Housing Policy and the Social Benefits of Homeownership

BY N. EDWARD COULSON

The major subsidies to homeownership arise from the U.S. tax code, and the costs of these subsidies are high. Are the social benefits from homeownership sufficient to warrant such subsidies? In this article, Ed Coulson reviews the research on the social benefits of ownership and some related questions. The evidence indicates that homeownership does carry substantial social benefits, but their dollar value remains uncertain.

Homeownership has long been a goal of social policy in the United States, and programs to promote it have been extraordinarily successful, at least on the surface. The homeownership rate — the percentage of households that live in housing units that they own — has risen from around 40 percent before World War II, to around 65 percent today. This pronounced rise has surely been in part due to the subsidies that owner-occupied housing has received. The major subsidies to homeownership arise from the U.S. income tax code, and their costs are high.

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Are such subsidies warranted? They can be if the social benefits from homeownership — the benefits received by those other than the homeowners themselves — are substantial. A variety of potential social benefits have been discussed in the economics literature. The evidence indicates that homeownership carries substantial social benefits, but their dollar value remains uncertain.

HOMEOWNERSHIP AND ITS SUBSIDIES

Although many institutions that encourage homeownership (such as the Federal Home Loan Bank System and the Federal Housing Administration) were established in the 1930s and 1940s, the oldest, and perhaps most powerful, incentives for ownership lie in the federal income tax code. The two most important such incentives have been part of the code since its formation in 1913: the exclusion of rental income in an owner-occupied unit and the deductibility of mortgage interest.[1]

Tax Subsidies and Their Effects. As Satyajit Chatterjee explained in an earlier issue of the *Business Review*, the owner of a piece of real estate might consider renting it to another household and live in a rental unit somewhere else. Although some people might want to do this (say, if they become empty-nesters and wish to live in a smaller unit), the tax system discourages this behavior because the rental income that others pay a landlord is taxable income for the landlord, whereas if we own the house we live in, we pay ourselves rent, which is not taxed. The Internal Revenue Service doesn't consider this rent to oneself to be part of a homeowner's income (and you probably don't either) presumably because there's no record of any transaction taking place and no funds changing hands. Nevertheless this rental income is as real as the house you live in and provides a major subsidy to homeownership.[2] As Chatterjee also pointed out, the deductibility of mortgage interest, while far more "visible" than the exclusion of rent, is, in reality, a

[1] Owner-occupied housing is also subsidized through the exclusion of the first $250,000 to $500,000 in capital gains from the sale of the unit and through the deductibility of local and state property taxes (see the article by Steven Bourassa and William Grigsby). Evidence suggests that these are less important in terms of their impact on the economy or tax collections than the exclusion of rental income and the deductibility of mortgage interest.

[2] Indeed, a number of European countries tax this implicit income. Whether such a tax can be administered fairly is an open question, since the absence of an actual record of the transaction leaves unknown the dollar amount of the implicit rent.

device that allows those who finance the purchase of their homes to have the same tax advantages (with regard to the rent excludability) as those who own their homes outright.

In a 1991 study, James Follain and David Ling estimated that the loss in federal tax revenue from those two provisions was in excess of $100 billion in 1988, and it is almost assuredly larger than that today.[3] More important, these tax breaks can give rise to "overinvestment" in housing. Overinvestment in this context means that the treatment of housing in the tax code causes people to invest more in housing (by becoming homeowners or buying a larger house) and less in other investment vehicles than would otherwise be the case. That, after all, is the point. But people do this because housing is cheaper than other investments, or, in what amounts to the same thing, housing has a higher rate of return because of the tax breaks. This gives housing an advantage over an investment whose return is taxed in the ordinary way.

This can be bad for the economy as a whole because some housing investments, for example, the ones that wouldn't get built if there were no tax breaks, are driving out investments that have a higher rate of return before taxes. This brings down the aggregate value of gross domestic product (GDP), that is, what the country produces. So, to the extent that GDP measures our well-being, this overinvestment in housing is not good, as noted by Edwin Mills in a 1987 *Business Review* article. This overinvestment is perhaps substantial; the most recent estimate — 1998 — comes from a study by Lori Taylor, who claims that roughly $200 billion in GDP is lost each year because of this misallocation of capital.[4]

In addition, it is somewhat disconcerting that these tax preferences are more beneficial to homeowners with higher levels of income because the value of the tax deductions is directly linked to the marginal tax bracket of the household. When you are in the 27 percent bracket, the government is in effect paying 27 percent of your mortgage interest bill each month. But if your income is low enough to qualify you for the 15 percent bracket, the government pays only 15 percent. The largest subsidies go to those in the highest tax brackets, that is, those with the highest income.

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Moreover, the subsidies to owner-occupied housing are thought to be responsible, at least in part, for other problems in the economy. One of these is urban sprawl. In a 1999 article in the *Business Review*, Richard Voith argued that the desire for larger amounts of space, spurred by the tax treatment described above, pushes the borders of urban areas beyond what is desirable. Another economist, Andrew Oswald, has argued that homeownership is directly tied to unemployment. To become owners, people spend a great deal of time and money upfront in the form of search costs, finance charges, and the like. Therefore, they are more closely tied, both financially and psychologically, to their dwellings than renters are. Consequently, owners are reluctant to move when their job prospects change. Oswald presents some evidence for this from European countries. The article by Coulson and Fisher finds little support for this link in the United States.

Why Subsidize Homeownership? If subsidizing homeownership has such negative effects on the economy, why are there such lucrative tax incentives in its favor? One argument is simply that homeownership is a good thing. Not only is it part of the American dream, but it's also something that people "should" have, in the same way that they "should" have medical care or even food. And since we have programs such as Medicare and food stamps that lower the price of these goods, why not programs for homeownership as well?

Such "merit good" arguments, as they are called, are unsatisfactory. On the one hand, if the goal is to simply make people better off, the government could just provide cash or lower tax rates to all households and avoid the misallocation of capital described above. On the other hand, providing tax breaks for any commodity, for no other reason than that it's good for consumers, smacks of paternalism — the notion that the

[3] The mortgage interest deduction on its own accounted for only about 10 percent of this figure. Presumably, the $100 billion figure would be higher today, since more households are owners and marginal tax rates have increased in the top brackets since then (which increases the value of the deduction).

[4] The method used by both Mills and Taylor involves calculating the real rate of return to housing and nonhousing capital. Each of these authors finds that the marginal return to housing is less than the marginal return to nonhousing capital. They infer from this that GDP would be higher if investment were shifted out of housing. Their method thus assesses the overinvestment that arises from all forms of housing policy preferences, including the tax features noted above. It cannot separate out the subsidies directed to owner-occupied housing from those directed to landlords, such as accelerated depreciation, nor to consumers of rental properties such as public housing. Nevertheless, since two-thirds of households live in owner-occupied dwellings, and given the large estimated loss in revenue from the rental exclusion, it seems clear that much of the difference noted by Mills and Taylor arises from subsidies to this group.

government somehow knows what is good for its citizens. Economists tend to reject such views. They prefer to let people make their own choices as much as possible.

Can Subsidies Be a Good Thing for Everyone? In spite of these drawbacks, can a case be made for providing tax incentives for owner-occupied housing? Yes, *if homeownership provides benefits to people other than the homeowners themselves*. Why does this matter? Suppose that all the houses along some street would benefit if one house in particular — call it the Smith residence — were converted from a rental property to an owner-occupied property. (Why they would so benefit will be discussed in a moment.)

In a perfect world, the street's residents would all get together, figure out how much they would value this conversion, get that much money together, take it over to the Smiths, and tell them to buy the unit. The Smiths may or may not take the money. That would depend on whether these contributions, when added to the money the Smiths themselves put into the pot, exceeded the cost of the conversion. But what's important is that in this perfect world, the right decision would be made. By "right," we simply mean the change in status from renting to owning should come about when, and only when, the total benefits are greater than the total costs. The total benefits include those that accrue both to the Smiths and to the Smiths' neighbors. The Smiths, in making the decision about ownership, are normally going to think only about their *private* benefits. The neighbors' contributions are necessary to get the Smiths to consider the *external,* or *social,* benefits. These contributions lower the price of ownership to the Smiths, causing them to *internalize, or take into consideration, the external benefit.*

But all this would happen in a perfect world. In the real, imperfect world, neighbors would not, under ordinary circumstances, make these contributions. The mere costs of coordinating the rest of the neighborhood would be enough to dissuade most people from implementing this scheme. Also, most people would find it difficult to guess how much benefit they would receive and so would not really know what the right contribution was. Perhaps most important, everyone would wait for other people to make their contributions first and hope that this would be enough. They would try to be what economists call free riders: They would try to get the benefit without paying the cost. And the Smiths would stay renters.

This is where the government might have a motive to step in. The tax incentives described above are a way of making the contributions that the neighbors would have made in the perfect world. They are an attempt to replicate what the private market would have done under ideal circumstances, but has failed to do.

WHY ARE HOMEOWNERS BETTER NEIGHBORS?

Homeownership Carries Incentives. In the previous scenario, the neighbors were willing to "bribe" the Smiths into becoming homeowners in the belief that ownership would make them better neighbors — homeownership would, in some way, change their behavior. Economists call this removing the *moral hazard* associated with renting. The moral hazard in this case involves an incentive to behave "badly" because renting provides less incentive to behave "well."[5] In what ways does ownership mitigate moral hazard? First, owners stay longer than renters because buying a house involves a lot of upfront costs that don't arise when you rent. There are transfer taxes, legal fees, and mortgage points to be paid, as well as hidden costs such as the time it takes to find just the right house or condo. These are not costs that households want to pay annually, so people become owners only when they are reasonably sure that they won't have to pay them again for a long time. Because owners usually live in their units for a longer time, the payoff from good behavior will be larger.

> [Another] thing that makes renters and owners behave differently is that ... owners reap the rewards of any improvements; renters do not.

The second thing that makes renters and owners behave differently is that (regardless of time spent) owners reap the rewards of any improvements; renters do not. When it comes time to sell the unit, the price will reflect the wear and tear to the residence and any deterioration to the neighborhood. Renters never see a return on any maintenance or care they may put into the unit; hence, they have less incentive to do so.

While these can be powerful incentives, it's possible that the cause and effect in the above arguments are backward. It may be that the differences in behavior are unaffected by whether a household owns or rents and that the choice to own or rent is motivated by the behavior itself.

How can this happen? Casual observation can confirm what research

[5] Moral hazard often comes up in the analysis of insurance markets, where being insured against bad outcomes (illness, traffic accidents) tempts people into risky behavior that leads to these same outcomes.

has shown: that owners are, on average, older, better educated, and richer than renters.[6] (See *Homeownership in the United States.*) They are more often married couples and, if they are not retired, have more children living at home. These demographic differences can be powerful influences on how one behaves, regardless of whether one is a homeowner. Another important difference is that owners most of the time live in single-family detached housing units, while renters usually live in multi-unit structures. Any number of these factors *could* cause the kind of social benefits that we might mistakenly associate with the choice to own or rent. Therefore, it would be a grave mistake to simply compare renters' and owners' behavior and attribute any difference to the fact that their housing choices are different.

In the discussion below, a number of studies that compare renters' and owners' behavior are analyzed. None of them makes the mistake of simply comparing the two groups; all of them use a statistical tool called multiple regression analysis, which allows the analyst to factor in other "controls" to isolate the "pure" effect of homeownership on behavior. For example, if the multiple regression analysis "controls" for income while measuring the effect of the choice to own or rent, it allows us to separate the influences of income and ownership on behavior. In effect, it shows how owners and renters with identical incomes would behave differently. Clearly, a fair number of controls are necessary in order to isolate the pure impact of homeownership — that is, the change in behavior that arises from becoming a homeowner.

[6] See the article by Allen Goodman; the article by L.M. Segal and D.G. Sullivan; and my 1999 article.

Homeownership Influences Behavior. For the most part, the studies discussed above all provide a large number of such controls; nevertheless, the reader might retain the suspicion that homeowners are different in some deeper sense. Homeownership might be motivated by a desire to have property of one's own, a desire for stability, and pride of ownership, things that cannot be easily captured by age, income, or other variables that we can measure in a survey. Nevertheless, we can gain some insight into how these motivations might affect other behavior by looking at the

ownership decision itself. Much of the research described below uses even more sophisticated statistical techniques to analyze who buys a house and who doesn't and separates the motivations to become a homeowner into observable ones (income, kids, and so forth) and unobservable ones. By doing this, we can estimate the unobservable motivation and use it as a control when looking at the behavioral differences of owners and renters, thus providing greater credibility to these measurements.

What, then, does the research show? We examine three behavioral dimensions in which differences between homeowners and renters are observed: maintenance, child-rearing, and citizenship.

Maintenance. A strong argument can be made that owner-occupants maintain their dwellings to a greater extent than renters (or landlords) maintain theirs.[7] Generally, renters don't maintain rental units as well as homeowners maintain their houses precisely because owners reap the benefit of good maintenance. The very act of becoming an owner leads people to behave differently toward their property because they have a financial incentive to do so. Thus, the moral hazard argument for improved maintenance in owner-occupied housing is straightforward.

On the other hand, it may be the case that renters are renters because of their ingrained behavior and that the difference is due to adverse selection. Imagine that the world has two kinds of people: sloppy and neat. When these two types of homeowners try to sell their respective properties, sloppy people pay for their behavior because they realize a lower selling price. Neat people are rewarded for the time they invested in being neat in the form of higher prices.

But notice that when sloppy people are renters, the landlord pays the price of sloppy behavior and reaps the rewards from having neat tenants. What does a landlord do when faced with this kind of market? She probably can't tell which type of tenant is moving in. If she could, she would try to charge sloppy renters a higher rent. Instead, she has to raise rents for *all* tenants or impose security deposits to cover the possibility that a new tenant is a sloppy person. But either of these strategies is going to drive

[7] Landlords have an incentive to maintain their units, but it is more costly for them to do so than it is for owner-occupants. Among other things, problems are harder to observe because landlords do not live on the property.

the neat tenants away because now homeownership is going to look like a much better deal to a typical neat person: He doesn't have to help pay for sloppy people's behavior, and he doesn't have to risk not getting his security deposit back from a dishonest landlord. Conversely, renting looks like a great deal to sloppy people because they might not have to pay the full cost of their behavior. So now most of the rental applicants will be sloppy people.

While something of a simplification, the above analysis serves to demonstrate that renters aren't going to be as careful as owner-occupants and that while landlords clearly have an incentive to maintain their units, they are not going to provide upkeep as easily or as cheaply as an owner-occupant.[8] When this happens, it causes a neighborhood externality.[9]

Various pieces of evidence suggest that this sort of thing happens. In what seems to be the only direct test, George Galster found that more money is spent on maintaining owner-occupied housing than is spent on maintaining rental property. Interestingly, he also found that the effect was greater for low-income households. Denise DiPasquale and Edward Glaeser found that homeowners spend more time gardening than renters. Equally important, though less direct, is the evidence provided by studies that test whether rental property depreciates faster than owner-occupied property. Depreciation and maintenance are two sides of the same coin: When money is spent on maintenance, it slows down the rate of depreciation. James Shilling, C.F. Sirmans, and Jonathan Dombrow compared depreciation rates of single-family houses that were tenant-occupied with ones that were owner-occupied and found that, in fact, the rental units depreciated significantly faster.

Is this difference due to homeownership per se or to inherent differences in owners and renters? Galster's regression analysis contained a number of important controls, including a number of family demographic characteristics and length of time in the unit. DiPasquale and Glaeser also had a large number of controls for demographic characteristics and building type, and they also used the more sophisticated statistical techniques that control for the unobservable factors that lead to homeownership. Perhaps the most compelling, though somewhat indirect, evidence is from a study by John Harding, Thomas Miceli, and C.F. Sirmans, who found that owners on the brink of defaulting on their mortgage loans engaged in less maintenance than other owners. Thus, *owners who become more like renters* (in the sense of having less financial stake in their property) have less incentive to maintain their units, which provides additional evidence of moral hazard in maintenance.[10]

Child-Rearing. Children can also create external effects in neighborhoods. According to a study by Richard Green and Michelle White, bad behavior of children — a homeowner's own or his neighbors' — "may reduce the attractiveness of the neighborhood and threaten the value of [the] homes. Thus, homeowners have a stronger incentive than renters to monitor their own children and their neighbors' children." The higher stake that homeowners have in the quality of their neighborhoods causes them to raise better children to the benefit of all.

Although it's difficult to measure the behavior of children directly, there are a number of indicators we can observe. Prominent among these are the quality and level of education children receive. While educational attainment is not a direct measure of neighborhood quality, the long tradition of public education in the United States attests to a societal belief that the education of children has significant external benefits. A number of studies have asked whether children in renter and owner households receive different education when other factors are held constant.

In fact, Green and White found that homeowners' children are less likely to drop out of school. Interestingly, the effect appears to be more pronounced in families with lower incomes: A high-schooler in a family with $40,000 in income (in 1980, the census year from which their data are drawn) is 4 percent less likely to drop out of school when the family owns its own home. However, for families with an income of just $10,000 there is a 9 percent decline in dropout rates. A similar study by D. Haurin, T. Parcel, and R. Haurin measured the educational attainment of children as a function of homeownership (among other things) and found that math and reading scores were about 7 to 9 percent higher for the children of homeowners.

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[8] There is always the possibility of too much maintenance. The act of maintaining one's property may create noise, for example, from a hammer or lawnmower, and possibly other inconveniences for one's neighbors.

[9] An externality, or spillover, is an uncompensated benefit or cost that results from the actions of an individual or group. For example, when a property owner does not maintain his property, others in the neighborhood may incur the cost in the form of lower property values, and they are not compensated for the decline in values. Similarly, when a property owner maintains her property, others in the neighborhood may benefit in the form of higher property values, and they do not have to contribute to the cost of maintenance.

[10] Such occupants may spend less because of financial constraints, although the financial return to maintenance provides incentives to keep up the property, even for those most constrained. These authors also speculate that many kinds of maintenance are not particularly visible and, therefore, may not pay off upon sale of the unit. They found little evidence that this is the case, though, and anyway this sort of maintenance is not going to cause the kind of neighborhood externality under discussion here.

Homeownership also appears to improve noneducational measures of behavior that may have external consequences. For example, Green and White found that the probability that a girl in an "average" household will become pregnant while in high school decreases from roughly 13 percent to 11 percent if her family owns its home. Haurin, Parcel, and Haurin found that an index of behavioral problems of younger children declines about 3 percent for children from an owner-occupied dwelling.

Citizenship. The greater commitment that homeowners presumably have toward their neighborhoods might very well manifest itself in greater socialization with neighbors, civic participation, volunteerism, and the like. These activities have obvious external benefits for the neighbors, who can "free ride" on others' efforts to make the community a better place to live. To the extent that homeownership does encourage this kind of behavior, it provides a powerful argument for subsidizing ownership. On the 50th anniversary of the Housing Act of 1949, former Secretary of Housing and Urban Development Andrew Cuomo said: "Housing is more than just bricks and mortar; it is the building block of community, it is powerfully tied to civic behavior — to working together with neighbors on shared concerns, to literally making us a part of a block, a neighborhood, a town, a county, a nation. Homeownership makes us stakeholders in something grander than ourselves."[11]

Do homeowners behave in the way that Secretary Cuomo suggests? In a 1996 study, Peter Rossi and Eleanor Weber used the General Social Survey and other data to compare the actions of renters and owners, actions that

[11] Secretary Cuomo's speech is available in its entirety at http://www.hud.gov/library/bookshelf18/pressrel/nanm.html.

Homeownership in the United States

The U.S. Census Bureau defines the homeownership rate as the percentage of households that own the unit in which they live.[a] This rate increased more or less steadily throughout the 1990s, particularly after 1994. However, there are significant differences in homeownership rates across regions, ethnic groups, and other demographic dimensions of U.S. society. To the extent that homeownership is responsible — as the text of the article proposes — for maintaining the social capital of a neighborhood or larger area, policymakers are right to be concerned when homeownership rates for particular groups are low, especially when groups are concentrated in certain areas.

For example, large differences in homeownership rates exist across the different regions of the U.S. (Figure 1). Ownership rates are quite high in the Midwest and South but much lower in the Northeast and West. In a forthcoming study, I found that much of these differences can be traced to the character of large northeastern cities, particularly New York City, which has a higher concentration of high-density urban housing, which leads to more rental housing and higher prices for homeownership. Higher prices for ownership (versus rental rates) also hinder the growth of owner-occupied housing in the West (particularly in California and Hawaii). Both of these low-homeownership regions also are home to large numbers of immigrants (both foreign and domestic), who tend not to become homeowners for a number of years after arriving at their new locations.

Immigration from other countries also helps explain the potentially puzzling differences seen in Figure 2, which plots historical homeownership trends for whites, blacks, Hispanic-Americans, and "others" (primarily Asian-Americans). It is clear that white households have much higher ownership rates than any other group. What is somewhat surprising is that Asian-Americans have such low rates, despite the fact that their income levels are comparable to those of whites. Recent research indicates that Asian households are more likely to be immigrant households and that immigrants of all ethnic groups are less likely to own.[b] In any case, Asian-American households are also likely to be younger and to live in the expensive Far West and Northeast regions (regardless of their immigrant status).

African-Americans have historically tended to have very low ownership rates. This is partly due to the lower income and wealth of African-American households. But these differences in resources do not completely explain the low propensity for homeownership. Some of the remaining difference may be attributed to discrimination in mortgage or real estate markets. Hispanic families have lower homeownership rates than any other ethnic groups. While Hispanics and blacks have roughly similar (low) income levels, the relatively large number of immigrants among Hispanic households tends to drive down their homeownership rate below that of African-Americans.[c]

Figure 3 gives the homeownership rate for different age groups for the head of household for 2001. This figure shows that homeowners tend to be older than renters and, therefore, more established citizens. Homeownership is very low for people in their twenties, but it rises sharply as people enter their thirties. It stays at a very high level for the remainder of one's life, declining only slightly when people reach their mid-seventies.

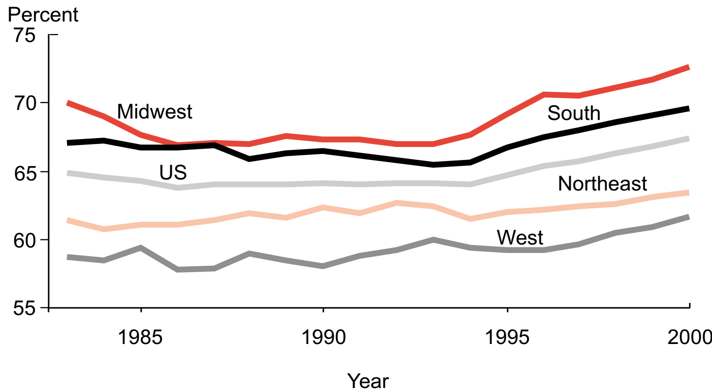
[a] "Owner" does not mean that one has completely paid off one's mortgage.

[b] See my 1999 article, and the article by G. Painter, S. Gabriel, and D. Myers.

[c] See my 1999 article.

FIGURE 1

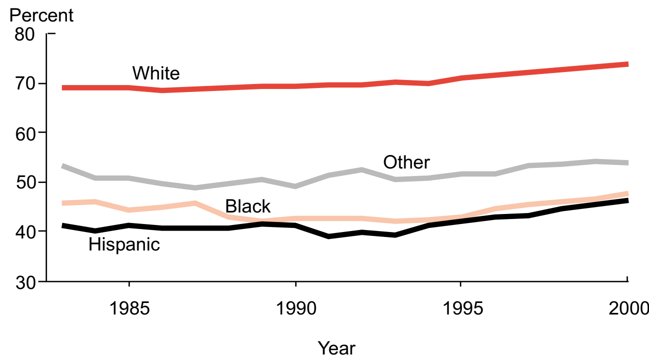
Regional Homeownership Rates, 1983-2000



Source: Department of Housing & Urban Development, Housing Market Conditions, November 2001.

FIGURE 2

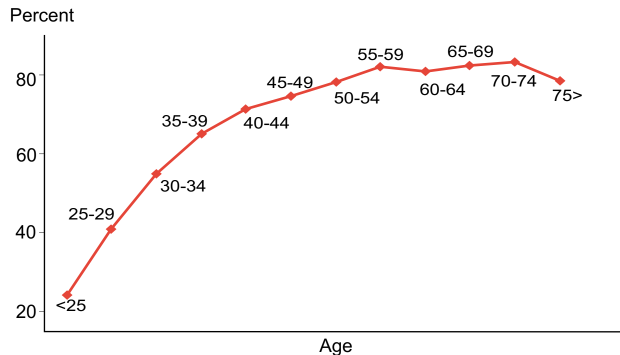
Homeownership by Ethnic Group, 1983-2000



Source: Department of Housing & Urban Development, Housing Market Conditions, November 2001.

FIGURE 3

Homeownership Rates by Age, 2001



Source: Housing Vacancy Survey, Fourth Quarter 2001, U.S. Bureau of the Census

correspond in various ways to our common perceptions of neighborliness.[12] A large number of comparisons were made, so it is not particularly surprising that the results were mixed. In some ways, renters are better neighbors than owners; in other ways, owners are superior. For example, renters are "more likely to spend evenings with neighbors," which perhaps casts some doubt on the greater "neighborliness" of owners; however, owners are more likely to "give help to others."

DiPasquale and Glaeser derived rather different conclusions from their examination of the General Social Survey. They found that homeowners consistently provide a greater degree of social benefit. Specifically, DiPasquale and Glaeser measured owners' and renters' propensity to create neighborhood benefits through tasks such as gardening, volunteering for public services, being interested in political affairs, and several other activities. In practically all of the cases that these two authors examined, owners participated more in civic activities than renters did.

The comparison between these two studies is of interest in light of the discussion above about controlling for related influences. These two studies both used the General Social Survey to gauge owner-renter differences. However, Rossi and Weber used only two controls: age and an index of socioeconomic status. While undoubtedly important, these two factors alone probably cannot isolate the pure effect of ownership. It is possible that some of the results they get arise from this problem. For example, the behavior described as "more likely to spend

[12] The General Social Survey, conducted by the National Opinion Research Center at the University of Chicago, is a survey of 1500 representative households in the United States.

evenings with neighbors" may be due to the type of structures that renters live in — multi-unit, high-density dwellings.

Indeed, an article by Edward Glaeser and Bruce Sacerdote looked at the difference in social behavior across *building type* (rather than tenure type) and found that people who lived in multi-unit buildings did socialize more than those in detached units. Thus, a failure to control for the type of structure (among other differences) may lead to misleading statements about the benefits (or lack thereof) of ownership. DiPasquale and Glaeser did control for structure type and many other differences; therefore, their results about the positive social benefits of homeownership carry somewhat more credibility. As noted above, they found that owners put more effort into gardening than renters (thereby creating the social benefit of a pleasant-looking neighborhood).

While the opportunity to garden is clearly related to the type of housing one lives in, these authors controlled for this difference and still found that owners do more than renters.

DiPasquale and Glaeser were also able to provide a deeper explanation for homeowners' more neighborly behavior. These authors related this behavior to the fact that homeowners stay in their units for a longer period of time; they're not just there for the investment. And the payoff to improving the neighborhood through participating in civic activities is higher the longer one stays.

An analysis by William Rohe and Michael Stegman indirectly supports this notion. These authors followed a group of low-income families in Baltimore as they moved from rental housing to subsidized homeownership in a newly built neighborhood. When Rohe and Stegman compared this group with a control group that stayed in rental housing, they found that owners *did not* have a greater degree of activism or involvement in the new neighborhood than renters with similar demographic characteristics. The authors attribute this, at least in part, to the fact that in this particular case, the owners' neighborhood was very new. No previous long-term residents had built up an inventory of social capital, and consequently, there was no easy way for the new residents to contribute to that inventory, despite their putative desire to do so in their role as new homeowners.

The conclusion, therefore, does not necessarily contradict that of DiPasquale and Glaeser; the work of these authors and of Rohe and Stegman is consistent with homeownership creating social benefits primarily because homeownership creates longevity and stability for neighborhoods.

THE POLICY DILEMMA

This review of research seems to indicate that homeownership provides external, or social, benefits in the form of greater maintenance and neighborhood conditions, better-raised children, and better "civic" behavior. These researchers have taken great care to overcome the objection that it's the type of people who choose ownership that makes the difference, and not the fact of owning or renting.

If we accept the evidence that homeownership does provide social benefits, the question is whether this should influence social policy. It was suggested above that it should. In the absence of some sort of subsidy to homeownership, potential home buyers will not take into account the social aspects of their decisions, and therefore, too few households will opt for ownership. We've noted that homeownership is already heavily subsidized, primarily because rental income to oneself is not taxed and mortgage interest is deductible. The questions then arise: Is this the right amount of subsidization, and is this the right way of going about it?

This review of research seems to indicate that homeownership provides external, or social, benefits in the form of greater maintenance and neighborhood conditions, better-raised children, and better "civic" behavior.

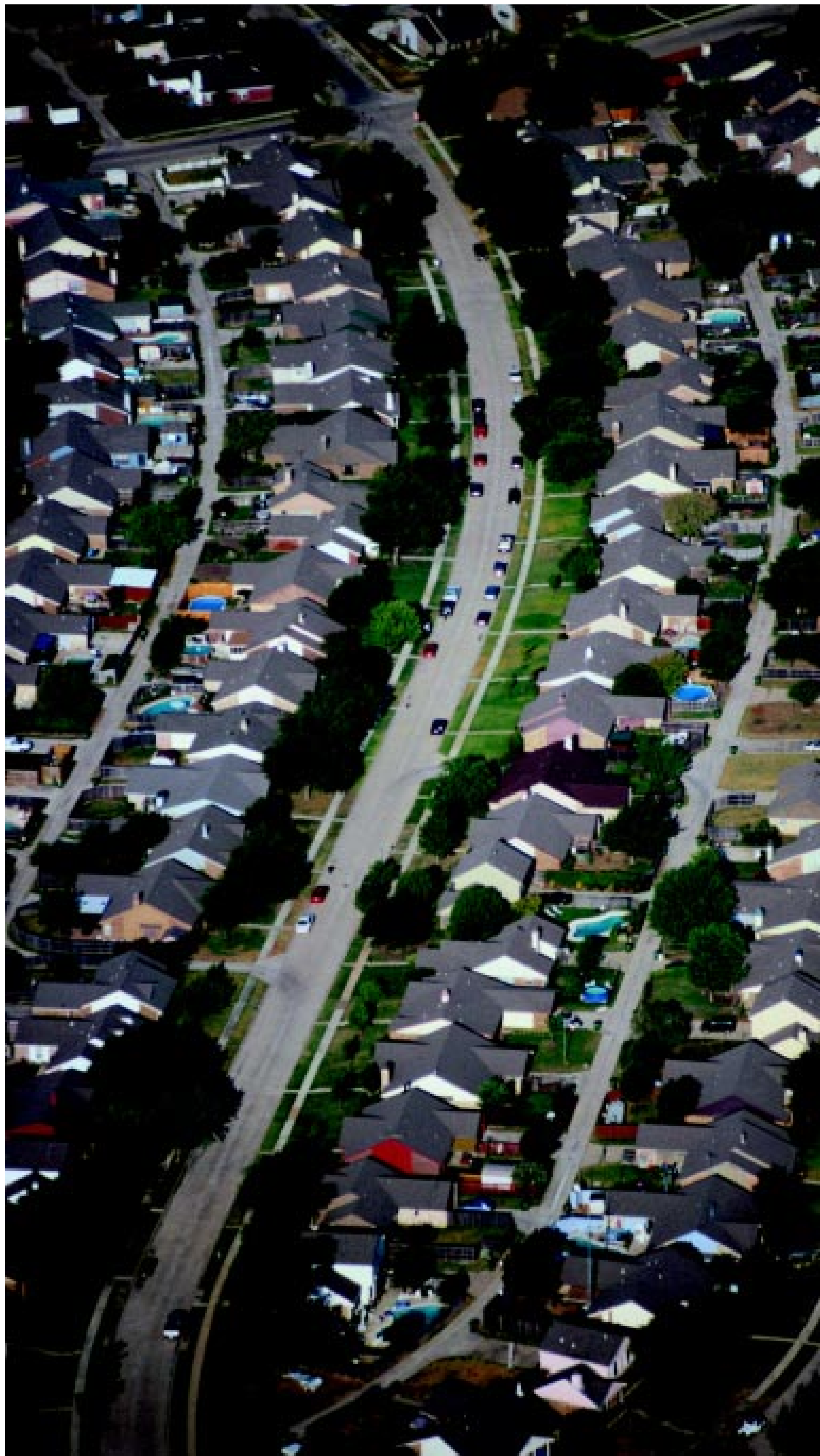
About the first question we have very little to go on. All of the research discussed in this article is concerned with establishing the existence of the social benefits of owner-occupied housing, rather than the harder question of how much external value there is to homeownership. The kinds of benefits brought about by ownership would seem to be very hard to quantify. What is the value of a well-raised child or a neighbor who votes more often? It's hard to know. However, the cost of the tax subsidies to the government and society is quite large, so if the external benefits are not large, the subsidies are clearly not justified. More research in this area is clearly needed to assess the monetary value of these benefits.

Should the tax system be changed? The mortgage interest deduction has come under increased scrutiny over the past decade or so, but as pointed out by Satyajit Chatterjee, this tax preference and the nontaxation of owners' rental income go hand in hand. J. Follain and L. Melamed make this point forcefully. If only the mortgage interest deduction were eliminated, households with sufficient wealth to purchase a home outright would still

enjoy a tax advantage from ownership through the rental exclusion. Middle-income households would no longer have that advantage, since it would no longer accrue to those who finance the purchase of a house.[13] Since the taxation of implicit rent appears to be infeasible, one might argue that the mortgage interest deduction should stay as well.

The policy dilemma is clear. Homeownership has definite social benefits, and on that account, there is a clear case for subsidies that encourage homeownership. Indeed, homeownership *is* subsidized. Furthermore, the tax subsidies are very large, and they're larger for high-income households than for low-income ones. Moreover, eliminating the subsidies from the tax code would be difficult at best.

But the dilemma is compounded because some of the research discussed in this article indicates that the social benefits are higher for low-income households; therefore, the benefits may be scaled the wrong way. Green and White and other authors have suggested the use of tax credits (as opposed to tax deductions) for first-time or low-income home buyers. In this way we can better match the subsidies to and benefits from homeownership and provide a more coherent set of policies to support an important social goal.



[13] People who do not itemize their deductions gain nothing and lose nothing from this change; these may be the lowest income households.

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