) expires at the end of 2011.

---

[1] Interest on a home equity loan not used to buy, build, or improve a residence is not deductible for alternative minimum tax purposes. See "Present Law and Background on the Tax Treatment of Household Debt," Joint Committee on Taxation, July 11, 2011, available at http://www.jct.gov/publications.html?func=startdown&id=3802.

[2] Because the deduction for home mortgage interest is not an alternative minimum tax (AMT) preference item, we assume that the new mortgage interest credit would not be limited by the AMT.

[3] This simplified example ignores the various phase-ins and phase-outs in the tax code that can cause a taxpayer's effective marginal tax rate to differ from her statutory rate.

[4] We assume that taxpayers respond optimally to the choice and pick whichever tax preference would give them the lowest tax liability.

The “current policy” baseline assumes that Congress permanently extends all provisions in the 2011 tax code (except the 2 percent reduction in Social Security payroll tax) as well as AMT relief, indexed for inflation after 2011.

Our revenue and distributional estimates assume that taxpayers optimally pay down their mortgage in response to a smaller tax preference for mortgage interest.[5] In addition, our revenue estimates are microdynamic: they assume that reported taxable income responds to changes in a taxpayer's statutory marginal tax rate.[6] We do not, however, incorporate in our estimates any possible impacts of the policy changes on homeownership rates, new investment in housing, home values, or mortgage interest rates.

A. Revenue Effects

Compared with current law, immediate enactment of the full proposal would raise approximately $573 billion over the 2012–21 budget window (see option 1 in table 1). The proposal would generate $378 billion when compared with current policy. Repealing the current mortgage interest deduction would generate less revenue against current policy because of that baseline's lower marginal tax rates, which results in a lower value of the deduction to taxpayers in higher tax brackets than under the current law baseline for tax years after 2012.

Option 2 would gradually phase down the value of the mortgage interest deduction over five years. In 2012, the value of the deduction would be capped at 31 percent.[7] This means that an additional $100 of home mortgage interest would be allowed to reduce tax liability by no more than $31. In subsequent years, the cap would fall by 4 percentage points annually until it would hit 15 percent in 2016. In 2017, the deduction would be completely eliminated. Beginning in 2012, taxpayers would be allowed to choose between the 15 percent nonrefundable credit and the limited mortgage interest deduction. This would immediately allow "nonitemizers"—those who claim the standard deduction—to benefit from the new tax credit. As in option 1, this proposal would also immediately implement the $500,000 cap on mortgage debt for a primary residence.[8] This option would generate $503 billion over 10 years against current law and $333 billion against current policy. Thus, compared with immediate repeal, the five-year phase down of the deduction would reduce the revenue gain by $70 billion against current law and $45 billion against current policy.

Option 3 is the same as option 2 but would phase in the stricter limitation on deductible interest. The restriction on January 1, 2012, would be for interest on the first $900,000 of debt on a primary residence. The cap would fall by $100,000 per year and would be $500,000 in 2016 and thereafter, not indexed for inflation. Compared with option 2, this would reduce the revenue gain by about $10 billion against current law and $9 billion

[5] Appendix A provides more details on our methodology.
[6] We assume a constant taxable income elasticity of 0.25 with respect to the net of tax rate.
[7] The limit on the value of the deduction would apply under both the regular tax and the AMT.
[8] Because the tax model database does not contain direct information on the value of outstanding mortgages, we approximate the cap on debt by limiting the amount of deductible mortgage interest to $25,000.

against current policy. Overall, option 3 would raise $492 billion against current law and $324 billion against current policy.

Option 4 would be similar to option 2 but would phase down the value of the mortgage interest deduction over 10 years rather than 5. The value of the deduction would be capped at 33 percent in 2012. In subsequent years, the cap would fall by 2 percentage points a year and would be 15 percent in 2021. In 2022, the deduction would be fully eliminated.[9] Beginning in 2012, taxpayers could choose between the deduction and the 15 percent nonrefundable credit. Option 4 would immediately implement the $500,000 mortgage debt cap. This option would generate $392 billion over the 10-year budget window against current law and $266 billion against current policy. Thus, compared with immediate repeal, the 10-year phase down of the deduction would reduce the revenue gain by $181 billion against current law and $112 billion against current policy.

Option 5 is the same as option 4 but would phase in the limitation on mortgage debt over 10 years. On January 1, 2012, interest would be restricted to the first $950,000 of debt on a primary residence. The limit would fall by $50,000 per year and would be $500,000 in 2021 and thereafter, not indexed for inflation. Compared with option 4, this would reduce the revenue gain by about $31 billion against current law and $28 billion against current policy. Overall, option 5 would raise $361 billion against current law and $238 billion against current policy.

B. Distributional Effects

In this analysis, we discuss the distributional effects of the five options relative to current policy in 2015.[10] The Tax Policy Center web site contains full distribution tables against both current law and current policy.[11]

Immediate full enactment of the proposal would raise taxes on about 16 percent of tax units and cut taxes for about 15 percent (table 2). Those with a tax hike would experience an average increase of $1,732 whereas those with a tax cut would see an average decrease of $414. The tax decreases would be concentrated among taxpayers with cash income less than $100,000; the proposal would cut taxes for close to one-third of taxpayers in the $50,000 to $100,000 income range. Most of these taxpayers claim the standard deduction and thus do not benefit from the current mortgage interest deduction, but would benefit from the new credit.

Among taxpayers affected by the proposal, virtually all with cash income of more than $200,000 would experience a tax increase. The proposal would increase taxes for almost 60 percent of taxpayers earning between $125,000 and $150,000 and for roughly 70 percent of those earning between $175,000 and $200,000. For these taxpayers in high tax brackets, the current deduction is much more valuable than a 15-percent credit would be.

---

[9] Note that 2022 is outside the 10-year budget window.
[10] Appendix tables B1 through B5 display the effects relative to the current law baseline.
[11] See http://www.taxpolicycenter.org.

Overall, the proposal would reduce after-tax income by an average of 0.3 percent, or $214. Taxpayers in the $200,000 to $500,000 cash income range would be hit hardest; they would see an average decrease in after-tax income of 1.1 percent or $2,529. On average, taxpayers in the $30,000 to $50,000 income range would benefit the most; they would see an average increase in after-tax income of 0.2 percent (about $50 to $80).

Phasing out the deduction over five years would mitigate some of the tax increases on upper-income taxpayers. Option 2 would limit the value of the deduction to 19 percent in 2015 and would allow taxpayers to choose between this limited deduction and the 15 percent nonrefundable credit. It would also immediately implement the $500,000 limit on debt on a primary residence. In 2015, this proposal would cut taxes for 15 percent of tax units, the same as immediate full enactment (table 3). This is because this proposal would allow those who do not currently itemize deductions to claim the 15 percent nonrefundable credit. The proposal would raise taxes on 15 percent of tax units, almost the same percentage as immediate full enactment, but the magnitude of the associated tax increase would be slightly smaller, $1,593 instead of $1,732. The smaller average increase would occur because taxpayers in higher tax brackets would claim the 19 percent deduction, giving them a slightly larger benefit than the 15 percent nonrefundable credit they would get under immediate full enactment.

Overall, option 2 would reduce after-tax income by an average of 0.3 percent, or $173. Taxpayers in the $200,000 to $500,000 cash income range would continue to be hit hardest; they would see an average decrease in after-tax income of 1.1 percent or $2,510. On average, taxpayers in the $40,000 to $50,000 income range would benefit the most; they would see an average increase in after-tax income of 0.3 percent, or $101.

Option 3 is similar to option 2 but it would phase in the cap on eligible mortgage debt over five years. By 2015, the cap would be $600,000 rather than the $500,000 amount under option 2. This would have the largest impact—although still a modest one—on upper-income households who tend to have larger mortgages. For example, affected taxpayers with cash income of more than $1 million would see an average tax increase of $7,804 under this proposal, down from $8,110 under option 2 (table 4). Phasing in the cap would have very little impact on more moderate-income taxpayers, very few of whom are affected by the mortgage cap. Affected taxpayers in the $100,000 to $200,000 income range would see an average tax increase that is about $53 lower ($1,005 versus $1,058) than with the $500,000 cap.

Option 4 would phase out the value of the deduction over 10 years but would immediately implement the $500,000 mortgage cap. In 2015, the value of the mortgage interest deduction would be limited to 27 percent. As with the other proposals, this option would reduce taxes for about 15 percent of tax units since it would also allow nonitemizers to claim the nonrefundable credit. The proposal would increase taxes for just 13 percent of tax units, with an average increase of $1,434, or about $298 less than under immediate full enactment (table 5). Because the value of the deduction would be limited to 27 percent, it would increase taxes on fewer upper-middle-income taxpayers who would be in the 25 percent bracket. Thus, the proposal would increase taxes on 46 percent of taxpayers in the $100,000 to $200,000 income range, down from 55 percent under option 1.

Overall, option 4 would reduce after-tax income by an average of 0.2 percent, or $120. Taxpayers in the $200,000 to $500,000 cash income range would continue to be hit hardest; they would see an average decrease in after-tax income of 1.1 percent or $2,481. On average, taxpayers in the $40,000 to $75,000 income range would benefit the most; they would see an average increase in after-tax income of 0.3 percent, or between $101 and $135.

Option 5 is similar to option 4 but would phase in the cap on eligible mortgage debt over 10 years. By 2015, the cap would be $800,000 rather than the $500,000 amount under option 4. As with option 3, phasing in the cap would have the biggest impact on upper-income taxpayers with larger mortgages. For example, affected taxpayers with cash income of more than $1 million would see an average tax increase of $7,317 under this proposal, $784 less than under option 4 (table 6). Phasing in the cap would have a smaller impact on more moderate-income households, few of whom are affected by the mortgage cap. Affected taxpayers in the $100,000 to $200,000 income range would see an average tax increase that is about $132 lower ($476 versus $608) than with the $500,000 cap.

C. Number of Beneficiaries

Under current policy in 2015—assuming all of the 2001–10 individual income tax cuts are made permanent—about 37.5 million tax units, or 22 percent of the total, benefit from the itemized deduction for mortgage interest (table 7). Among tax units with cash income less than $50,000, just 4.4 million—or about 5 percent—benefit from the deduction since most would take the standard deduction instead. In contrast, about two-thirds of households with incomes between $125,000 and $500,000 benefit from the deduction. At the top of the income scale, fewer taxpayers have mortgages and so just one-third of those with incomes greater than $1 million benefit from the current deduction.

Overall, the average benefit for taxpayers who claim the deduction will be $2,708. The average size of the benefit rises with income for two reasons: higher-income taxpayers tend to have larger mortgages, and the value of the deduction for any given amount of mortgage interest rises with the taxpayer's marginal income tax rate. So, for example, the average benefit under current law in 2015 for a taxpayer in the $40,000 to $50,000 income range is about $930; for someone with cash income of more than $1 million the average benefit is $9,900.

If the current deduction were repealed and replaced with a 15 percent nonrefundable credit, and if the cap on eligible mortgages were reduced to $500,000 for a primary residence only, the number of taxpayers who benefit would rise by about 15 million, to a total of 52.2 million, or about 31 percent of all tax units. A much higher percentage of taxpayers in lower income groups would receive tax benefits from the mortgage interest credit compared with the deduction. Among taxpayers with cash income less than $50,000, the number that benefit would more than double to 11.6 million, or 12 percent of the total. For taxpayers with income between $50,000 and $75,000 the number who benefit from the credit would rise to 11.5 million (48 percent of the total), up from 6.7 million under the deduction. This would occur because taxpayers at lower income levels are less likely to be itemizers and hence would not benefit from the mortgage interest deduction, whereas the credit would be available even if the taxpayer were to claim the standard deduction.

Although more taxpayers would benefit from the credit than the deduction, the average value of the benefit from the credit would be significantly lower than the benefit from the deduction. Overall, the average benefit in 2015 would be $1,273, or more than $1,400 lower than the deduction. The decline would occur among all cash income levels but the largest drop would be in the upper income categories. High-income taxpayers in the top tax brackets would experience the biggest discrepancy between the current value of the deduction—which would depend on their marginal tax rate—and the 15 percent credit. They would also be the group hit hardest by the $500,000 mortgage cap and the restriction to debt on a primary residence because high-income households are likely to have larger mortgages than the cap and own second homes.[12]

[12] Appendix table B6 shows the impact of the current deduction and the proposed credit relative to a current law baseline in 2015. Under current law, close to 3 million more taxpayers would benefit from both the deduction and the credit than under current policy. The difference would occur because under current policy, tax rates are lower and many credits, such as the child tax credit, education credits, and the child and dependent care credit, are more valuable. These provisions would reduce tax liability under current policy relative to current law and thus eliminate the benefit of claiming the mortgage interest deduction for some taxpayers.

Table 1

Options to Replace Mortgage Interest Deduction (MID) with Tax Credit

Impact on Individual Income Tax Revenue (billions of current dollars), 2012–21 [1]

	Fiscal Years										
	2012	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2012-21**
Baseline: Current Law											
Option 1: Replace MID with 15% nonrefundable credit; cap deductible interest [2]	15.1	39.4	44.0	49.6	55.4	61.2	67.0	73.4	80.0	87.5	572.6
Option 2: Phase down MID over 5 years, then eliminate; 15% credit; cap deductible interest [3]	6.8	18.1	24.1	35.5	49.4	60.8	67.0	73.4	80.0	87.5	502.6
Option 3: Option 2 but phase in cap on deductible interest over 5 years [4]	5.6	15.2	21.2	33.2	48.3	60.8	67.0	73.4	80.0	87.5	492.3
Option 4: Phase down MID over 10 years, then eliminate; 15% credit, cap deductible interest [5]	6.7	17.7	20.6	24.4	29.8	37.3	46.4	57.1	69.0	82.7	391.8
Option 5: Option 4 but phase in cap on deductible interest over 10 years.[6]	5.5	14.6	17.1	20.6	25.7	33.2	42.4	53.6	66.5	81.6	360.7
Baseline: Current Policy [7]											
Option 1: Replace MID with 15% nonrefundable credit; cap deductible interest [2]	9.9	25.8	28.7	32.8	37.0	41.0	44.7	48.6	52.5	57.0	378.0
Option 2: Phase down MID over 5 years, then eliminate; 15% credit; cap deductible interest [3]	5.1	13.4	16.3	23.1	32.5	40.3	44.7	48.6	52.5	57.0	333.4
Option 3: Option 2 but phase in cap on deductible interest over 5 years [4]	4.1	10.7	13.7	20.9	31.5	40.3	44.7	48.6	52.5	57.0	324.0
Option 4: Phase down MID over 10 years, then eliminate; 15% credit, cap deductible interest [5]	5.1	13.2	15.0	18.0	21.4	25.4	31.1	38.0	45.3	53.6	266.2
Option 5: Option 4 but phase in cap on deductible interest over 10 years.[6]	4.0	10.4	11.9	14.6	17.7	21.6	27.5	34.7	42.9	52.6	238.0

Source*:* Urban-Brookings Tax Policy Center Microsimulation Model (version 0411-2).

(1) Fiscal years. Estimates assume a 40-60 fiscal split. Proposals are effective 01/01/12. Estimates include a microdynamic behavioral response and assume that taxpayers would adjust their investment portfolio and optimally pay down their mortgage balance if their tax benefit from mortgage interest were reduced.

(2) Proposal would replace the current mortgage interest deduction with a 15 percent nonrefundable credit, effective 01/01/12. The credit would be limited to interest on the first $500,000 of a mortgage on a primary residence only, not indexed for inflation.

(3) Proposal would reduce the value of the mortgage interest deduction to 15 percent over five years, and then eliminate. Effective 01/01/12, in lieu of the deduction, taxpayers could elect to claim a 15 percent nonrefundable tax credit for mortgage interest. The deduction and the credit would be limited to interest on the first $500,000 of a mortgage on a primary residence, not indexed for inflation.

(4) Proposal would phase in the limit on eligible interest over 5 years. Effective 01/01/16, the limit would be interest on the first $500,000 of a mortgage on a primary residence only, not indexed for inflation.

(5) Proposal would reduce the value of the mortgage interest deduction to 15 percent over 10 years, and then eliminate it. Effective 01/01/12, in lieu of the deduction, taxpayers could elect to claim a 15 percent nonrefundable tax credit for mortgage interest. The deduction and the credit would be limited to interest on the first $500,000 of a mortgage on a primary residence, not

(6) Proposal would phase in the limit on eligible interest over 10 years. Effective 01/01/21, the limit would be interest on the first $500,000 of a mortgage on a primary residence only, not indexed for inflation.

(7) Current policy makes 2011 tax law permanent with the exception of the temporary 2 percent reduction in Social Security payroll taxes.

Table 2
Option 1: Immediate Full Enactment
Baseline: Current Policy
Distribution of Federal Tax Change by Cash Income Level, 2015 [1]

Cash Income Level (thousands of 2011 dollars) [2]	Tax Units with Tax Increase or Cut [3]				Pct Change in After-Tax Income [4]	Share of Total Federal Tax Change	Average Federal Tax Change ($)	Average Federal Tax Rate[5]	
	With Tax Cut		With Tax Increase						
	Pct of Tax Units	Avg Tax Cut	Pct of Tax Units	Avg Tax Increase				Change (Pct Points)	Under the Proposal
Less than 10	*	**	0.0	0	0.0	0.0	0	0.0	2.8
10–20	3.2	-146	0.1	285	0.0	-0.3	-4	0.0	1.8
20–30	9.4	-247	0.8	267	0.1	-1.2	-21	-0.1	7.0
30–40	20.4	-302	2.4	335	0.2	-2.5	-54	-0.1	11.3
40–50	28.9	-363	5.0	426	0.2	-3.2	-83	-0.2	14.3
50–75	32.8	-458	14.7	603	0.1	-4.1	-61	-0.1	16.9
75–100	30.3	-555	24.4	768	0.0	0.8	20	0.0	19.1
100–200	10.4	-472	54.7	1,383	-0.6	46.6	707	0.5	22.3
200–500	1.2	-470	64.6	3,923	-1.1	49.3	2,529	0.8	25.4
500–1,000	0.8	-401	53.4	5,539	-0.6	9.7	2,956	0.4	27.1
More than 1,000	0.2	-518	35.6	8,115	-0.1	4.8	2,890	0.1	31.7
All	14.8	-414	15.9	1,732	-0.3	100.0	214	0.3	21.2
Addendum									
100–125	16.9	-484	44.4	871	-0.3	8.5	305	1.3	0.0
125–150	7.5	-469	58.5	1,364	-0.7	14.5	763	2.4	0.1
150–175	4.5	-405	63.6	1,750	-0.8	12.7	1,094	2.8	0.1
175–200	2.7	-370	69.0	2,122	-1.0	10.9	1,454	3.1	0.1

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0411-2).
Number of AMT Taxpayers (millions). Baseline: 6.1 Proposal: 6.8
* Less than 0.05
** Insufficient data
(1) Calendar year. Baseline is current policy. Proposal would replace mortgage interest deduction with a 15 percent nonrefundable credit for mortgage interest and limit this credit to the first $500,000 of a mortgage on primary residence only. Estimates assume that taxpayers would adjust their investment portfolio and optimally pay down their mortgage balance if their tax benefit from mortgage interest were reduced.
(2) Tax units with negative cash income are excluded from the lowest income class but are included in the totals. For a description of cash income, see http://www.taxpolicycenter.org/TaxModel/income.cfm.
(3) Includes both filing and nonfiling units but excludes those that are dependents of other tax units.
(4) After-tax income is cash income less individual income tax net of refundable credits, corporate income tax, payroll taxes (Social Security and
(5) Average federal tax (includes individual and corporate income tax, payroll taxes for Social Security and Medicare, and the estate tax) as a percentage of average cash income.

Table 3
Option 2: Phase Down Deduction Over 5 Years, Immediate $500,000 Cap
Baseline: Current Policy
Distribution of Federal Tax Change by Cash Income Level, 2015 [1]

Cash Income Level (thousands of 2011 dollars) [2]	Tax Units with Tax Increase or Cut [3]				Pct Change in After-Tax Income [4]	Share of Total Federal Tax Change	Average Federal Tax Change ($)	Average Federal Tax Rate [5]	
	With Tax Cut		With Tax Increase						
	Pct of Tax Units	Avg Tax Cut	Pct of Tax Units	Avg Tax Increase				Change (Pct Points)	Under the Proposal
Less than 10	*	**	0.0	0	0.0	0.0	0	0.0	2.8
10–20	3.2	-146	0.1	263	0.0	-0.4	-4	0.0	1.8
20–30	9.4	-247	0.2	192	0.1	-1.6	-23	-0.1	7.0
30–40	20.4	-302	0.6	158	0.2	-3.4	-61	-0.2	11.2
40–50	28.9	-363	2.0	202	0.3	-4.7	-101	-0.2	14.3
50–75	32.9	-456	11.8	390	0.2	-8.6	-104	-0.2	16.8
75–100	30.4	-553	22.5	549	0.1	-2.3	-45	-0.1	19.0
100–200	10.4	-471	53.8	1,058	-0.5	42.5	520	0.4	22.1
200–500	1.2	-470	64.6	3,897	-1.1	60.6	2,510	0.8	25.3
500–1,000	0.8	-401	53.3	5,539	-0.6	12.0	2,951	0.4	27.1
More than 1,000	0.2	-518	35.6	8,110	-0.1	6.0	2,887	0.1	31.7
All	14.9	-413	14.7	1,593	-0.3	100.0	173	0.2	21.2
Addendum									
100–125	16.9	-484	42.8	630	-0.2	6.5	188	0.8	0.0
125–150	7.5	-468	58.1	993	-0.5	12.8	542	1.7	0.1
150–175	4.5	-405	63.4	1,282	-0.6	11.4	794	2.0	0.1
175–200	2.7	-370	68.8	1,862	-0.8	11.8	1,270	2.7	0.1

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0411-2).
Number of AMT Taxpayers (millions). Baseline: 6.1 Proposal: 6.8
* Less than 0.05
** Insufficient data
(1) Calendar year. Baseline is current policy. Proposal would reduce mortgage interest deduction to 15 percent over five years and then completely replace this deduction with a 15 percent nonrefundable credit for mortgage interest. In 2015, deduction would be limited to 19 percent. Both the credit and the deduction will be limited to the first $500,000 of a mortgage on primary residence only. Estimates assume that taxpayers would adjust their investment portfolio and optimally pay down their mortgage balance if their tax benefit from mortgage interest were reduced.
(2) Tax units with negative cash income are excluded from the lowest income class but are included in the totals. For a description of cash income, see http://www.taxpolicycenter.org/TaxModel/income.cfm.
(3) Includes both filing and nonfiling units but excludes those that are dependents of other tax units.
(4) After-tax income is cash income less individual income tax net of refundable credits, corporate income tax, payroll taxes (Social Security and
(5) Average federal tax (includes individual and corporate income tax, payroll taxes for Social Security and Medicare, and the estate tax) as a percentage of average cash income.

Table 4

Option 3: Phase Down Deduction Over 5 Years, Phase In Mortgage Cap Over 5 Years

Baseline: Current Policy

Distribution of Federal Tax Change by Cash Income Level, 2015 [1]

Cash Income Level (thousands of 2011 dollars) [2]	Tax Units with Tax Increase or Cut [3]				Pct Change in After-Tax Income [4]	Share of Total Federal Tax Change	Average Federal Tax Change ($)	Average Federal Tax Rate[5]	
	With Tax Cut		With Tax Increase						
	Pct of Tax Units	Avg Tax Cut	Pct of Tax Units	Avg Tax Increase				Change (Pct Points)	Under the Proposal
Less than 10	*	**	0.0	0	0.0	0.0	0	0.0	2.8
10–20	3.2	-146	0.1	263	0.0	-0.4	-4	0.0	1.8
20–30	9.4	-247	0.2	192	0.1	-1.7	-23	-0.1	7.0
30–40	20.4	-302	0.6	157	0.2	-3.7	-61	-0.2	11.2
40–50	28.9	-363	1.8	175	0.3	-5.1	-102	-0.2	14.3
50–75	33.0	-457	11.6	380	0.2	-9.3	-107	-0.2	16.8
75–100	30.7	-553	22.0	523	0.1	-3.0	-55	-0.1	19.0
100–200	10.4	-471	53.5	1,005	-0.4	42.4	489	0.3	22.1
200–500	1.2	-470	64.5	3,782	-1.1	62.4	2,434	0.8	25.3
500–1,000	0.8	-404	53.3	5,302	-0.5	12.2	2,824	0.4	27.1
More than 1,000	0.2	-515	35.6	7,804	-0.1	6.1	2,774	0.1	31.7
All	14.9	-414	14.6	1,540	-0.3	100.0	163	0.2	21.2
Addendum									
100–125	17.0	-484	42.3	600	-0.2	6.3	171	0.7	0.0
125–150	7.5	-469	57.9	940	-0.5	12.8	509	1.6	0.1
150–175	4.5	-405	63.2	1,210	-0.6	11.4	747	1.9	0.1
175–200	2.7	-370	68.8	1,776	-0.8	11.9	1,211	2.6	0.1

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0411-2).

Number of AMT Taxpayers (millions). Baseline: 6.1 Proposal: 6.8

* Less than 0.05

** Insufficient data

(1) Calendar year. Baseline is current policy. Proposal would reduce mortgage interest deduction to 15 percent over five years and then completely replace this deduction with a 15 percent nonrefundable credit for mortgage interest. Deduction would be limited to 19 percent for 2015. Both the credit and the deduction would be limited to the first $600,000 of a mortgage on primary residence only in 2015. Estimates assume that taxpayers would adjust their investment portfolio and optimally pay down their mortgage balance if their tax benefit from mortgage interest were reduced.

(2) Tax units with negative cash income are excluded from the lowest income class but are included in the totals. For a description of cash income, see http://www.taxpolicycenter.org/TaxModel/income.cfm.

(3) Includes both filing and nonfiling units but excludes those that are dependents of other tax units.

(4) After-tax income is cash income less individual income tax net of refundable credits, corporate income tax, payroll taxes (Social Security and

(5) Average federal tax (includes individual and corporate income tax, payroll taxes for Social Security and Medicare, and the estate tax) as a percentage of average cash income.

Table 5

Option 4: Phase Down Deduction Over 10 Years, Immediate $500,000 Mortgage Cap

Baseline: Current Policy

Distribution of Federal Tax Change by Cash Income Level, 2015 [1]

Cash Income Level (thousands of 2011 dollars) [2]	Tax Units with Tax Increase or Cut [3]				Pct Change in After-Tax Income [4]	Share of Total Federal Tax Change	Average Federal Tax Change ($)	Average Federal Tax Rate[5]	
	With Tax Cut		With Tax Increase						
	Pct of Tax Units	Avg Tax Cut	Pct of Tax Units	Avg Tax Increase				Change (Pct Points)	Under the Proposal
Less than 10	*	**	0.0	0	0.0	0.0	0	0.0	2.8
10–20	3.2	-146	0.1	264	0.0	-0.6	-4	0.0	1.8
20–30	9.4	-247	0.2	199	0.1	-2.3	-23	-0.1	7.0
30–40	20.4	-302	0.6	158	0.2	-5.0	-61	-0.2	11.2
40–50	28.9	-363	1.9	203	0.3	-6.9	-101	-0.2	14.3
50–75	32.9	-457	8.4	178	0.3	-16.1	-135	-0.2	16.8
75–100	30.4	-553	17.6	278	0.2	-8.8	-119	-0.1	18.9
100–200	10.5	-468	45.7	608	-0.2	27.1	229	0.2	21.9
200–500	1.2	-470	64.2	3,872	-1.1	86.7	2,481	0.8	25.3
500–1,000	0.8	-401	53.3	5,528	-0.6	17.3	2,945	0.4	27.1
More than 1,000	0.2	-518	35.6	8,101	-0.1	8.6	2,883	0.1	31.7
All	14.9	-413	12.6	1,434	-0.2	100.0	120	0.2	21.1
Addendum									
100–125	17.0	-482	34.1	313	0.0	1.2	25	0.1	-0.1
125–150	7.9	-460	48.8	445	-0.2	6.2	181	0.6	0.0
150–175	4.6	-404	55.2	600	-0.2	6.5	312	0.8	0.0
175–200	2.8	-371	66.6	1,483	-0.6	13.1	978	2.1	0.1

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0411-2).

Number of AMT Taxpayers (millions). Baseline: 6.1 Proposal: 6.6

* Less than 0.05

** Insufficient data

(1) Calendar year. Baseline is current policy. Proposal would reduce mortgage interest deduction to 15 percent over 10 years and then completely replace this deduction with a 15 percent nonrefundable credit for mortgage interest. Deduction would be limited to 27 percent for 2015. Both the credit and the deduction will be limited to the first $500,000 of a mortgage on primary residence only. Estimates assume that taxpayers would adjust their investment portfolio and optimally pay down their mortgage balance if their tax benefit from mortgage interest were reduced.

(2) Tax units with negative cash income are excluded from the lowest income class but are included in the totals. For a description of cash income, see http://www.taxpolicycenter.org/TaxModel/income.cfm.

(3) Includes both filing and nonfiling units but excludes those that are dependents of other tax units.

(4) After-tax income is cash income less individual income tax net of refundable credits, corporate income tax, payroll taxes (Social Security and

(5) Average federal tax (includes individual and corporate income tax, payroll taxes for Social Security and Medicare, and the estate tax) as a percentage of average cash income.

Table 6

Option 5: Phase Down Deduction Over 10 Years, Phase in Mortgage Cap Over 10 Years

Baseline: Current Policy

Distribution of Federal Tax Change by Cash Income Level, 2015 [1]

Cash Income Level (thousands of 2011 dollars) [2]	Tax Units with Tax Increase or Cut [3]				Pct Change in After-Tax Income [4]	Share of Total Federal Tax Change	Average Federal Tax Change ($)	Average Federal Tax Rate[5]	
	With Tax Cut		With Tax Increase						
	Pct of Tax Units	Avg Tax Cut	Pct of Tax Units	Avg Tax Increase				Change (Pct Points)	Under the Proposal
Less than 10	*	**	0.0	0	0.0	0.0	0	0.0	2.8
10–20	3.2	-146	0.1	264	0.0	-0.7	-4	0.0	1.8
20–30	9.4	-247	0.2	199	0.1	-2.8	-23	-0.1	7.0
30–40	20.4	-302	0.6	157	0.2	-6.1	-61	-0.2	11.2
40–50	28.9	-363	1.6	175	0.3	-8.5	-102	-0.2	14.3
50–75	33.0	-458	8.0	145	0.3	-20.2	-139	-0.2	16.8
75–100	30.8	-554	16.4	210	0.2	-12.2	-136	-0.2	18.9
100–200	10.6	-469	44.5	476	-0.1	23.3	162	0.1	21.9
200–500	1.2	-469	64.1	3,632	-1.0	98.8	2,323	0.8	25.3
500–1,000	0.8	-403	53.3	4,961	-0.5	18.9	2,642	0.4	27.1
More than 1,000	0.2	-514	35.5	7,317	-0.1	9.4	2,595	0.1	31.7
All	15.0	-414	12.3	1,305	-0.2	100.0	98	0.1	21.1
Addendum									
100–125	17.2	-483	32.9	229	0.0	-0.5	-8	0.0	-0.1
125–150	7.9	-461	47.3	317	-0.1	4.7	114	0.4	0.0
150–175	4.6	-402	53.8	403	-0.2	5.0	198	0.5	0.0
175–200	2.8	-370	65.7	1,315	-0.6	14.0	854	1.8	0.1

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0411-2).

Number of AMT Taxpayers (millions). Baseline: 6.1 Proposal: 6.6

* Less than 0.05

** Insufficient data

(1) Calendar year. Baseline is current policy. Proposal would reduce mortgage interest deduction to 15 percent over 10 years and then completely replace this deduction with a 15 percent nonrefundable credit for mortgage interest. Deduction would be limited to 27 percent in 2015. Both the credit and the deduction would be limited to the first $800,000 of a mortgage on primary residence only in 2015. Estimates assume that taxpayers would adjust their investment portfolio and optimally pay down their mortgage balance if their tax benefit from mortgage interest were reduced.

(2) Tax units with negative cash income are excluded from the lowest income class but are included in the totals. For a description of cash income, see http://www.taxpolicycenter.org/TaxModel/income.cfm.

(3) Includes both filing and nonfiling units but excludes those that are dependents of other tax units.

(4) After-tax income is cash income less individual income tax net of refundable credits, corporate income tax, payroll taxes (Social Security and

(5) Average federal tax (includes individual and corporate income tax, payroll taxes for Social Security and Medicare, and the estate tax) as a percentage of average cash income.

Table 7

Benefits from Mortgage Interest Deduction and 15 percent Nonrefundable Credit, 2015 [1]
Baseline: Current Policy

Cash Income Level (thousands of 2011 dollars)	Tax Units (thousands) [3]	Current Mortgage Interest Deduction: Tax Units with Benefit		Current Mortgage Interest Deduction: Average Benefit (dollars)		Proposal: 15 Percent Non-refundable Credit [2]: Tax Units with Benefit		Proposal: 15 Percent Non-refundable Credit [2]: Average Benefit (dollars)	
		Number (thousands)	Percent within Class	All Tax Units	Tax Units with Benefit	Number (thousands)	Percent within Class	All Tax Units	Tax Units with Benefit
Less than 10	18,828	0	0.0	0	0	0	0.0	0	25
10–20	26,753	214	0.8	2	289	963	3.6	7	191
20–30	20,164	665	3.3	20	601	2,117	10.5	41	393
30–40	16,562	1,342	8.1	56	697	3,776	22.8	110	482
40–50	13,738	2,129	15.5	144	930	4,698	34.2	228	666
50–75	24,031	6,681	27.8	379	1,362	11,487	47.8	440	921
75–100	14,893	6,478	43.5	762	1,751	8,370	56.2	744	1,325
100–125	10,050	5,638	56.1	1,271	2,267	6,181	61.5	970	1,577
125–150	6,907	4,358	63.1	1,918	3,039	4,510	65.3	1,160	1,777
150–175	4,215	2,794	66.3	2,393	3,611	2,824	67.0	1,306	1,949
175–200	2,715	1,903	70.1	2,786	3,975	1,914	70.5	1,348	1,912
200–500	7,059	4,532	64.2	3,860	6,016	4,553	64.5	1,389	2,155
500–1,000	1,187	616	51.9	4,096	7,899	625	52.6	1,309	2,488
More than 1,000	603	210	34.8	3,441	9,897	212	35.2	946	2,689
All	168,946	37,506	22.2	602	2,708	52,204	30.9	394	1,273

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0411-2).
(1) Calendar year.
(2) The proposal would also limit the amount of deductible interest to the first $500,000 of a mortgage on a primary residence only. Estimates include a microdynamic behavioral response and assume that taxpayers would adjust their investment portfolio and optimally pay down their mortgage balance if their tax benefit from mortgage interest were reduced.
(3) Includes both filing and nonfiling units but excludes those that are dependents of other tax units.

Appendix A: Description of Portfolio Adjustment

We assume that high-income taxpayers would adjust their investment portfolio in response to a reduction in the tax benefits for mortgage interest. Specifically, we assume that they would sell bonds that generate taxable interest income in order to pay down their outstanding mortgage balance. In this section, we explain the economic intuition behind this assumption and describe our simplified modeling techniques.

Under current law, taxpayers that choose to itemize their deductions can deduct their mortgage interest payments from taxable income. The exact value of the resulting tax benefit depends on the taxpayer's marginal tax bracket. Consider a taxpayer in the top 35 percent tax bracket who faces a 5 percent mortgage interest rate. An additional $100 in mortgage debt would generate an additional $5 in mortgage interest.[13] Under current law, the taxpayer would be allowed to deduct the $5 in interest, which would save her 35 percent of $5, or $1.75 in tax liability. Thus, the after-tax interest cost of holding an additional $100 of mortgage debt would be $3.25.

Suppose this taxpayer also has a portfolio of taxable bonds. We make the simplifying assumption that the interest rate on taxable bonds is the same as the mortgage interest rate, or 5 percent on a pretax basis. An additional $100 in taxable bond holdings would generate $5 in additional taxable income. Since the taxpayer must pay 35 percent tax on this interest income, her tax liability would go up by $1.75, leaving her with an after-tax return of $3.25. Thus, the taxpayer's after-tax return on investing in bonds is the same as her after-tax cost of holding mortgage debt, and the taxpayer is indifferent between the two.

Now suppose that Congress converts the itemized deduction for mortgage interest to a 15 percent nonrefundable tax credit. In this case, each additional $100 of mortgage debt would reduce the taxpayer's liability by 15 percent of the additional interest, regardless of which tax bracket she were in. This implies that the taxpayer would no longer be indifferent between holding bonds and mortgage debt. Suppose the taxpayer were to sell $100 worth of bonds in order to pay down $100 of mortgage debt.[14] She would reduce her taxable interest income by $5, which would reduce her tax liability by 35 percent of $5, or $1.75. The reduction in mortgage interest by $5 would now increase tax liability by 15 percent of $5, or $0.75. Overall, her tax liability from this transaction would fall by $0.50. Thus, this taxpayer has an incentive to sell available assets to pay down her mortgage.[15] Allowing for a portfolio adjustment to the proposal would therefore result in a smaller overall revenue gain for the Treasury from the proposal.
Compared with current law, the taxpayer in this example would avoid any tax increase by selling bonds to pay off her mortgage debt. By comparison, if we neglected to account for this asset-shifting, the increase in tax liability would be the difference between 35 percent and 15 percent multiplied by the amount of mortgage interest, or $20 in taxes for every $100 of mortgage interest.

[13] This simplified example ignores the fact that under a typical amortization schedule the amount of the taxpayer's monthly mortgage payment that represents interest falls over time. We are also ignoring the various phase-ins and phase-outs in the tax code that can cause a taxpayer's effective marginal rate to differ from her statutory rate.
[14] We ignore the possibility that the taxpayer would realize capital gains income from selling her bond portfolio.
[15] We assume that taxpayers sell up to 90 percent of available taxable bonds in order to pay down their mortgage in response to a reduction in the tax benefits for mortgage interest.

Note that the portfolio adjustment would not be optimal for taxpayers in lower brackets. For a taxpayer in the 15 percent bracket, for example, replacing the deduction with a 15 percent credit does not affect after-tax return and therefore creates no incentive to pay down mortgage debt.[16] More important, generally only very high-income taxpayers have enough assets that they can reshuffle their portfolio to avoid facing a tax increase.

In order to implement the portfolio adjustment in our microsimulation tax model, we make the following assumptions. Define "affected mortgage interest" (AMI) to be interest that (a) would receive a lower tax subsidy than its projected current law value (e.g., 15 percent instead of 35 percent as in the example above), or (b) would receive no tax subsidy due to the lower cap on eligible mortgage debt, or (c) would receive no tax subsidy due to the restriction to primary residences.

We assume that taxpayers would sell bonds to pay off debt with AMI as much as possible without allowing interest income to drop below 10 percent of its original value in that year. That is, we assume that taxpayers would keep at least 10 percent of their original bond holdings to maintain liquidity and a diversified portfolio. In the options that would phase in either mortgage caps or maximum deduction rates, we assume taxpayers would respond to the cap or rate at exactly the phased-in level. For example, if an option limits the deduction to 27 percent in a given year and applies a mortgage debt cap of $800,000, we would apply the adjustment to interest that (a) would be taxed at a rate higher than 27 percent when held as interest-bearing bonds, (b) would be associated with debt in excess of $800,000, or (c) would be associated with debt from something other than a primary residence.

[16] The proposal would also restrict eligible mortgages to primary residences, capped at $500,000. This could affect a taxpayer in the 15 percent bracket and below, who would adjust her portfolio to pay down mortgage debt whose interest is no longer subsidized.

Appendix Table B1
Option 1: Immediate Full Enactment
Baseline: Current Law
Distribution of Federal Tax Change by Cash Income Level, 2015 [1]

Cash Income Level (thousands of 2011 dollars) [2]	Tax Units with Tax Increase or Cut [3]				Pct Change in After-Tax Income [4]	Share of Total Federal Tax Change	Average Federal Tax Change ($)	Average Federal Tax Rate[5]	
	With Tax Cut		With Tax Increase						
	Pct of Tax Units	Avg Tax Cut	Pct of Tax Units	Avg Tax Increase				Change (Pct Points)	Under the Proposal
Less than 10	*	**	0.0	0	0.0	0.0	0	0.0	4.9
10–20	3.4	-164	*	**	0.0	-0.3	-5	0.0	3.8
20–30	11.0	-269	0.3	194	0.1	-1.1	-29	-0.1	9.5
30–40	24.1	-330	1.4	206	0.2	-2.3	-77	-0.2	13.6
40–50	31.6	-381	5.1	323	0.3	-2.6	-104	-0.2	16.4
50–75	28.8	-420	19.5	711	0.0	0.8	17	0.0	19.3
75–100	14.3	-440	42.2	1,087	-0.6	10.8	396	0.4	22.2
100–200	4.6	-461	60.7	1,836	-1.0	47.6	1,093	0.8	25.7
200–500	0.8	-595	65.0	4,160	-1.2	34.8	2,701	0.9	28.6
500–1,000	1.0	-1,022	53.2	7,289	-0.8	8.4	3,871	0.5	30.2
More than 1,000	0.6	-1,080	36.8	9,742	-0.2	3.9	3,580	0.1	36.0
All	12.8	-374	18.9	1,973	-0.5	100.0	324	0.4	24.4
Addendum									
100–125	6.7	-479	55.4	1,445	-0.8	14.1	768	2.7	0.1
125–150	4.1	-415	61.8	1,763	-1.0	13.5	1,072	2.9	0.1
150–175	2.3	-487	65.6	2,127	-1.1	10.7	1,385	3.1	0.1
175–200	1.3	-413	69.9	2,721	-1.3	9.4	1,896	3.6	0.1

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0411-2).
Number of AMT Taxpayers (millions). Baseline: 27.0 Proposal: 30.0
* Less than 0.05
** Insufficient data
(1) Calendar year. Baseline is current law. Proposal would replace mortgage interest deduction with a 15 percent nonrefundable credit for mortgage interest and limit this credit to the first $500,000 of a mortgage on primary residence only. Estimates assume that taxpayers would adjust their investment portfolio and optimally pay down their mortgage balance if their tax benefit from mortgage interest were reduced.
(2) Tax units with negative cash income are excluded from the lowest income class but are included in the totals. For a description of cash income, see http://www.taxpolicycenter.org/TaxModel/income.cfm.
(3) Includes both filing and nonfiling units but excludes those that are dependents of other tax units.
(4) After-tax income is cash income less individual income tax net of refundable credits, corporate income tax, payroll taxes (Social Security and
(5) Average federal tax (includes individual and corporate income tax, payroll taxes for Social Security and Medicare, and the estate tax) as a percentage of average cash income.

Appendix Table B2

Option 2: Phase Down Deduction Over 5 Years, Immediate $500,000 Mortgage Cap

Baseline: Current Law

Distribution of Federal Tax Change by Cash Income Level, 2015 [1]

Cash Income Level (thousands of 2011 dollars) [2]	Tax Units with Tax Increase or Cut [3]				Pct Change in After-Tax Income [4]	Share of Total Federal Tax Change	Average Federal Tax Change ($)	Average Federal Tax Rate[5]	
	With Tax Cut		With Tax Increase						
	Pct of Tax Units	Avg Tax Cut	Pct of Tax Units	Avg Tax Increase				Change (Pct Points)	Under the Proposal
Less than 10	*	**	0.0	0	0.0	0.0	0	0.0	4.9
10–20	3.4	-164	*	**	0.0	-0.3	-6	0.0	3.8
20–30	11.0	-269	0.2	221	0.1	-1.3	-29	-0.1	9.5
30–40	24.1	-330	0.9	220	0.2	-2.8	-78	-0.2	13.6
40–50	31.6	-381	3.7	241	0.3	-3.4	-112	-0.2	16.4
50–75	28.9	-418	17.4	533	0.1	-1.5	-28	0.0	19.2
75–100	14.5	-436	41.0	781	-0.4	8.4	257	0.3	22.0
100–200	4.6	-461	60.5	1,431	-0.8	44.4	845	0.6	25.6
200–500	0.8	-595	65.0	4,126	-1.2	41.6	2,677	0.9	28.6
500–1,000	1.0	-1,022	53.2	7,283	-0.8	10.1	3,862	0.5	30.2
More than 1,000	0.6	-1,080	36.8	9,727	-0.2	4.8	3,574	0.1	36.0
All	12.9	-373	18.3	1,733	-0.4	100.0	269	0.3	24.3
Addendum									
100–125	6.7	-479	55.2	1,061	-0.6	12.2	553	2.0	0.1
125–150	4.1	-415	61.7	1,324	-0.7	12.2	800	2.2	0.1
150–175	2.3	-487	65.4	1,640	-0.8	9.9	1,062	2.4	0.1
175–200	1.3	-413	69.8	2,445	-1.2	10.2	1,702	3.2	0.1

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0411-2).
Number of AMT Taxpayers (millions). Baseline: 27.0 Proposal: 28.7
* Less than 0.05
** Insufficient data
(1) Calendar year. Baseline is current law. Proposal would reduce mortgage interest deduction to 15 percent over five years and then completely replace this deduction with a 15 percent nonrefundable credit for mortgage interest. Deduction would be limited to 19 percent for 2015. Both the credit and the deduction will be limited to the first $500,000 of a mortgage on primary residence only. Estimates assume that taxpayers would adjust their investment portfolio and optimally pay down their mortgage balance if their tax benefit from mortgage interest were reduced.
(2) Tax units with negative cash income are excluded from the lowest income class but are included in the totals. For a description of cash income, see http://www.taxpolicycenter.org/TaxModel/income.cfm.
(3) Includes both filing and nonfiling units but excludes those that are dependents of other tax units.
(4) After-tax income is cash income less individual income tax net of refundable credits, corporate income tax, payroll taxes (Social Security and
(5) Average federal tax (includes individual and corporate income tax, payroll taxes for Social Security and Medicare, and the estate tax) as a percentage of average cash income.

Appendix Table B3
Option 3: Phase Down Deduction Over 5 Years, Phase In Mortgage Cap Over 5 Years
Baseline: Current Law
Distribution of Federal Tax Change by Cash Income Level, 2015 [1]

Cash Income Level (thousands of 2011 dollars) [2]	Tax Units with Tax Increase or Cut [3]				Pct Change in After-Tax Income [4]	Share of Total Federal Tax Change	Average Federal Tax Change ($)	Average Federal Tax Rate[5]	
	With Tax Cut		With Tax Increase						
	Pct of Tax Units	Avg Tax Cut	Pct of Tax Units	Avg Tax Increase				Change (Pct Points)	Under the Proposal
Less than 10	*	**	0.0	0	0.0	0.0	0	0.0	4.9
10–20	3.4	-164	*	**	0.0	-0.3	-6	0.0	3.8
20–30	11.0	-269	0.2	221	0.1	-1.4	-29	-0.1	9.5
30–40	24.1	-330	0.8	219	0.2	-3.0	-78	-0.2	13.6
40–50	31.6	-381	3.5	221	0.3	-3.6	-113	-0.2	16.4
50–75	29.0	-418	17.2	523	0.1	-1.7	-31	-0.1	19.2
75–100	14.6	-435	40.8	755	-0.3	8.4	245	0.3	22.0
100–200	4.6	-461	60.5	1,376	-0.7	44.5	812	0.6	25.5
200–500	0.8	-597	65.0	4,010	-1.2	42.1	2,601	0.9	28.6
500–1,000	1.0	-1,023	53.1	7,051	-0.7	10.2	3,737	0.5	30.2
More than 1,000	0.6	-1,080	36.8	9,421	-0.2	4.8	3,461	0.1	36.0
All	12.9	-373	18.2	1,681	-0.4	100.0	258	0.3	24.3
Addendum									
100–125	6.7	-479	55.1	1,027	-0.6	12.3	534	1.9	0.1
125–150	4.1	-417	61.7	1,269	-0.7	12.1	766	2.1	0.1
150–175	2.3	-485	65.4	1,568	-0.8	9.8	1,014	2.3	0.1
175–200	1.3	-413	69.8	2,360	-1.1	10.2	1,643	3.1	0.1

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0411-2).
Number of AMT Taxpayers (millions). Baseline: 27.0 Proposal: 28.7
* Less than 0.05
** Insufficient data
(1) Calendar year. Baseline is current law. Proposal would reduce mortgage interest deduction to 15 percent over five years and then completely replace this deduction with a 15 percent nonrefundable credit for mortgage interest. Deduction would be limited to 19 percent for 2015. Both the credit and the deduction would be limited to the first $600,000 of a mortgage on primary residence only in 2015. Estimates assume that taxpayers would adjust their investment portfolio and optimally pay down their mortgage balance if their tax benefit from mortgage interest were reduced.
(2) Tax units with negative cash income are excluded from the lowest income class but are included in the totals. For a description of cash income, see http://www.taxpolicycenter.org/TaxModel/income.cfm.
(3) Includes both filing and nonfiling units but excludes those that are dependents of other tax units.
(4) After-tax income is cash income less individual income tax net of refundable credits, corporate income tax, payroll taxes (Social Security and
(5) Average federal tax (includes individual and corporate income tax, payroll taxes for Social Security and Medicare, and the estate tax) as a percentage of average cash income.

Appendix Table B4
Option 4: Phase Down Deduction Over 10 Year, Immediate $500,000 Mortgage Cap
Baseline: Current Law
Distribution of Federal Tax Change by Cash Income Level, 2015 [1]

Cash Income Level (thousands of 2011 dollars) [2]	Tax Units with Tax Increase or Cut [3]				Pct Change in After-Tax Income [4]	Share of Total Federal Tax Change	Average Federal Tax Change ($)	Average Federal Tax Rate[5]	
	With Tax Cut		With Tax Increase						
	Pct of Tax Units	Avg Tax Cut	Pct of Tax Units	Avg Tax Increase				Change (Pct Points)	Under the Proposal
Less than 10	*	**	0.0	0	0.0	0.0	0	0.0	4.9
10–20	3.4	-164	*	**	0.0	-0.5	-6	0.0	3.8
20–30	11.0	-269	0.2	204	0.1	-2.1	-29	-0.1	9.5
30–40	24.1	-330	0.7	208	0.2	-4.6	-78	-0.2	13.6
40–50	31.6	-381	2.5	201	0.3	-5.7	-115	-0.2	16.4
50–75	29.0	-417	12.0	191	0.2	-8.4	-98	-0.2	19.1
75–100	14.7	-432	23.3	342	0.0	0.9	16	0.0	21.7
100–200	4.6	-460	40.5	917	-0.3	29.9	350	0.2	25.2
200–500	0.8	-591	63.9	4,123	-1.2	66.5	2,631	0.9	28.6
500–1,000	1.0	-1,022	52.8	7,307	-0.8	16.4	3,847	0.5	30.2
More than 1,000	0.6	-1,080	36.8	9,717	-0.2	7.7	3,567	0.1	36.0
All	12.9	-373	13.0	1,648	-0.3	100.0	165	0.2	24.2
Addendum									
100–125	6.8	-477	31.0	510	-0.1	4.5	126	0.4	0.0
125–150	4.1	-415	38.2	727	-0.2	6.4	260	0.7	0.0
150–175	2.3	-487	49.8	857	-0.3	6.3	415	0.9	0.0
175–200	1.3	-413	67.1	1,955	-0.9	12.7	1,307	2.5	0.1

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0411-2).
Number of AMT Taxpayers (millions). Baseline: 27.0 Proposal: 27.7
* Less than 0.05
** Insufficient data
(1) Calendar year. Baseline is current law. Proposal would reduce mortgage interest deduction to 15 percent over 10 years and then completely replace this deduction with a 15 percent nonrefundable credit for mortgage interest. Deduction would be limited to 27 percent for 2015. Both the credit and the deduction will be limited to the first $500,000 of a mortgage on primary residence only. Estimates assume that taxpayers would adjust their investment portfolio and optimally pay down their mortgage balance if their tax benefit from mortgage interest were reduced.
(2) Tax units with negative cash income are excluded from the lowest income class but are included in the totals. For a description of cash income, see http://www.taxpolicycenter.org/TaxModel/income.cfm.
(3) Includes both filing and nonfiling units but excludes those that are dependents of other tax units.
(4) After-tax income is cash income less individual income tax net of refundable credits, corporate income tax, payroll taxes (Social Security and
(5) Average federal tax (includes individual and corporate income tax, payroll taxes for Social Security and Medicare, and the estate tax) as a percentage of average cash income.

Appendix Table B5

Option 5: Phase Down Deduction Over 10 Years, Phase In Mortgage Cap Over 10 Years

Baseline: Current Law

Distribution of Federal Tax Change by Cash Income Level, 2015 [1]

Cash Income Level (thousands of 2011 dollars) [2]	Tax Units with Tax Increase or Cut [3]				Pct Change in After-Tax Income [4]	Share of Total Federal Tax Change	Average Federal Tax Change ($)	Average Federal Tax Rate[5]	
	With Tax Cut		With Tax Increase						
	Pct of Tax Units	Avg Tax Cut	Pct of Tax Units	Avg Tax Increase				Change (Pct Points)	Under the Proposal
Less than 10	*	**	0.0	0	0.0	0.0	0	0.0	4.9
10–20	3.4	-164	*	**	0.0	-0.6	-6	0.0	3.8
20–30	11.0	-269	0.2	204	0.1	-2.5	-29	-0.1	9.5
30–40	24.1	-330	0.7	207	0.2	-5.4	-78	-0.2	13.6
40–50	31.7	-381	2.2	166	0.3	-6.7	-117	-0.2	16.4
50–75	29.1	-418	11.5	163	0.2	-10.4	-103	-0.2	19.1
75–100	14.8	-430	22.0	258	0.0	-0.4	-7	0.0	21.7
100–200	4.6	-460	38.7	748	-0.3	26.9	268	0.2	25.2
200–500	0.8	-594	63.9	3,878	-1.1	73.2	2,471	0.8	28.5
500–1,000	1.0	-1,024	52.8	6,745	-0.7	17.7	3,549	0.5	30.2
More than 1,000	0.6	-1,080	36.8	8,936	-0.2	8.3	3,280	0.1	36.0
All	12.9	-373	12.5	1,516	-0.2	100.0	141	0.2	24.2
Addendum									
100–125	6.8	-476	29.2	381	-0.1	3.3	79	0.3	0.0
125–150	4.1	-418	35.9	531	-0.2	5.0	174	0.5	0.0
150–175	2.3	-486	47.8	630	-0.2	5.1	290	0.7	0.0
175–200	1.3	-413	66.6	1,773	-0.8	13.4	1,176	2.2	0.1

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0411-2).
Number of AMT Taxpayers (millions). Baseline: 27.0 Proposal: 27.7
* Less than 0.05
** Insufficient data
(1) Calendar year. Baseline is current law. Proposal would reduce mortgage interest deduction to 15 percent over 10 years and then completely replace this deduction with a 15 percent nonrefundable credit for mortgage interest. Deduction would be limited to 27 percent for 2015. Both the credit and the deduction would be limited to the first $800,000 of a mortgage on primary residence only in 2015. Estimates assume that taxpayers would adjust their investment portfolio and optimally pay down their mortgage balance if their tax benefit from mortgage interest were reduced.
(2) Tax units with negative cash income are excluded from the lowest income class but are included in the totals. For a description of cash income, see http://www.taxpolicycenter.org/TaxModel/income.cfm.
(3) Includes both filing and nonfiling units but excludes those that are dependents of other tax units.
(4) After-tax income is cash income less individual income tax net of refundable credits, corporate income tax, payroll taxes (Social Security and
(5) Average federal tax (includes individual and corporate income tax, payroll taxes for Social Security and Medicare, and the estate tax) as a percentage of average cash income.

Appendix Table B6

Benefits from Mortgage Interest Deduction and 15 percent Nonrefundable Credit, 2015 [1]

Baseline: Current Law

Cash Income Level (thousands of 2011 dollars)	Tax Units (thousands) [3]	Current Mortgage Interest Deduction				Proposal: 15 Percent Non-refundable Credit [2]			
		Tax Units with Benefit		Average Benefit (dollars)		Tax Units with Benefit		Average Benefit (dollars)	
		Number (thousands)	Percent within Class	All Tax Units	Tax Units with Benefit	Number (thousands)	Percent within Class	All Tax Units	Tax Units with Benefit
Less than 10	18,828	0	0.0	0	0	0	0.0	0	41
10–20	26,753	214	0.8	3	416	1,043	3.9	9	232
20–30	20,164	665	3.3	24	716	2,500	12.4	53	429
30–40	16,562	1,457	8.8	67	765	4,588	27.7	145	524
40–50	13,738	2,459	17.9	180	1,005	5,427	39.5	285	721
50–75	24,031	7,762	32.3	509	1,573	12,184	50.7	492	972
75–100	14,893	7,238	48.6	1,164	2,395	8,489	57.0	771	1,353
100–125	10,050	5,829	58.0	1,753	3,023	6,221	61.9	987	1,594
125–150	6,907	4,421	64.0	2,243	3,506	4,538	65.7	1,173	1,786
150–175	4,215	2,807	66.6	2,703	4,057	2,841	67.4	1,321	1,960
175–200	2,715	1,917	70.6	3,257	4,613	1,925	70.9	1,363	1,922
200–500	7,059	4,532	64.2	4,034	6,278	4,560	64.6	1,397	2,161
500–1,000	1,187	613	51.6	4,950	9,598	617	52.0	1,299	2,497
More than 1,000	603	204	33.9	3,720	10,972	212	35.2	948	2,691
All	168,946	40,209	23.8	732	3,080	55,077	32.6	416	1,273

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0411-2).

(1) Calendar year.

(2) The proposal would also limit the amount of deductible interest to the first $500,000 of a mortgage on a primary residence only. Estimates include a microdynamic behavioral response and assume that taxpayers would adjust their investment portfolio and optimally pay down their mortgage balance if their tax benefit from mortgage interest were reduced.

(3) Includes both filing and nonfiling units but excludes those that are dependents of other tax units.