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Itemized Deductions in a High Standard Deduction World

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Abstract. New tax legislation enacted in December 2017 exacerbates the extent to which various itemized deductions, such as the charitable contribution deduction and the home mortgage interest deduction, disproportionately benefit high income individuals. This essay develops this critique and concludes by suggesting paths for reform that should be considered by a future Congress.

Introduction

In December 2017, Congress enacted tax legislation with broad ramifications. Congress acted with unprecedented speed, dispensing with the type of deliberation that has accompanied sweeping tax changes in the past.[1] The new tax legislation alters the landscape for individuals and businesses operating in the United States and abroad. Many aspects of the legislation have been critiqued in editorials, on blogs, in articles, and in other venues, and doubtlessly more concerns and questions will emerge as the changes are fully processed by commentators and as academics and tax practitioners uncover new loopholes in the hastily adopted provisions.

This Essay critiques one aspect of the new legislation. It highlights how the increase in the standard deduction, coupled with the elimination or reduction of various itemized deductions, exacerbates the extent to which remaining itemized deductions disproportionately benefit higher income individuals. This is by no means the only aspect of the new legislation warranting critique, and

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1. *See, e.g.*, Jesse Drucker & Patricia Cohen, *Tax Bill Offers Last-Minute Breaks for Developers, Banks and Oil Industry*, N.Y. TIMES (Dec. 2, 2017), https://perma.cc/XXX3-TSBM ("The overhaul by Republican lawmakers of the nation's tax laws percolated for weeks with virtually no public input, and by the end it turned into a chaotic mad dash with many last-minute changes on Friday night and Saturday morning, some handwritten in the margins of the nearly 500-page bill."); Jim Tankersley & Alan Rappeport, *A Hasty, Hand-Scribbled Tax Bill Sets Off an Outcry*, N.Y. TIMES (Dec. 1, 2017), https://perma.cc/ND56-A5ES.

by no means the only facet of the legislation that further skews the tax system in favor of wealthy individuals.[2] However, it is a significant feature of the legislation that bears note.

As this Essay will argue, in a high standard deduction world, itemized deductions such as the charitable contribution deduction and the home mortgage interest deduction benefit a smaller pool of even higher income individuals than the group of beneficiaries that existed under prior law. The overall contours of the new tax act suggest that the current Congress views bestowing disproportionate benefits on high income individuals as a feature of the legislation rather than a flaw. Therefore, the current Congress is unlikely to take up the call to remedy this bias. However, a future Congress should consider a number of different options for reform. For some itemized deductions (like the charitable contribution deduction) the best path forward likely entails reform that provides a tax incentive for charitable giving but does so in a way that ameliorates the disproportionate benefits bestowed on high income individuals by the tax incentive contained in current law. For other itemized deductions (like the home mortgage interest deduction), elimination of the deduction entirely may be the route to take.

This Essay will proceed as follows. Part I will describe the ability of taxpayers to either claim the standard deduction or itemize deductions, providing an overview of the system in place prior to the effective date of the new legislation and recounting the ways in which recently enacted law modifies the system. Part II will explain the ways in which itemized deductions disproportionally benefited higher income individuals under the previously existing system. Part III will illustrate how legislative changes exacerbate this bias. Part IV will conclude by offering suggestions for reform.

I. Standard Deduction Versus Itemized Deductions

Every year, individual taxpayers choose between claiming the standard deduction or itemizing deductions.[3] If an individual claims the standard deduction then, when calculating his or her taxable income, that individual will subtract the relevant standard deduction amount from the individual's adjusted gross income (AGI).[4] The standard deduction is a specific dollar amount, adjusted annually for inflation.[5] If a taxpayer elects to itemize deductions then, in lieu of claiming the standard deduction, that taxpayer will subtract from AGI

2. See, for instance, the Tax Policy Center's distributional analysis of the legislation discussed below at note 40 and accompanying text.

3. *See* 26 I.R.C. § 63 (2016). Citations to the Internal Revenue Code followed by "(2016)" refer to the Code in place prior to enactment of the new tax law.

4. AGI is calculated by subtracting from a taxpayer's gross income various expenses, including certain trade or business expenses.

5. *See* 26 I.R.C. § 63(c) (2016).

the dollar amount of certain expenses actually incurred by the taxpayer, subject to certain limitations.[6] Thus, a taxpayer will generally opt to claim the standard deduction if it is higher than the taxpayer's total itemized deductions, and the taxpayer will opt to itemize when the opposite is true.

Part I.A will provide a more detailed account of the state of the law prior to the adoption of the new tax act, and Part I.B will describe the changes wrought by the new legislation.

A. Prior Regime

For 2017, the standard deduction was $6,350 for a single taxpayer and $12,700 for married individuals filing joint returns.[7]

Under prior law, allowable itemized deductions included, among others, the deductions for (1) home mortgage interest;[8] (2) state and local taxes;[9] (3) charitable contributions;[10] and (4) unreimbursed medical expenses to the extent they exceeded 10% of a taxpayer's AGI.[11] Under prior law, some itemized deductions were also subject to a phase-out for taxpayers with high AGIs.[12]

In addition to subtracting from AGI either the standard deduction or itemized deductions, a taxpayer would also subtract the relevant personal exemption amount.[13] The personal exemption amount was a flat dollar amount adjusted for inflation ($4,050 in 2017)[14] multiplied by the number of exemptions claimed by the taxpayer. The personal exemption amount was also subject to a phase-out for taxpayers with high AGIs.[15]

The preceding discussion can be illustrated by the following example.

> **Example.** Elizabeth and Matt are married taxpayers with no dependents. In 2017, they donate $1,000 to a charitable organization. They incur $4,000 in state income taxes. They own a home, and they incur $16,000 in property taxes and pay $12,000 of deductible home mortgage interest. They do not incur any other expenses giving rise to itemizable deductions. Their adjusted gross income is $200,000. They file a joint return. For Elizabeth and Matt, the $12,700 standard deduction

6. *See id.* § 63.
7. Rev. Proc. 2016-55 § 3.14, 2016-45 I.R.B. 707, 712.
8. *See* 26 I.R.C. § 163(h)(2)(D) (2016). Section 163 also contains various limitations on the ability to deduct home mortgage interest. *See id.* § 163(h)(3).
9. *Id.* § 164.
10. *Id.* § 170. Section 170 also contains various limitations on the charitable contribution deduction. *See*

id. § 170(b).

11. *Id.* § 213.
12. *See id.* § 68.
13. *See id.* § 151.
14. Rev. Proc. 2016-55 § 3.24, 2016-45 I.R.B. 707, 713.
15. 26 I.R.C. § 151(d)(3) (2016).

is less than their $33,000 of potential itemized deductions ($1,000 charitable contribution plus $4,000 state income taxes plus $16,000 property taxes plus $12,000 home mortgage interest). Therefore, they would claim itemized deductions of $33,000 and the personal exemption amount of $4,050 multiplied by two, resulting in taxable income of $200,000 - $33,000 - $8,100 = $158,900.

B. Changes Adopted

The new tax legislation increases the amount of the standard deduction, at least temporarily.[16] For 2018, the standard deduction is $12,000 for a single taxpayer and $24,000 for a married couple filing a joint return.[17] The new legislation eliminates the ability to claim any personal exemptions.[18] In the case of personal exemptions that could have been claimed for some dependents under prior law, the effect of this change, for some taxpayers, may be partly or entirely offset by an expanded child tax credit.[19]

The new tax legislation modifies or eliminates many previously allowed itemized deductions. These changes include, but are not limited to, the adoption of a new cap on the deduction for state and local taxes, so that taxpayers may now deduct up to a maximum of $10,000 (or $5,000 for a married taxpayer filing a separate return)[20] of the combined total of state and local income taxes (or sales taxes in lieu of income taxes) plus state and local property taxes not incurred in a trade or business.[21] The new tax act slightly expands the deduction for unreimbursed medical expenses to allow an itemized deduction for unreimbursed medical expenses to the extent that they exceed 7.5% of AGI (replacing the 10% of AGI floor with a 7.5% of AGI floor).[22] The new tax act makes some modifications to the home mortgage interest deduction. Among other changes, in the case of debt incurred on or after December 15, 2017, the new tax act limits the home mortgage interest deduction to interest incurred on "acquisition indebtedness" of up to $750,000.[23] Acquisition indebtedness is

16. Except where otherwise noted, all changes are effective for the years 2018 through 2025.

17. *See* H.R. REP. NO. 115-466, at 20 (2017) (Conf. Rep.), https://perma.cc/5KQN-Y32V; *see also id.* at 201-02.

18. *See id.* at 30.

19. *See id.* at 21-22; *see also id.* at 225-27. The new tax act also adds a $500 credit for certain dependents that are not qualifying children. *Id.*

20. I*d.* at 34, 260-61. The fact that the limitation is $5,000 for a married taxpayer filing a separate return suggests that for married individuals filing a joint return, the $10,000 limitation applies to the total amount of state and local taxes claimed as an itemized deduction on that return. In other words, although not entirely free from doubt, it appears that the same $10,000 limitation that applies to a tax return filed by single taxpayer also applies to a tax return filed jointly by a married couple.

21. *See id.*

22. *Id.* at 25; *see also id.* at 276-77. These new rules are effective for 2017 through 2018. *Id.*

23. *See id.* at 34-35; *see also id.* at 258.

debt incurred to acquire, construct, or substantially improve a qualified residence (meaning the taxpayer's principal residence and one other residence) that is secured by the residence. Under prior law, the cap on acquisition indebtedness was $1,000,000, and taxpayers could also deduct interest on up to $100,000 of home equity indebtedness in some cases.[24] In addition to various other changes made to specific itemized deductions,[25] the new legislation eliminates the phase-out of itemized deductions for taxpayers with high AGIs.[26]

In order to demonstrate the changes' effect, we can return to the example of Elizabeth and Matt above, imagine that all facts remain the same, but now imagine that all events occur in 2018. The following describes the determination of taxable income for the couple under the new tax legislation.

> **Example in 2018.** For Elizabeth and Matt, the $24,000 standard deduction is more than their $23,000 of potential itemized deductions ((1) their total state and local income taxes and property taxes of $20,000 will be subject to the new $10,000 limitation, resulting in a deductible amount of only $10,000[27] plus (2) $12,000 home mortgage interest plus (3) $1,000 charitable contribution deduction). Therefore, they will claim the standard deduction of $24,000. They are no longer entitled to a personal exemption. Their resulting taxable income is $200,000 - $24,000 = $176,000. This is higher than their 2017 taxable income of $158,900. The standard deduction of $24,000 is lower than the $33,000 of itemized expenses that they were able to claim before the new limitation on state and local taxes, which, coupled with the loss of their $8,100 personal exemption amount, results in the $17,100 increase in their taxable income.

A change in taxable income does not definitively show whether the given taxpayers will benefit from or be burdened by the legislative changes because alterations to tax rates and tax credits (including the child tax credit) will also affect taxpayers' ultimate tax liability. For some taxpayers, tax liability will decrease even though taxable income increases. In the case of Elizabeth and Matt, for instance, assuming that they are not entitled to any tax credits or to any deductions other than those mentioned in the facts of the example, in 2017,

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24. 26 I.R.C. §§ 163(h)(2)(D)-(h)(3) (2016).

25. These changes include, among others, an increased limitation for certain charitable contribution deductions and the repeal of various miscellaneous itemized deductions. *See* H.R. REP. NO. 115-466, at 22-23; *id.* at 36; *see also id.* at 272-73, 276.

26. *See id.* at 36, 255-56.

27. This assumes that the taxpayers are not able to, instead, make deductible charitable contributions that entitle them to a credit against state income tax. For discussion of this possibility, see, for example, Joseph Bankman et al., Federal Income Tax Treatment of Charitable Contributions Entitling Donor to a State Tax Credit 1-2 (Jan. 8, 2018) (unpublished manuscript), https://perma.cc/47CX-Z87S. If the taxpayers reside in a state that allows state tax credits for charitable contributions and if the IRS does not successfully challenge the deductibility of the contributions for federal income tax purposes, then the results would differ.

their $158,900 taxable income is subject to total tax liability of $31,377,[28] while, in 2018, their $176,000 taxable income is subject to total tax liability of $30,819;[29] thus, their tax liability declines by $558 even though their taxable income increases.

However, for purposes of this Essay, the relevant observation is not what happens to tax liability or even what happens to taxable income. Rather, the key observation is what happens to the likelihood that a taxpayer will claim various itemized deductions such as the charitable contribution deduction or the home mortgage interest deduction. This likelihood declines. Many taxpayers who claimed these deductions under prior law no longer will. This is true of the hypothetical taxpayers in the example above. To gauge the magnitude of this change more generally, the Tax Policy Center estimates that the new legislation will decrease the number of taxpayers who itemize deductions from 46.5 million (under prior law) to slightly over 19 million (under new legislation).[30]

To provide a more general example that demonstrates how the pool of taxpayers who benefit from an itemized deduction like the home mortgage interest deduction will shrink, imagine a married couple's only itemizable expenses are state income taxes, local property taxes, and the home mortgage interest deduction. Imagine they incur property taxes plus state income taxes that total at least $10,000. In order to make use of itemized deductions under the new law, their home mortgage interest expenses would have to exceed $14,000 (or the $24,000 standard deduction amount minus the $10,000 of state and local taxes that would be deductible after factoring in the new $10,000 limitation on state and local taxes). Based on a 4.25% fixed thirty-year mortgage rate, $14,000 of interest expense translates into approximately $330,000 of debt.[31] Assuming at least 20% equity in their home, this amount of debt would be outstanding on a home with a price of at least $412,500.[32]

28. This amount is determined as follows: (1) 10% times $18,650 + (2) 15% times ($75,900 - $18,650) + (3) 25% times ($153,100 - $75,900) + (4) 28% times ($158,900 - $153,100).

29. This amount is determined as follows: (1) 10% times $19,050 + (2) 12% times ($77,400 - $19,050) + (3) 22% times ($165,000 - $77,400) + (4) 24% times ($176,000 - $165,000).

30. *T18-0002 – Impact on the Number of Itemizers of H.R. 1*, TAX POL'Y CTR. (Jan. 11, 2018), https://perma.cc/MS3X-YD5L.

31. This is an approximate figure because the amount of principal outstanding on the loan would change over the course of the year.

32. This again assumes that the taxpayers are not able to, instead, make deductible charitable contributions that entitle them to a credit against state income tax. For discussion of this possibility, see, for example, Joseph Bankman et al., *supra* note 27, at 1-2. If the taxpayers reside in a state that allows state tax credits for charitable contributions and if the IRS does not successfully challenge the deductibility of the contributions for federal income tax purposes, then the results would differ, and the change from present law would be less drastic. Nevertheless, the increase in the standard deduction amount, on its own, would increase the upside-down subsidy effect to some extent.

Under prior law, when the standard deduction was $12,700 for a married couple filing a joint return, the couple's itemized deductions would exceed the standard deduction as long as their home mortgage interest was at least $2,700, assuming state and local taxes of $10,000 (or, if state and local taxes were greater than $10,000, an even smaller amount of home mortgage interest would suffice to turn the couple into itemizers). Based on a 4.25% fixed thirty-year mortgage rate, $2,700 of interest expense translates into approximately $63,500 of debt. Assuming at least 20% equity in their home, this amount of debt would be outstanding on a home with a price of at least $79,375. Thus, the effect of the change for a couple similar to this hypothetical couple is to increase the home price at which the home mortgage interest deduction provides a tax benefit from $80,000 to $412,000.[33]

II. Upside Down Subsidy Critique

One critique that is often leveled at the use of itemized deductions to subsidize a given activity is that itemized deductions provide an "upside-down subsidy," meaning they provide greater benefits to individuals with higher incomes.[34]

Take the charitable contribution deduction, for instance. For several reasons, this deduction disproportionately benefits higher income individuals.[35] First, individuals with more disposable income are more able to make charitable contributions in the first place. Second, higher income individuals are more likely than lower income individuals to itemize deductions because their total itemizable expenses are more likely to exceed the standard deduction.[36] Higher income individuals are more likely to itemize because, just as charitable contributions tend to increase with income, so too do other itemizable expenses such as state and local taxes and home mortgage interest. The charitable contribution deduction and other itemized deductions provide no benefit to individuals who do not itemize, and, given that higher income individuals are more likely to itemize, itemized deductions are more likely to benefit higher income individuals. Third, if an individual's taxable income is

33. For single taxpayers, the change would be less drastic—given the lower standard deduction amount that applies to single taxpayers and given that the new state and local property tax limitation appears to be the same ($10,000) for single taxpayers as it is for married taxpayers filing a joint return. Nevertheless, the amount of home mortgage interest that justifies itemizing deductions for single taxpayers would also increase as a result of the changes.

34. *See* STANLEY S. SURREY & PAUL R. MCDANIEL, TAX EXPENDITURES 71-82 (1985).

35. *See, e.g.*, David M. Schizer, *Limiting Tax Expenditures*, 68 TAX L. REV. 275, 315-16 (2015).

36. *See, e.g.*, Alicia Parlapiano, *Six Charts That Help Explain the Republican Tax Plan*, N.Y. TIMES (Nov. 2, 2017), https://perma.cc/52JT-L3A9 (containing a chart showing the percentage of taxpayers who itemize versus claim the standard deduction in various adjusted gross income brackets based on 2014 data).

less than the amount of a deduction, the individual does not receive the full benefit of the deduction. Finally, a given deduction leads to greater tax savings the higher an individual's marginal tax rate is, and marginal tax rates increase as income rises. A $1,000 deduction saves $350 in tax for an individual whose last $1,000 would be taxed at 35% but saves only $100 in tax for an individual whose last $1,000 would be taxed at 10%.

Similar observations could be made about the home mortgage interest deduction. Higher income individuals are more likely to own homes and incur home mortgage interest in the first place.[37] They are more likely to own more expensive homes, leading to more interest expense.[38] They are more likely to itemize, they are more likely to earn taxable income that exceeds the amount of the deduction, and they reap a larger benefit from a given deduction in light of their higher tax rates.[39]

The phase-out of certain itemized deductions for high income taxpayers partially counters their "upside down subsidy" effect. However, the new tax act eliminated the phase-out of itemized deductions for taxpayers with high AGIs. In the case of the home mortgage interest deduction, the new legislation does reduce the cap on acquisition indebtedness from $1,000,000 to $750,000, which ameliorates the "upside down subsidy" effect to some extent. Nevertheless, a taxpayer who incurs more than $750,000 of acquisition indebtedness can still benefit from the deduction for interest attributable to $750,000 of the borrowing. Moreover, for debt that was incurred before December 15, 2017, the cap remains $1,000,000.

III. Upside-Down Subsidies Are Now Even More Top-Heavy

For all of the reasons described in the preceding Part, itemized deductions tend to provide a greater benefit to higher income individuals. The new tax act, by increasing the standard deduction and limiting various itemized deductions such as the state and local tax deduction, exacerbates the extent to which the remaining itemized deductions disproportionately benefit higher income individuals. This is true because the changes have the effect of further narrowing the pool of individuals who itemize deductions and leaving higher income individuals in the pool that remains. Consider, for instance, the example above in which, under prior law, a married couple could receive some benefit from the home mortgage interest deduction as long as their home was worth at least $80,000, but, under the new regime, the benefit evaporates unless the home is worth at least $412,000.

37. *See, e.g.*, Rebecca N. Morrow, *Billions of Tax Dollars Spent Inflating the Housing Bubble: How and Why the Mortgage Interest Deduction Failed*, 17 FORDHAM J. CORP. & FIN. L. 751, 795 (2012) (reporting that higher income homeowners are also more likely to have mortgages on their homes than lower income homeowners).

38. *See id.*

39. *Id.* at 795-96.

One might respond that lower income individuals are still made better off by the new tax act if it lowers their ultimate tax liability. It is true that the new tax act lowers the current tax liability for many taxpayers and increases the tax liability for other taxpayers in various income ranges. The Tax Policy Center's distributional analysis of the legislation drew the following conclusions:

> In general, higher income households receive larger average tax cuts as a percentage of after-tax income, with the largest cuts as a share of income going to taxpayers in the 95th to 99th percentiles of the income distribution. On average, in 2027 taxes would change little for lower- and middle-income groups and decrease for higher-income groups. Compared to current law, 5 percent of taxpayers would pay more tax in 2018, 9 percent in 2025, and 53 percent in 2027.[40]

For taxpayers whose current tax liability declines, the tax act does provide a current benefit.[41]

Relatedly, one might argue that a taxpayer does not lose the benefit of an itemized deduction merely because the standard deduction is more than the itemized deduction. Rather, that taxpayer is benefited by the standard deduction being so high because it lowers their taxable income compared with an alternative regime under which the standard deduction were lower.[42]

However, for purposes of this Essay, the key observation is not whether any given individual's tax liability rises or falls as a result of the new legislation. Rather, the question is who benefits from the itemized deductions that remain.[43] The answer is that the home mortgage interest deduction and charitable contribution deduction will tend to assist a shrinking pool of even higher-income beneficiaries than the recipients who benefited under prior law. Likewise, the argument that a person whose itemizable expenses are less than

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40. TAX POLICY CTR., URBAN INST. & BROOKINGS INST., DISTRIBUTIONAL ANALYSIS OF THE CONFERENCE AGREEMENT FOR THE TAX CUTS AND JOBS ACT 1 (2017), https://perma.cc/JYP5-JLKM.

41. In some cases, current benefits may be offset by future tax increases or future reductions in benefits.

42. As Brooks observes, this conclusion would follow from viewing the standard deduction as a simplification measure intended to substitute for itemized deductions. *See* John R. Brooks II, *Doing Too Much: The Standard Deduction and the Conflict Between Progressivity and Simplification*, 2 COLUM. J. TAX L. 203, 228 (2011) ("If the standard deduction is intended to be a proxy for personal deductions like the charitable deduction, then non-itemizers are already getting the full benefit of their charitable deductions—and then some.").

43. A shrinking pool of taxpayers who itemize also weakens the ability of itemized deductions to incentivize behavior. For discussion of this issue in the context of the charitable contribution deduction, see, for example, Joseph Rosenberg & Philip Stallworth, *The House Bill Is Not Very Charitable to Nonprofits*, TAX POL'Y CTR.: TAXVOX (Nov. 15, 2017), https://perma.cc/45SZ-KJAZ. For discussion of potential work-arounds (such as bunching charitable contributions into one year that would otherwise be spread out across multiple years) that may, in some cases, help to maintain a tax incentive for charitable giving, see, for example, Ann Carrns, *How to Write Off Donations Under the New Tax Plan: Consider 'Bunching,'* N.Y. TIMES (Dec. 20, 2017), https://perma.cc/G64S-LG69.

the standard deduction bears no burden because they are better off than they would be in a world with a lower standard deduction does not address this Essay's critique. That observation might be relevant if the question posed was whether or not to lower the standard deduction. The question posed by this Essay is, instead, whether the continued existence of certain itemized deductions can be justified in a high standard deduction world. This Essay argues that their continued existence, at least in their current form, is not justified given that they benefit an increasingly smaller pool of high income individuals.

IV. Conclusion

Even before the adoption of the new tax act, many itemized deductions disproportionately benefited high income individuals. In a high standard deduction world, this phenomenon becomes even more pronounced. There are potential cures. The overall contours of the new tax act suggest that the current Congress views bestowing disproportionate benefits on high income individuals as a feature of the legislation rather than a flaw. Therefore, the current Congress is unlikely to take up the call to remedy this bias.

For a future Congress, one possible path forward involves elimination of the standard deduction, reinstatement of the ability to claim personal exemptions set at a higher dollar amount than the $4,050 allowed under prior law,[44] and adoption of various floors under each of the itemized deductions some of which could be related to AGI.[45] For instance, donations to charity could be deducted only to the extent they exceeded *X*% of AGI. Brooks proposed such a system as a reform of prior law for a number of reasons.[46] One virtue of separate AGI-related floors for certain itemized deductions is that AGI-related floors ameliorate one of the factors that causes itemized deductions to provide

44. If the standard deduction were eliminated, increasing the personal exemption amount could fill one purpose of the standard deduction which is to provide for a range of income that is implicitly taxed at zero percent. For discussion of this role, see, for example, Brooks, *supra* note 42, at 205-09.

45. Adopting floors under the various deductions serves a number of roles. It protects revenue—if the itemized deductions were allowed with no floors in addition to an increased personal exemption, tax revenue would decline. Floors also provide certain simplification benefits and can be used to tinker with the incentive effects of tax provisions. *See, e.g.*, *id.* at 242-46; Schizer, *supra* note 35, at 295-96, 311-12, 321-27.

46. *See, e.g.*, Brooks, *supra* note 42, at 208 ("This would separate the determination of the proper deduction amount for a given itemizable expense from the amounts of any other itemizable expenses. . . . This article further argues that deduction floors have particular, and underused, tax policy benefits, since they can allow policymakers to more effectively manage deductions by adjusting floors to optimize trade-offs between simplicity, revenue, incentives, and equity for each given deduction.").

an "upside-down subsidy."[47] In particular, AGI-related floors act to counter the fact that lower income individuals' itemizable expenses are more likely to be lower than a standard deduction of a flat dollar amount. If the floor on a deduction is AGI-related rather than set at a flat dollar amount, then the floor is lower for lower income individuals, so they have a more equal chance of incurring expenses that exceed the floor. Furthermore, lower-AGI taxpayers are able to deduct a larger portion of their expenses.[48]

For instance, imagine that charitable contributions were deductible only to the extent they exceeded 2% of AGI. For a taxpayer with an AGI of $50,000, the floor would be 2% of $50,000 or $1,000. Thus, if this taxpayer donated more than $1,000 to charity, he or she could deduct the excess of the donation over $1,000 (for instance, if he or she donated $1,500, he or she could deduct $500). For a taxpayer with an AGI of $500,000, the floor would be 2% of $500,000 or $10,000. Thus, if this taxpayer donated more than $10,000 to charity, he or she could deduct the excess of the donation over $10,000 (for instance, if he or she donated $10,500, he or she could deduct $500). Contrast these results with a floor of a flat dollar amount of $5,500. Under the flat dollar amount floor, the taxpayer with the lower AGI deducts nothing, and the taxpayer with the higher AGI deducts $5,000. Other reforms could include converting deductions into refundable tax credits.[49]

In lieu of reforming existing deductions, another path forward entails elimination of, in particular, the home mortgage interest deduction. Even before the most recent changes shrunk the pool of taxpayers who benefit from it, this deduction was vulnerable to policy-based objections.[50] Its longevity is largely attributable to the political difficulty of repeal.[51] The ramifications of the new tax act for the future feasibility of repeal are unclear. An optimist might predict that the new tax act paves the way for future repeal by limiting the pool of taxpayers who would be harmed by elimination of the deduction. A pessimist

47. Another virtue of this approach is that, particularly compared to current law, it may do a better job of maintaining a tax incentive for charitable giving. For discussion of the effects of the new law on this incentive, see Rosenberg & Stallworth, *supra* note 43.

48. In other words, an AGI-related floor also counters the upside-down subsidy effect by making a larger portion of the expense nondeductible for higher income taxpayers. For further discussion, see, for example, Brooks, *supra* note 42, at 245.

49. In addition to removing the upside-down subsidy effect, such a change could have other benefits. *See, e.g.*, Lily L. Batchelder et al., *Efficiency and Tax Incentives: The Case for Refundable Tax Credits*, 59 STAN. L. REV. 23, 24-30 (2006).

50. *See, e.g.*, Roberta F. Mann, *The (Not So) Little House on the Prairie: The Hidden Costs of the Home Mortgage Interest Deduction*, 32 ARIZ. ST. L.J. 1347, 1348-51 (2000); Morrow, *supra* note 37, at 755-99.

51. *See, e.g.*, Mann, *supra* note 50, at 1348; Morrow, *supra* note 37, at 760-61. Indeed, while the bill initially passed by the House capped the amount of acquisition indebtedness at $500,000, the bill initially passed by the Senate retained the $1,000,000 cap. *See* H.R. REP. NO. 115-466, at 256-58 (2017) (Conf. Rep.). The version eventually passed by Congress adopted a cap of $750,000. *See id.* at 257-58.

might wager that, by concentrating the benefits of the provision in the hands of an even smaller group of wealthy individuals, Congress has strengthened its staying power.[52] The pessimist could also cite to the fact that, even under prior law, the provision enjoyed support from individuals who did not benefit from it.[53]

52. For additional discussion of how the fact that itemized deductions are not uniformly used can complicate their reform, see, for example, Allan J. Samansky, *Nonstandard Thoughts About the Standard Deduction*, 1991 UTAH L. REV. 531, 547-48.

53. *See, e.g.*, Morrow, *supra* note 37, at 760-61, 815-16.