

Renting vs. Buying Shelter in Michigan Communities



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Considering buying a home? If you do, you will join a majority of American families. By 1974, home ownership had become a reality for 65% of American households and projections at that time were that by the late 1970's, even more families would own homes.

If you are like the average family in a recent **HOUSE AND HOME/HOUSING** survey, you have high expectations for what you hope to own. The families surveyed, for instance, preferred a detached, split-level home to a two-story or single-story house; they overwhelmingly wanted 3 or 4 bedrooms with large closets included, and compartmental baths. In addition, they wanted at least 1500 square feet of living area.

That was the basic dream-house buyers were seeking in the housing market in 1976. Today, however, many buyers find that the very high cost of this package, along with the high interest rates being charged to finance the purchase of a home plus increasing energy costs to heat and cool a house, make them reconsider whether to join the homeowner's ranks. Thus, for some families, renting has become a more viable alternative.

There are basic advantages and disadvantages to both forms of occupancy. Only you, knowing the particular needs and wants of your family as well as the financial situation of your family, can make the final decision. Weighing the key factors involved may help.

Advantages to Buying in Comparison to Renting

—Inflation will increase rental costs, as it will costs of home ownership; however, the home purchaser has several advantages over the renter. If the monthly mortgage payment to the lender includes taxes and

insurance, it could go up when these costs rise but the payment for the principal and interest portion remain at pre-determined amounts, if you take out a level payment mortgage. If you have a graduated payment mortgage the principal and interest payment will go up in known steps according to the mortgage agreement. If you take out a variable interest rate mortgage, the monthly principal and interest payment may increase or decrease, depending on the going interest rate.

—Ownership has traditionally been an excellent hedge against inflation for the average consumer; appreciation of the home during the time it is owned helps the owner realize a substantial gain when the property is sold (this has been especially true in the late 1970's as prices for housing have increased dramatically).

—Appreciation of value realized in resale is generally treated as a "capital gain" for federal income tax purposes. Thus, the gain is taxed at a more favorable rate than personal service income such as salaries and wages. The capital gain tax may be deferred by investing in a home of equal or greater value within 18 months of the sale. Capital gains from several previous homes can be carried over, as long as you continue to invest in houses of equal or greater value.

—If the seller is 55 or older, up to \$100,000 of capital gain can be excluded once in a life time on the sale of an owner occupied home.

—Property tax and mortgage interest payments are deductible from income for federal tax purposes for those who itemize and do not take the standard deduction. If your taxes, interest, charitable contri-

butions and casualty losses exceed the standard deduction, then you will come out ahead of those who are renting. In Michigan, for state income tax purposes, both renters and owners can claim a property tax credit equal to the amount by which their property taxes exceed 3.5% of their income. (Currently, renters compute the amount for property tax credits by considering 17% of their yearly rent as property tax.)

—Ownership may be a desirable form of forced savings for some consumers. Principal invested each month is returned when the property is sold, as well as the "interest" gained on it by appreciation of the property.

—Costs of ownership exclude paying a landlord for the costs of managing the property, for maintaining vacant dwellings, and paying for the landlord's profit.

—Through ownership you can avoid paying for costly services often available in rental units that you may not want to use (e.g., pools, party rooms).

—Ownership assures that you cannot be forced to move because the lease was not renewed or the rent was increased.

—Ownership reduces dependence on others to make repairs or provide routine maintenance.

—Ownership allows greater freedom to make changes you desire, both inside and outside the dwelling. Condominium and cooperative forms of ownership may place restrictions on this freedom, however. If you purchase these forms of shelter, inquire about your rights to change the exterior of your home.

—Ownership, for some people, can provide a strong emotional advantage. You have made a long-term geographical commitment and thus may feel freer to develop strong ties to the community, and become involved in its problems and its benefits.

Disadvantages of Buying in Comparison to Renting

—Ownership ties up your financial resources. By making a down payment the homeowner loses dividends and interest which the money could produce if invested wisely in some alternative, one that would give a greater return on each dollar than housing value increases; renting gives greater financial flexibility.

—Although ownership recently has been a good hedge against inflation (with the value of housing units rising faster than the rate of inflation) there is no assurance that this trend will continue. For example, during the depression of the 1930's, housing values declined and resale was difficult. Currently, in some areas facing declining populations, values of homes are going down. And finally, there is simply no guarantee that values will continue to increase in the future at the rapid rate they have in the 1970's.

—The "absolute costs" or "true costs" of renting

may be lower than the costs of ownership due to several factors: 1) state income tax credits given to renters may help reduce renting costs; 2) due to the landlord's favorable income tax treatment, which allows him to depreciate the property as he owns it, savings are sometimes passed on to the renter, thus cutting some costs; and 3) in apartment situations, land costs, construction costs, and maintenance costs may be less due to the density of people occupying the site. This may help reduce rental costs in comparison to purchase costs.

—Ownership involves costly and often unexpected maintenance, repair, and replacement expenses. When you rent, these expenses are built into your monthly rental fee and the landlord has the headache of seeing to them, not you.

—Ownership limits your freedom to easily change your housing situation as family needs, size, employment, or income change. Selling a house involves an expense and time; renting seldom does.

—Ownership involves the expense of financing the purchase (generally 2% or more of the purchase price is required to pay the "extras" involved in settlement in addition to the down payment) and eventually, the cost of selling the property (generally 8% or more of the sales price is required to pay the real estate agent's commission, assessments, property taxes, attorney's fee, etc.). Renter's expense involves the loss of the use of capital, if required, for security deposits and may require loss of this income completely if the rental property is left in damaged condition.

—Special services and facilities are often available to renters for a nominal charge, services which may be too expensive for homeowners to provide themselves.

—Ownership requires time; no one cares for routine maintenance and repair but you. Renting, on the other hand, requires less personal involvement in the property; taxes, insurance, repairs, and sometimes utilities are someone else's responsibility, although responsible upkeep and care of the property on the part of the renter is to be expected.

—Property tax rate changes, maintenance and repair costs, and utility costs have increased rapidly in the past decade, and some of these costs are expected to continue rising. It is the increases in these costs that are difficult to predict, where ownership is involved, and thus they make ownership somewhat riskier than renting because the homeowner pays for them directly.

Once you have made the decision to buy a home rather than rent, you face a second alternative. Should you build or buy a new home, or buy an existing home? The majority of the housing stock in this country consists of older or "used" homes. Thus, this alternative may provide more choices than buying new. There are other factors to think about as well.

Advantages of an "Older Home" in Comparison to a New Home

—In older homes you frequently find more space available for the money invested.

—Price and value are more likely to be established in older homes and not artificially inflated by "newness" or stylistic features that may quickly become out-dated.

—If the house needs repairs, the buyer, who enjoys and is able to adequately complete do-it-yourself projects, can make improvements to increase livability and comfort by investing time and skills rather than financial resources.

—During periods of "short money" when interest rates and down payment requirements are increasing, the buyer may be able to assume the seller's mortgage or negotiate a land contract at terms more favorable than a new mortgage.

—It may be somewhat easier to predict the costs of taxes, assessments, utilities and insurance on older homes, as these expenses have established a pattern over time.

—A wider range of locations is available if you choose an older home simply because there are more older homes than new homes available. In addition, new homes, in urban locations at least, tend to be clustered together, thus reducing location options.

—It is easier to predict how family satisfaction will be influenced by location when you purchase an older home since neighborhood character and traffic patterns are well established and apparent.

—Costly landscaping may be minimized in an older home, since trees, shrubs, and lawn are more likely to be mature.

—A greater choice of character, style, design, materials and other features are available in older homes.

—Occasionally, unique craftsmanship and finishing details may be found, things that are usually only available in older dwellings.

—The quality of a new house is greatly dependent on the reputation of the builder and the materials and workmanship used. Often problems don't show up for a period of time. With older homes problems may be easier to spot. Settling, shrinkage, drainage, and other problems have become evident and can be seen if you take the time to look.

Disadvantages of Buying on "Older Home" in Comparison to a New Home

—Although older homes are usually less costly than new homes, and thus may give you more space per dollar spent, you may find that the design, layout, and floor plan of the older home are dated and not suitable for your present life style.

—Unless you have dollars to invest in major furnishing or remodeling changes, you may be stuck with someone else's mistakes, headaches, or inconveniences.

—Resale value of an older home may not increase as much as that of a newer home. This, of course, will depend upon location, condition of the home, demand for housing in the area, and other factors.

—Resale value may not appreciate significantly with simple cosmetic improvements such as painting, especially if the structure or any utility systems are deficient.

—Some financing alternatives available with older homes, especially land contracts, may be quite risky and provide less protection than regular mortgage financing.

—Operating expenses for utility and maintenance are usually more expensive in older homes. These two costs have taken an increasing share of the home ownership dollar in recent years and are expected to continue to do so.

—The neighborhood in which the home is located may be deteriorating economically and physically to the extent that it is difficult for individual owners to realize a financial benefit by investing in the area. It is possible to arrest such decay, but it takes commitment from others in the area as well as the individual owner.

—Any craftsmanship or finishing details available in the home originally may have been lost through years of owner "improvements."

—The buyer may purchase the problems the seller is attempting to abandon. There is usually no warranty on construction or equipment available from the seller of older homes. However, some realtors now offer a warranty on used homes to protect the purchaser against defects in heating, electrical and plumbing systems. The warranty can be purchased by either the buyer or the seller. Information on these warranty programs can usually be obtained through real estate brokers in your area.

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