Homeownership and Public Policy: What Helps, and What Hinders, the American Dream
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What more sacred, what more strongly guarded by every holy feeling, than a man's own home? —Cicero

America’s founding fathers inherited from English common law the doctrine that “a man's house is his castle.”¹ Property ownership and political autonomy are two sides of the same coin. John Locke regarded the right to private property as a quintessential natural right, a right that gave citizens ground for demanding representative government.² Thomas Jefferson understood private property to be foundational for “the pursuit of happiness” broadly considered, and guided by that understanding, the Second Continental Congress issued the Declaration of Independence, which stated, “to secure these rights, governments are instituted among men, deriving their just powers from the consent of the governed.” In the aftermath of the Revolution, the states in 1791 ratified the Fourth Amendment to the U.S. Constitution, an amendment that protects

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American homes against “unreasonable searches and seizures.”

To secure their homes, American families long have expected government protection. Starting with the New Deal reforms of the 1930s, growing numbers of people also have sought government provision for housing. Like any government policy, federal housing programs have resulted from compromises occasioned by conflicting political passions and forged by opportunistic policymakers. As the United States today struggles to recover from the worst housing crisis of a generation, prudence calls for an examination of the longer history of federal housing policy in order to determine what sustains, and what suffocates, the American dream of homeownership and, perhaps more importantly, home entrepreneurship.

Why Ownership Matters, and Why It Doesn’t

Two objectives have competed for preeminence in federal housing policy since the 1920s, when Secretary of Commerce Herbert Hoover launched Better Homes for America, an initiative providing affordable housing for all Americans and stimulating growth for the broader economy. Neither of these objectives necessarily calls for homeownership as a desirable end, and neither requires homeownership as a means. Affordable rental housing could, at least in principle, satisfy the first objective; policies aimed at stimulating other sectors of the economy could, in principle, satisfy the second objective. But the ideal of homeownership carries symbolic weight in policy evaluations, and symbolism matters a great deal for both policymakers and their constituents. The symbolic value of homeownership derives from the tradition of civic republicanism that America’s founders drew from the writings of Locke and Jefferson: landholders are relatively self-sufficient, and therefore are not beholden to others, and therefore can uniquely exercise personal liberty while also making virtuous decisions on behalf of the nation that protects their property. But in the twentieth and twentieth-first centuries, are homeowners any more


credible than renters as heirs of the civic republicanism of eighteenth-century agrarian property holders? Or is the mystique of homeownership merely an empty hope for national prosperity?

Homeownership indeed correlates positively with numerous measures of social capital and civic engagement, which, arguably, are essential for establishing and maintaining a civilized social order. “Each June during National Homeownership Month,” proclaims the website of the National Association of Home Builders, “Americans have the opportunity to reflect on how homeownership has enhanced our lives and contributed to the thriving communities we call home.” Homeowners stay in the neighborhood four times longer than renters and are more likely to join community organizations and contribute to political campaigns. Their children fare better, too, as indicated by lower rates of unwed teen pregnancy and higher rates of college enrollment. Owners also have greater accumulated wealth than renters by middle age, primarily in the form of home equity. Although empirically confirmed advantages to homeownership tend to be modest, every president since Herbert Hoover has boldly extolled the value of homeownership. In recent memory, George W. Bush called for an “ownership society,” one-upping Bill Clinton’s encouragement for Fannie Mae and Freddie Mac to expand mortgage lending for minority and moderate-income households. In response to the foreclosure crisis, President Barack Obama launched his “Making Homeownership Affordable” plan. Homeownership and national prosperity appear to be kissing cousins, indeed.

But correlations—as is widely known but often forgotten—do not prove causation. Scholars debate whether homeownership leads to the positive externalities described above, or whether other characteristics


that make persons eligible for homeownership lead to both the purchasing of a home and to subsequent engagement in civil life and investment in social capital for the rising generation. If transforming a person into a homeowner also makes that person a more responsible citizen whose children will thereby acquire greater social capital, then public policies that stimulate homeownership would appear to serve the state's interest in fostering a stable and prosperous society. If, on the other hand, people remain ill-equipped to own a home until they demonstrate certain personal traits, then policies aimed too directly at homeownership will not help—and might even hinder—community development. The sobering fact is that the record-setting rate of homeownership achieved nationwide in the 1990s correlates with a decline in overall civic engagement and a sharper stratification in the distribution of social capital. As sociologist Robert Putnam quantified, more Americans are “bowling alone,” despite the fact that more of them nominally own their own home than ever before.9

One reason that the higher rates of homeownership have meant worse rather than better community well-being is that many Americans have acquired their homes only through reckless borrowing. However, Putnam himself pointed in other directions, seeing in the sprawling suburban neighborhoods new homeowners addicted to television and to other isolation-inducing distractions. Then again, Putnam completed his book when the national median price-to-income ratio for single-family homes was still hovering at its historic average of about 3.4 percent. But from 2000 to 2005, it rose to nearly 4.75 percent, indicating that homeownership was slipping out of the financial reach of an increasing number of Americans.10 Nevertheless, homeownership rates continued rising, leveling at a record high of 69 percent from 2004 to 2006.11 That last


year, 43 percent of first-time buyers and 19 percent of repeat buyers—by weighted average, 30 percent of all buyers nationwide—paid zero money down. Another 10 percent of buyers put down 3 percent or less.\textsuperscript{12}

How was this possible? For one thing, U.S. Bank’s “Home Possible 100” underwriting guidelines—for mortgages with a 100-percent loan-to-value ratio—were requiring of the borrower a merely nominal contribution of $500, notably less than the insurance deposits for some rental units.\textsuperscript{13} Of course, a renter low on funds might acquire the deposit money from a generous friend or relative, and thanks to Freddie Mac, a prospective homebuyer in 2008 could have done the same thing (“no borrower contribution required”), even with a total loan-to-value ratio of 105 percent—yes, that meant borrowing 5 percent more than the appraised value of the home.\textsuperscript{14}

One might suppose that would-be homeowners would balk at taking on such staggering levels of debt, but a persistent perception of homes as assets apparently mitigated that fear. Buying your own home, so goes conventional wisdom, is the safest investment you can ever make. Yet, financial guru Robert Kiyosaki, of Rich Dad, Poor Dad fame, warns that many supposed assets are really “doodads.”\textsuperscript{15} An asset is something that generates income for its owner; a liability entails expenses for its owner. A property rented out to tenants is an asset, but an owner-occupied house is a doodad—but probably a liability, at best a pseudo-asset that gives the middle class a false sense of wealth. True, mortgage payments for one’s home may be less than the cost of renting a comparable residence, but transaction expenses and ongoing maintenance responsibilities often reduce that benefit beyond the break-even point. Ownership also ties

up cash that could accumulate in liquid savings for a renter.\textsuperscript{16} Owners furthermore incur opportunity costs for time spent maintaining a home rather than running a home-based business. Owners also are at a disadvantage in times of unemployment, since renters have greater mobility to relocate into more promising job markets.\textsuperscript{17} And although property appreciation may mean that selling a home gives a homeowner a nominal return on his investment, that homeowner is then likely to discover how small that return is worth when he tries to buy a replacement home. After all, the same monetary tide that raised the price of his first home has also raised the price of all homes that he might consider as a replacement. Moreover, a decline in property values—when the proverbial tide falls—can leave owners at a loss when they sell or refinance.

The wealth-building potential of homeownership comes, then, not from living in one’s own home but from putting that ownership to work: owning a house that is rented out to others, telecommuting from home, or leveraging home equity to finance a business. Economic historian Hernando de Soto has traced the bulk of wealth production in the modern world to the economic dynamics of societies in which clear claims to title enable real estate to serve as collateral for loans that start or expand entrepreneurial pursuits. In America, the home-equity loan has provided a stepping-stone from the lower-middle class into the upper-middle and upper classes for twentieth-century Americans.\textsuperscript{18} This strategy may prove less viable in the early twenty-first century, as claims to title become less secure due to confusion resulting from sloppy securitization and erroneous electronic filing. Putative loan holders have been surprised by court rulings denying their claims to securitized property amid the murky performance of the Mortgage Electronic Registration Systems (MERS), which has processed more than 60 million mortgages since its inception in 1995, including about two-thirds of the nation’s home mortgages.

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\textsuperscript{17} Green, “Homeowning, Social Outcomes, Tenure Choice, and U.S. Housing Policy,” p. 23.
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during the peak years of the “housing bubble.”

For the near term, low-capital entrepreneurial efforts may be the best bet. Rather than saving for a down payment, the self-employed—writers, consultants, and a diverse bunch of e-commerce entrepreneurs—can be content to rent while investing modestly in home-office expenses in order to build a cottage industry that shields them from the risks of underemployment. Unfortunately, the past century of housing policy has done little to encourage industriousness within the cottage, and in fact has done much to discourage productivity at the home.

**From Cottage Industries to Suburban Dormitories**

The social value of real estate, no less than its economic value, depends largely upon three factors: location, location, and location. Homeowners—both in small rural towns and in large central cities—tend to invest themselves in the community by building social capital through parent-teacher associations, churches, and other civic organizations. The same held true, during the 1950s and 1960s, in suburbs, but in the latter decades of the twentieth century, the nation’s fast-growth communities—built further and further away from central cities—suffered from the social disintegration known as “suburban sprawl.” Commuters are now habituated to sitting solo in traffic jams, only to return home to gated communities that forbid Girl Scouts from selling cookies door-to-door. Suburbanites lack the opportunity, and perhaps even the desire, to form tight-knit communities or volunteer for local nonprofit organizations. Putnam calculated that “each additional ten minutes in daily commuting time cuts involvement in community affairs by 10 percent.”

The consequences of suburbanization—social segregation into homogeneous communities, and dissociation between one’s neighbors and one’s business relations—impose a “sprawl

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civic penalty’ of roughly 20 percent on most measures of community involvement.”

The fact that nearly three out of four suburbanites own rather than rent does nothing to bring them closer to neighbors who are gone all day at the office anyway.

The sharp separation of productive labor from the family home is, historically speaking, a departure from the previously universal human practice of working simultaneously for and near one’s family. As men left family farms and cottage industries in the nineteenth century for city jobs, a social code of “separate spheres” became characteristic of Victorian morality: commerce occasions vice, and so the home must be kept free of market activities in order to remain a safe haven for children. As women left the home for outside employment in the twentieth century, feminists sought to purge the separate-spheres doctrine of its gendered language—a “woman’s place” no longer would be “in the home”—but the separation between work and family remained; indeed, the separation intensified, as women exchanged homespun clothing for occupations in textile industries and gave up renting out a room to boarders to pursue employment distant from the family dwelling.

The adoption of uniform zoning laws in the 1920s reinforced “the idea that ‘home’ and ‘work’ are incompatible, that the ‘home’ should be carefully segregated into exclusively residential, commerce-free zones.”

Although state and municipal legislatures are ostensibly the government bodies responsible for enacting zoning regulations, it has actually been the federal government which has promoted these regulations through the promulgation of “A Standard State Enabling Act Under Which Municipalities May Adopt Zoning Regulations,” prepared by the U.S. Department of Commerce under Secretary Herbert Hoover in 1924. Within a year, eleven states had passed enabling acts, and by January 1926, Hoover could boast that more than four hundred municipalities had implemented zoning regulations, impacting “more than half the


urban population of the country.”24 Local authorities took their cue from explanatory footnotes urging them to adopt the model legislation with little to no amendment, since the federal government already had researched constitutional provisions and case law precedents state by state. The result was a Progressive Era tour de force for “promoting health, safety, morals, or the general welfare of the community” by regulating “the density of population, and the location and use of buildings, structures, and land for trade, industry, residence, or other purposes.”25

The Supreme Court upheld municipal zoning in Village of Euclid v. Ambler Realty (1926), with Justice George Sutherland opining, “A nuisance may be merely a right thing in the wrong place—like a pig in the parlor instead of the barnyard.” Henceforth, local legislative debate would focus on the proper means for determining the most prudent regulations for eliminating “the evils of over-crowding, and the like, and excluding from residential sections offensive trades, industries and structures likely to create nuisances.”26 State courts routinely emphasized the importance of preserving “the very foundation of good citizenship” by “the fostering of home life” through zoning.27 As Justice William Douglas, who had served as secretary of the Securities and Exchange Commission under President Franklin Roosevelt, opined in 1974, toward the end of his record-setting thirty-six year tenure in the Supreme Court:

The regimes of boardinghouses, fraternity houses, and the like present urban problems. More people occupy a given space; more cars rather continuously pass by; more cars are parked; noise travels with crowds.

A quiet place where yards are wide, people few, and motor vehicles restricted are legitimate guidelines in a land use project addressed to family needs. . . . The police power is not confined to elimination of filth, stench, and unhealthy places. It is ample to lay out zones where

25. Ibid., pp. 4, 5.
family values, youth values, and the blessings of quiet seclusion and clean air make the area a sanctuary for people.\footnote{Village of Belle Terre v. Boraas, 416 U.S. 1, 9 (1974).}

The resulting patchwork of local zoning restrictions has not only fostered residential cul-de-sacs where children may safely play ball or ride their bikes, but also created neighborhoods in which entrepreneurial pursuits are prohibited, thereby forcing parents to commute to jobs or else operate clandestine home-based businesses. When the family wage disappeared from American economic life in the 1970s, it became increasingly difficult for a single earner to support a family.\footnote{Ryan C. MacPherson, “Marital Parenthood and American Prosperity: As Goes the Middle-Class Family, So Goes the Nation,” Family in America 26.1 (Spring 2012): 1–21.} A labyrinth of zoning ordinances has also made it difficult for the second earner to work at home where she can remain close to her children. (Let it be remembered that “two-thirds of full-time home-based workers are women.”\footnote{Garnett, “On Castles and Commerce,” p. 1213.}) Some cities permit psychologists, but not psychiatrists, to work from home; other cities allow artists’ studios, but forbid photographers’ studios. Often residential zones prohibit the storage of sales inventory in one’s garage or basement.\footnote{Joanne H. Pratt, “Legal Barriers to Home-Based Work,” National Center for Policy Analysis Report No. 129, September 1997, pp. 26–27.} Zoning ordinances have not kept pace with the dot-com revolution, relegating e-Bay moonlighters, telecommuters, and self-published authors to the outdated Victorian category of commercial vice as they operate in the home-based black-market economy.

Ironically, women and children, whose safety and purity the Victorians ostensibly had in mind, may suffer the most from the consequences of the zoning laws that Victorian-minded policymakers first pioneered. Rather than spending their days together, they become estranged through the forced separation of family and work. Unwed mothers have it especially tough. Linda Fisher, a single mom struggling to support her son, incurred a fine in Westminster, Maryland, for selling homemade muffins to her neighbors in 1997.\footnote{Garnett, “On Castles and Commerce,” p. 1218.} Reader, beware: before hosting another Mary Kay, Tupperware, or Amway party, you might...
want to check with the local zoning authority. Be sure to also ask a lawyer about other state and federal regulations of home-based enterprises. For example, Wisconsin child-labor law prohibits a minor under the age of twelve from working in a parent’s home business. Even adults must be careful about what they produce at home. Starting in 1942, federal law prohibited homespun production of seven classes of apparel; when the Department of Labor rescinded the ban in 1981, textile producers and trade associations took the issue to court.

At the center of the controversy, several New England women had dared to knit sweaters at home rather than commute to minimum-wage textile-factory jobs. Union supporters warned that unregulated homespun put women in jeopardy of harsh conditions and low wages, but the New England knitters disagreed, complaining that factories were noisy, work days were long, commutes were expensive, and—worst of all—“mothers and fathers . . . only see their babies when they are asleep in their cribs. Believe me, ‘minimum wage’ doesn’t begin to cover it.” Nevertheless, the U.S. Court of Appeals ruled in favor of the textile industry, finding Ronald Reagan’s laissez-faire labor secretary “arbitrary and capricious” for suspending protective labor laws.

Not all home-work violates the law, but federal housing policy has done little to encourage family productivity while doing much to discourage home-based enterprises. The Housing Act of 1949 promised “a decent home . . . for every American family,” but after forty years of ascendant individualism, the history books truncated that slogan to “a decent home for every American.” In the intervening years, mortgage guidelines drafted by the Federal Housing Administration (FHA) restricted homebuyers from investing in properties designed to accommodate productive space (a shop or office) in addition to consumptive space (a family dwelling). As the FHA increased its market share, builders were less

33. Wisconsin Statutes 103.67(2)(g) (2011).
willing to pursue cottage-industry architecture that subsidized buyers would not be able to purchase. Fannie Mae historian Gertrude Sipperly Fish acknowledged that “the family was no longer the basic economic as well as the social unit,” so homes constructed for the late twentieth century would have smaller kitchens stocked with processed food and fewer work spaces for anything productive. Ironically, it is precisely when people were doing less and less at home that the government became more and more concerned that people could afford housing.

What, then, has been the combined impact of zoning ordinances, labor regulations, and federal housing guidelines over the past half century? Nothing short of government-subsidized suburban dormitories. As law professor Nicole Stelle Garnett has observed:

The legal segregation of commercial and residential uses of property contributes to this isolation not merely by depriving residents of places to gather within their neighborhoods, but also by virtually guaranteeing that they rarely will be in their neighborhoods. . . . [S]uburban neighborhoods are empty during the day. Moms and dads go to work; kids go to school or childcare centers.

The Moral Hazard of Meddling with Housing

Alex F. Schwartz, chair of Urban Policy Analysis at the Milano School of International Affairs, Management, and Urban Policy, finds that “the United States has the world’s largest and most complex system of housing finance.” In such an environment, it is hardly surprising that “housing policy is seldom just about housing.” Proposals often explicitly identify goals as diverse as modern plumbing, building family wealth, integrating various racial groups, and managing metropolitan growth, but the


The real significance of housing policy lies in unstated goals and unforeseen effects.

As President Franklin D. Roosevelt began his second term in 1937, he spoke of “one-third of the nation ill-housed, ill-clad, ill-nourished.” This was classic FDR rhetoric—rousing words that would ultimately unfold his vision of national progress. “I paint it for you in hope,” he said, calling upon “those who have much” to “provide enough for those who have too little.”

Congress delivered, enacting the Housing Act of 1937 to establish public housing programs that would continue where the first wave of New Deal reforms had left off. The Home Owners’ Loan Act of 1933 sought to rescue people from the Great Depression’s foreclosure crisis. The National Housing Act of 1934 established the FHA to spur on housing construction and provide government insurance for private mortgage lenders. Other programs played less obvious roles in changing the housing market.

For example, the National Industrial Recovery Act of 1933 included a provision for aiding low-cost housing initiatives. The first beneficiary, to the tune of $1,039,000, was the American Federation of Hosiery Workers, a Philadelphia-based union that in the 1920s had already been seeking to provide housing benefits to its members. The Hosiery Workers had clear objectives for broader social reform, hoping to forge an industrial order in which workers were so united economically and socially that they could curtail the influence of capitalism over their lives. Oskar Stonorov, the architect for their Mackley Houses apartment complex, shared their ideology, calling owner-occupied, single-family homes “fortresses of individualism” that must be replaced by the erection of cooperative living spaces that could unite workers’ families into a communal lifestyle. Stonorov and his union clients further hoped that such architecture would foster political support for public pensions that would replace the family-owned home as the chief security against insolvency or old-age dependency.

Housing policy thereby solidified the New Deal coalition.

The New Deal, meanwhile, did not assist all Americans equally. FHA

40. Franklin Delano Roosevelt, Second Inaugural Address, January 20, 1937.

41. Radford, Modern Housing for America, pp. 123 (quotation), 128.
appraisals reinforced racial stereotypes, fostering discriminatory lending and establishing de facto residential segregation that relegated minorities to public-housing projects. The federal government subsequently sought to address the racial disparities through enactment of the Fair Housing (1968), Equal Credit Opportunity (1974), and Community Reinvestment (1977) acts. Meanwhile, a plethora of government programs developed, intertwining federal, state, and local authorities with the private sector in economic arrangements that subsidized both rented and owner-occupied properties. All in all, “housing is a mainstay of the U.S. economy, consistently accounting for more than one fifth of the gross domestic product,” and one of the greatest investors is Uncle Sam.

The largest housing expenditures by the federal government are, however, kept off the books, in the only two American corporations that have federal charters: the Federal National Mortgage Association (“Fannie Mae”) and the Federal Home Loan Mortgage Corporation (“Freddie Mac”). Fannie Mae, initially chartered in 1938 and converted into a publicly traded private corporation in 1968, expanded lending opportunities by buying FHA-insured residential mortgages from the originating banks. The Government National Mortgage Association (“Ginnie Mae”) took over Fannie Mae’s on-the-books activities within the Department of Housing and Urban Development (HUD) after Fannie became privatized. Freddie Mac, created in 1970 and converted into a publicly traded corporation in 1989, initially securitized mortgages originated by savings and loans associations, but in time the activities of Freddie and Fannie have blended together. Since 1980, Fannie’s and Freddie’s asset holdings have grown nearly twenty-fold, outpacing the residential mortgage market as a whole and accumulating, by 2000, a 71-percent market share of eligible single-family, fixed-rate mortgages. By December 2003, Fannie and Freddie were the second- and third-largest U.S. corporations, with combined assets of nearly $2 trillion, forming a formidable duopoly in


43. Schwartz, Housing Policy in the United States, p. 4.
the mortgage industry.\textsuperscript{44}

Traders on the New York Stock Exchange long considered both Fannie and Freddie to be safe investments. Not only were their debts securitized by real estate, but their solvency was also implicitly guaranteed by the U.S. Treasury Department. The two corporations thus played a “double game” of leading investors to believe the government would back them, while assuring Congress that Fannie’s and Freddie’s finances were not part of the federal ledger. The two corporations proved very profitable through the turn of the century, multiplying their return on investment through a highly leveraged capital-to-asset ratio of less than 4 percent. (FDIC-insured depositors, by contrast, must maintain a capital-to-asset ratio of 9.2 percent.) Lurking underneath the profit margin, however, was the moral hazard created when creditors relaxed their gaze because they thought their money was safe with these government-sponsored enterprises (GSEs).\textsuperscript{45} The implicit federal guarantee became explicit when Congress brought the GSEs under federal conservatorship in 2008. Meanwhile, the foreclosure rate had already soared between 2006 and 2007, up 79 percent nationwide, and leaping some 300 percent in California, where one in fifty houses went into foreclosure proceedings, evaporating the benefits—especially for first-time home buyers and racial minorities—that Freddie and Fannie worked so aggressively to deliver.\textsuperscript{46}

Another crack in the foundation of federal housing policy may be discovered in tax incentives. Libertarian diehards and social-welfare advocates both agree that federal tax incentives favoring mortgaged homeownership have inflated the housing bubble with a lot of hot air, some of which may still need to leak out before housing prices stabilize again. In terms of tax benefits, buying beats renting, and borrowing beats buying outright. The home-mortgage interest deduction is, for many


\textsuperscript{45} Ibid., pp. 159, 160, 175.

families, the largest single tax-saving vehicle, outperforming deductions for IRA contributions and employee-paid health insurance premiums, for example. On the government’s side of the ledger, the mortgage deduction exceeds all other federal tax expenditures for housing combined. Moreover, homeowners also can deduct property taxes and exclude capital gains upon selling their home (up to $500,000 per married couple, once every two years), as well as avoid the 10 percent early-withdrawal penalty if they apply a premature IRA distribution toward the purchase or improvement of a home. Tax incentives for rental-housing developers—such as accelerated depreciation and the Low-Income Housing Tax Credit—barely amass to one-tenth the value of personal tax savings imputed to homeowners.47

The IRS Form 1040 is a buyer’s market, “channeling more artificial demand into the housing sector,” in the estimation of free-marketeer Thomas E. Woods Jr.48 The analysts who share this perspective include Federal Reserve Board economist Hui Shan. When the Taxpayer Relief Act of 1997 excluded capital gains from the sale of any home that had been owner-occupied for two of the preceding five years, he notes that ownership turnover escalated, with sales rates for homes characterized by capital gains beneath the $500,000 exemption limit rising 19 to 24 percent. Shan further finds that turnover for homes with gains above that limit also increased, encouraged by a reduction in the long-term capital gains tax from 28 percent to 20 percent in the 1997 legislation, by further reduction in 2001 to 18 percent (for assets held at least five years), and finally, in 2003, to 15 percent (for assets held at least one year).49

In the wake of the Taxpayer Relief Act, home prices began rising not merely because demand increased after transaction taxes had been reduced or eliminated, but also because many Americans regarded a home purchase not just as a consumer expense (analogous to paying

47. Schwartz, Housing Policy in the United States, p. 90, table 4.1.


rent) but also as an investment to hedge against inflation (“the nest has become the nest egg”50). Whereas rising prices in consumer goods discourage further consumption, rising prices in assets encourage buyers who hope to ride the wave of investment gains. Once jump-started by the 1997 act (and further fueled by the Federal Reserve Board’s inflationary monetary policy), the process became self-perpetuating—until, of course, the bubble burst.51 Shan predicts that the bubble will deflate still further, now that the long-term capital gains rate for 2012 has returned to 20 percent, the highest rate in twelve years.52

As Americans entered the twenty-first century with a government-induced homeowner craze, they had not yet recognized the sarcasm in humorist Dave Barry’s analysis: “It’s easy to get rich in real estate. You don’t have to take any risk, or work hard, or even have a central nervous system.”53 Apparently lenders did not need a central nervous system any more than buyers did. At the peak of the bubble, an $8-per-hour clerk was named “vice president” of five different banks simultaneously and cranked out 4,000 signatures per day as a “robo-signer” on mortgage loan documents. But at least this VP was not forging someone else’s signature, as happened 250 times in a case brought before a New Jersey bankruptcy judge in 2006.54

Already in 2002, MERS had been registering itself as the owner of 21,000 loans per day. And as volume swelled, the information-technology proverb “garbage in, garbage out” gained an ugly relevance. Not only did banks find themselves unable to foreclose on delinquent home buyers, but diligent homeowners who paid every month on time discovered that MERS had assigned their mortgage somewhere else; they had been paying “rent” to the wrong bank, while failing to fulfill their mortgage

52. Shan, “The Effect of Capital Gains Taxation on Home Sales.”
obligations to the bank on record with MERS. Courts have struggled to find a consistent response to the mess occasioned by computers that think faster than people. A five-minute loan origination one day may well lead to a five-minute foreclosure processing another day. But ultimately the foreclosing bank is no more secure than the evicted homeowner. “You are acting as a robot for a plaintiff who is not even giving you the information you need to file a proper foreclosure,” said one judge, chastising a mortgage bank’s “robo-lawyer.” Perhaps it is time for the children of the electronic age to reconsider some old-fashioned ideas.

Rebuilding Home(ownership) Economics from the Family Up

Now that the national median price-to-income ratio has returned to its historic average of about 3.4 percent, Americans are beginning to put the housing bubble behind them. For potential buyers, a drop in home values is a welcome opportunity. For sellers, it is confirmation of the old adage that what goes up must come down—especially if it never belonged up in the first place. Important lessons seldom come easy for the learner, but a lesson learned well once will not have to be learned again. So what are the morals of this story?

First, the nation must realize that giving people what they have not earned and cannot maintain destroys the very social capital that homeownership purportedly fosters. As the dust settles from the recent housing crisis, it now is clear that “loans that were developed and actively marketed to lower- and middle-income borrowers to help them achieve their homeownership dream have placed them at risk of losing both their housing investment and any reasonable chance to permanently change their social status from renter to homeowner.” Mandatory financial education for borrowers might help, particularly if such education includes a fair assessment of the advantages that renting sometimes holds over buying. Public policy should reflect a nuanced understanding of home-

ownership: costs, benefits, responsibilities, and alternatives. For a promising path forward, consider innovative Neighborhood Stabilization Plan programs, such as the American Equity Foundation’s “Continue Home” initiative. This program strives to keep families in their original homes after foreclosure by enrolling them in a rent-to-own rehabilitation service complete with credit enhancement and financial education.59

Second, subsidized homebuilding is a poor tool for fostering economic development. What seems good for Levitt and Sons, or Home Depot, may not always be good for America. Rather, the free market can determine what is best for America more efficiently than the majority of 535 part-time residents of Washington, D.C., and the tenant with a four-year lease at 1600 Pennsylvania Avenue. When government allocations, whether directly through HUD or indirectly through the GSEs, send more dollars chasing after homes, and when tax breaks make the net costs gapingly lower than the nominal costs, then demand within the housing sector increases faster than the market would spontaneously allow. The initial result of this artificial demand for housing is inflation, but inflation does not impact all parties equally: owners feel richer while nominal home values rise, but buyers feel increasingly pinched by the changing market. As the eighteenth-century British political economist Richard Cantillon discovered, those first-in-line in an inflationary economy receive the benefits, while those last-in-line bear the costs, since the dollars they are holding can no longer purchase as much as they could in the recent past.60 In practical terms, this means that housing developers and homeowners initially fare better, on average, than homebuyers. Subsequent injections of housing credit can briefly empower another generation of buyers, but only by disadvantaging those who follow them (as well as those who choose to purchase something other than housing). When artificial credit dries up, the bubble bursts and owners find themselves under water in a foreclosure market that rewards a new kind of bottom-feeding buyer.


At a minimum, policies intended to assist those who cannot afford a particular level of housing must be crafted carefully to deliver the intended benefits to the intended people. A refundable tax credit for housing expenses—whether rented or owned—would in this regard do more than the current mortgage-interest deduction for households with income below the standard-deduction threshold; as it currently stands, the mortgage-interest deduction aids families struggling to afford a second home, not necessarily a first one. To reach the working- and lower-middle classes, a housing-related tax break “must allow households to claim a benefit beyond the standard deduction, and it must be refundable.”\(^{61}\) Of course, this strategy for assisting the working and lower-middle class also carries its own Cantillon risks.

So long as policymakers concern themselves with getting people into homes, they may as well think about what people might do at home. Public policy should permit and encourage, rather than penalize or intimidate, home-based businesses by following a few common-sense suggestions:

1. Abolish zoning regulations that forbid neighborhoods from being economically productive simply because they are designated as “residential.” Regulations instead should permit non-disruptive home-based business practices, including e-commerce, consulting, or other activities that are no more obtrusive than hosting a child’s friends for a birthday party. “The legal rules,” as Garnett remarks, “should not target the businesses themselves, but rather their potential for generating negative externalities.”\(^{62}\)

2. Amend child-labor regulations to allow parents to employ their children in a safe and responsible manner, allowing—for instance—parents to hire a nine-year-old to file papers alphabetically or an eleven-year-old to build a website. The state’s presumption should be that a parent’s home business functions not as a sweatshop for exploiting minors, but rather as a schoolhouse for instilling the

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virtues of cooperation and diligence, just as countless home-based enterprises did prior to the late-nineteenth-century separation of work from family.

3. Repeal union-favoring legislation so that home-based entrepreneurs may compete for a market share in, for example, the knitwear industry, again provided that the work they perform at home does not disturb the peace of the neighborhood (which knitting hardly ever would).

4. Replace IRS regulations that limit home-office deductions to household space that is reserved 100 percent for business use to a more reasonable threshold, such as twenty hours per week. If a freelance writer uses the dining-room table more often for work than for family meals, then why should the fact that it also is used for meals prevent the deduction?

Before suggestions like these can be taken seriously, lawmakers will have to jettison their twentieth-century housing policy paradigms and revert to a more traditional set of expectations. Only then can the American dream be once again seen as an opportunity for home-based businesses, not merely homeownership.

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