Building the American Dream: Asset-Building as a Foundation

The Problem

Homeownership and savings are key to middle class security. Families that sacrifice to build wealth for the future are more likely to prosper over the long term. And, amid the difficult economic times of recent years, many American households have been reminded that the ability to tap savings or home equity is crucial to weathering the loss of a job or other financial misfortune.

Unfortunately, millions of Americans have neither savings nor significant home equity. Homeownership rates are at a historic high — nearly 70 percent — but many younger adults and working families find themselves priced out of the market by exorbitant housing costs. In addition, the ownership rates for minorities lag far behind those of whites — 46 percent for Hispanics and 48 percent for African-Americans. For asset-poor households, one financial setback can lead to a downward spiral of credit card debt and other high-cost forms of credit. Many households that do own homes spend so much on large mortgages, with the interest frontloaded, that they are unable to save for other purposes and remain very vulnerable to an economic setback.

A family's net worth has major implications for future generations. In fact, research shows that household wealth — much more than income — is among the greatest predictors of how well children will do in life, and especially whether they go to college. Yet today, forty percent of all white children, and nearly three-quarters of all African-American children, grow up in households with zero or negative net financial assets.

Solutions

The federal government helps Americans build personal wealth in a variety of ways, most notably with tax breaks related to homeownership and retirement savings. However, most of this assistance goes to people who are already doing well. In 2003, the federal government spent $110.5 billion in homeownership incentives, the bulk of which accrue to better-off families. For example, nearly 90 percent of the mortgage interest deduction benefit accrues to tax filers with adjusted gross incomes over $50,000. Homeowners are even able to deduct mortgage interest on second residences. Meanwhile, tens of billions of dollars in tax breaks to encourage retirement savings go to Americans whose significant net worth already guarantees a secure retirement.

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New steps are urgently needed to extend asset-building efforts down the economic ladder and enact policies that benefit all Americans. Expanding homeownership should be a major priority. The most significant impediment toward purchasing a first home is the ability to save enough money for a down payment, particularly as housing prices have rapidly increased. Combine these challenges with existing low levels of asset accumulation and it becomes clear that several types of new policies are needed to help all Americans become stakeholders in our society.

1. Make the mortgage interest deduction refundable, and cap the benefit level of the deduction to $10,000. Index the level to inflation.

With minor revisions to the mortgage interest deduction, billions of dollars can be used to subsidize homeownership for those most in need -- instead of homeownership subsidies for higher income tax filers who need little or no incentive to purchase a home. The mortgage interest deduction should be capped at $10,000 for all new home purchases and the deduction should be made refundable for working families. This would mean cash back at the end of the year for families who owe less in taxes but who have mortgages. These refunds, in turn, could be used to help build greater equity.

2. Create a matching savings program to help low-income families save toward a down payment on a home.

For millions of working families, a single downpayment could transform the monthly cost of housing from a costly expenditure into a rewarding investment. First-time homebuyers earning less than $50,000 should receive a $1 for $1 match for the money they save toward a down payment. (The match would be phased out for those making between $50,000 and $100,000.) The homeownership down payment assistance subsidy would have a maximum benefit of $7,500, allowing first-time homebuyers to accumulate $15,000 toward a first-home purchase.

3. Provide newborn children with an asset account at birth as well as an endowment.

Every child born in America should grow up with the belief that they can and should build personal wealth. Research shows that having even small personal savings can change people's attitudes about the future, encouraging better planning and more personal responsibility. Children should understand the benefits of savings and investing, and enter young adulthood with financial assets that they can use to increase their life opportunities. One way to help achieve this goal is to create Opportunity Accounts: savings accounts established for each child at birth. For families earning less than $50,000, a deposit of $6,000 by the federal government will be made into each account. Families earning between $50,000 and $75,000 would receive a $3,000 deposit. For families earning between $75,000 and $100,000 the endowment would be phased down to $1,500. Additional voluntary contributions can be made which would be tax exempt and not greater than $1,000 per year.