Research Priorities for Low-Income Housing Policy

Ed Olsen
Department of Economics
University of Virginia

Presented at Conference on Building Evidence to Promote Stable Housing
Sponsored by Wilson Sheehan Lab for Economic Opportunities
In Partnership with Catholic Charities

June 8, 2017

I'm delighted to have this opportunity to talk with such a distinguished group of researchers and practitioners about a topic dear to my heart, and I want to thank Jim for organizing this conference. I've followed research and debates about housing policy for many years, and two years ago I wrote a survey of the evidence on the performance of low-income housing programs. Jim told me that the primary goal of the conference is to lay the groundwork for a number of large-scale research projects that would provide rigorous evidence of program impact. We decided that my best contribution is to give you my views about the most important gaps in our knowledge from the viewpoint of housing policy reform.

To my mind, the title of the conference Building Evidence to Promote Stable Housing indicates a focus on the very poorest people. They are the people who are evicted or who move to avoid it. I believe that the solution to this problem is to offer housing assistance to all of the poorest people. Contrary to popular opinion, this does not require additional public spending. I've written a paper that shows how reforms of HUD's low-income housing programs would enable us to offer housing assistance to all of the poorest households without spending more money. This involves phasing out cost-ineffective project-based housing assistance and offering housing vouchers less generous that the current Housing Choice Voucher program. I estimate that the proposed reforms would ultimately double receipt of housing assistance by the poorest 10 percent of households.

Overview of Current System

Even though I'm sure that everyone in the room has considerable knowledge of some parts of the current system of low-income housing assistance and some familiarity with the entire system, Jim suggested that I take a few minutes to provide an overview.

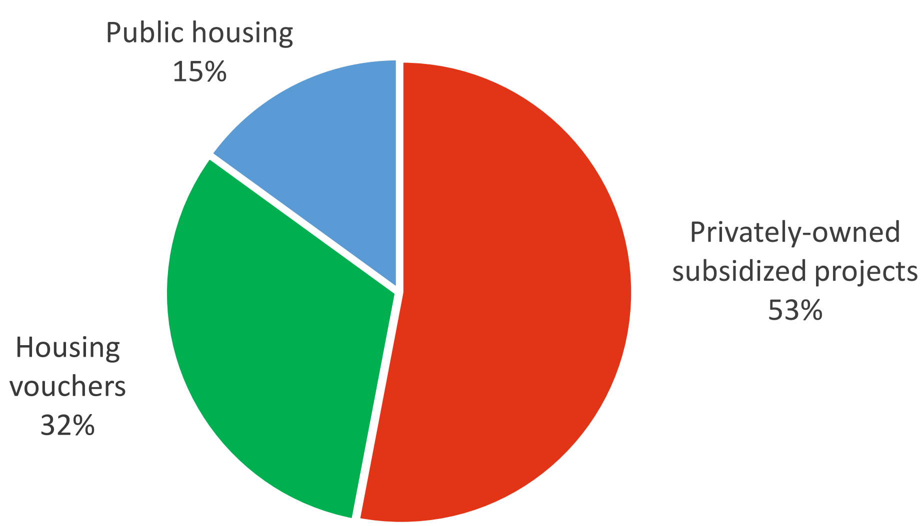
The bulk of low-income housing assistance in the U. S. is funded by the federal government through a large number of programs with a combined cost of more than $50 billion a year. State and local governments spend an unknown, but surely much smaller, amount from their own resources.

Unlike other major means-tested transfer programs like Medicaid, food stamps, and the EITC, low-income housing programs don't offer assistance to all of the families that are eligible for them. Eligible families that want assistance must get on a waiting list, and waiting lists are often long and usually closed to new applicants.

Most low-income housing assistance in the U.S. is for renting a unit, and the most important distinction among rental housing programs is whether the subsidy is attached to the housing project (project-based assistance) or the assisted household (tenant-based assistance). If the subsidy is attached to a housing project, the family must accept the particular unit offered to receive assistance and loses the subsidy if it moves unless it can find alternative housing assistance before moving. Each family offered tenant-based assistance is free to occupy any unit that meets the program's minimum housing standards, that rents for less than the program's ceiling, that is affordable with the help of the subsidy, and whose owner is willing to participate in the program. The family retains the subsidy if it moves to another unit meeting these conditions.

Figure 1 indicates the percentage of subsidized households that receive each type of rental assistance.

Figure 1



There are two broad types of project-based rental assistance: public housing and privately owned subsidized projects. Both types have usually involved constructing new buildings. In almost all other cases, they've involved substantial rehabilitation of existing buildings. Many of these programs no longer subsidize the construction of projects, but most projects built under them still house low-income households with the help of subsidies for their operation and renovation.

Public housing projects are developed and operated by local government agencies called public housing authorities, albeit with substantial federal subsidies and regulations that restrict their choices. In the public housing program, government employees make most of the decisions that unsubsidized for-profit firms would make in the private market—what to build, how to maintain it, and when to tear it down. Decisions about where to build projects have been heavily influenced by local political bodies. The public housing stock has declined by about 400,000 units since its peak in 1991. Today about 1 million households live in public housing.

Government agencies also contract with private parties to provide housing in subsidized projects. Most are for-profit firms, but not-for-profits have a significant presence. Under these programs, in exchange for certain subsidies, private parties agree to provide rental housing meeting certain standards at restricted rents to eligible households for a specified number of years. There are many programs of this type. The largest are the Low-Income Housing Tax Credit (LIHTC) that is funded mainly by the federal government but administered by state housing agencies and HUD's Section 8 New Construction Program. About 4 million households live in projects of this type.

Overall, project-based assistance accounts for about two thirds of all households that receive low-income rental assistance.

HUD's housing voucher program is the only significant program that provides tenant-based assistance. It's the second-largest low-income housing program, serving about 2 million households and accounting for about a third of all households that receive low-income rental assistance. It's funded entirely by the federal government but administered by the same local government agencies that administer the public housing program.

Overview of Evidence on Program Performance

My survey of the evidence about the performance of low-income housing programs covered many topics.

EFFECTS OF LOW-INCOME HOUSING PROGRAMS

- **Consumption Patterns**
- **Neighborhood Choices**
- **Recipient Health**
- **Education Achievement**
- **Labor Earnings and Employment**
- **Mean Recipient Benefit and Subsidy**
- **Participation Rates**
- **Distribution of Recipient Benefits**
- **Neighbors**
- **Market Rents**
- **Crowd-out Private Production**
- **Cost-Effectiveness**

In designing housing policies, what we would like to know about each program and about each proposed reform is its cost and its effects in these and other respects. In the survey article, I mentioned that putting together this information from the existing literature resembled an archaeological dig and that the dig revealed many gaps in our knowledge.

We have no high-quality evidence on the cost-effectiveness and most other outcomes of the largest new low-income housing programs, the LIHTC and HOME, despite the fact that they aren't at all new. They were established in 1986 and 1990 respectively.

And we have no recent evidence on many aspects of the performance of older programs that subsidized the construction of housing projects, still subsidize their operation, and house a substantial minority of assisted households. For example, no attempt has been made in quite some time to determine how much better or worse housing public housing tenants occupy than they would occupy in the absence of housing assistance. Almost all evidence is based on data from the 1960s and 1970s, and the applicability of these results to the current situation is questionable.

Gaps Recently Filled

I completed the final draft of my survey in the fall of 2014. Most gaps in our knowledge that existed then still exist today. There are two notable exceptions, and we are very fortunate to have four of the people who filled these gaps with us.

In the fall of 2014, good evidence on the effects of low-income housing programs on the later adult outcomes of children in recipient households was scarce. Given the motivations for welfare assistance, this was a serious gap in knowledge. Since then, two excellent papers have been published on that topic and a third is being revised for publication. I'm talking about papers by Jens Ludwig and his coauthors, Raj Chetty and his coauthors, and Eric Chyn. I'll leave it to Jens and Eric to talk about this matter.

There have also been major developments in the study of homelessness. The final report of a superb cost-effectiveness study of alternative approaches to dealing with family homelessness has been published. Beth Shinn was a principal investigator. And Igor Popov has completed a first-rate dissertation about the effects on the number of unsheltered and sheltered individuals and families of spending more on the current system of homeless programs. I'll leave it to Beth and Igor to talk about programs specifically designed to help the homeless.

I don't have nearly enough time to talk about all of the remaining gaps in our knowledge. I'll focus on two – one quite specific and one very general.

Cost-Effectiveness

In my opinion, cost-effectiveness is by far the largest and most consequential difference between low-income housing programs. Since there are different types of cost-effectiveness studies, I'll be specific about the type that I have in mind, tell you what previous studies have shown about it, and explain why it is so important and why it's important to have new studies.

I'm talking about differences in the total cost of providing equally good housing in equally desirable neighborhoods under different programs. Total cost is the sum of the rents paid by tenants and all public subsidies. Within a market, market rent has been used as an index of the overall desirability of the housing and its neighborhood. Units with the same market rent are equally desirable overall.

It's easy to estimate the cost-effectiveness of the housing voucher program. Its total cost is the sum of the tenant's rent and HUD's payment to the landlord. Both are in HUD's administrative records. To estimate the market rents of the units occupied by voucher recipients, analysts first estimate a statistical relationship between the rent and characteristics of unsubsidized apartments, and then substitute the characteristics of the subsidized units into this estimated equation. Essentially, the predicted market rent of each voucher unit is the mean rent of unsubsidized units with the same housing and neighborhood characteristics.

The same approach is used to predict the market rents of units in subsidized housing projects. However, estimating the cost-effectiveness of housing projects is much more complicated for several reasons.

First, these projects almost always receive subsidies from multiple sources, the subsidies aren't all in the records of one agency, and some are well hidden. For example, public housing authorities don't pay full property taxes for their projects. Instead they make a small payment in lieu of property taxes. This represents a substantial subsidy from local governments. Almost all tax credit projects receive subsidies from several sources. All projects receive substantial tax credits. These can be up to 90% of development costs, and many are this large. Many receive loans at below-market interest rates. Some receive land at well below-market prices. Some receive property tax abatements. Some receive subsidies from public housing authorities in the form of project-based and tenant-based housing vouchers. And when tax credits are used to renovate or redevelop public housing or privately owned subsidized projects, these projects continue to receive substantial subsidies from the programs involved.

Another complexity is that the time path of the costs is usually very different from the time path of the market rents of the units, and so we wouldn't want to determine the cost-effectiveness of a housing project by comparing the cost with the market rent of the units in some arbitrary year. Instead, we would want to compare the present value of the total cost with the present value of the market rents of the units. This requires estimates of the market rents of units in housing projects in each year that they provide housing to low-income households at restricted rents.

The best evidence on the cost-effectiveness of housing programs in providing housing pertains to HUD's public housing program, its two largest programs that subsidized the construction and operation of privately owned projects, and its housing voucher program. The best study of HUD's largest program that subsidized the construction of privately owned projects (the Section 8 New Construction Program) found an excess total cost of at least 44 percent. That is, the total cost of providing housing under this program was at least 44 percent greater than the total cost of providing equally good housing under the housing voucher program. This translates into excessive taxpayer cost of at least 72 percent for the same outcome. It implies that housing vouchers could have served all the people served by this program equally well (that is, provided them with equally good housing for the same rent) and served at least 72 percent more people with the same characteristics without any increase in public spending. The best study indicates an even larger excess cost for public housing.

These large gains in the number of households that could be served equally well by shifting resources from one type of housing assistance to another explain why I attach so much significance cost-effectiveness studies. Anyone who truly cares about helping the poor will enthusiastically support cost-effectiveness analyses of alternative methods for delivering housing assistance to them.

The tax credit program is the largest and fastest growing low-income housing program. An important question is whether the older results apply to this program. The tax credit program has important similarities with HUD's Section 8 New Construction Program. It provides subsidies to selected developers on the condition that they provide rental housing meeting certain standards at restricted rents to low-income households for a specified number of years. However, there are also many differences. State housing agencies rather than HUD chooses which developers receive the subsidies, the subsidies are delivered through nonrefundable tax credits, etc. I don't regard these differences as fundamental. However, we can't know how important they are for cost-effectiveness or any other outcome without a careful study.

Given the large additional sum committed to the tax credit program each year (about $8 billion), we should have a cost-effectiveness study of this program that is at least as good as the studies of the older programs. We don't have such a study.

The best evidence available suggests that tax credit projects cost 16% more than the voucher program to provide units with the same number of bedrooms in the same metro area. This study unambiguously understates the cost of the tax credit program because it omits some of the public subsidies such as land sold to developers by local governments at below-market prices, local property tax abatements received by some developers, subsidies from the housing voucher program, and later subsidies for renovating the projects. Whether the present value of the market rents of tax credit units over their 30-year use agreement is greater or less than the present value of the market rents of voucher units is an open question.

The best evidence available also indicates that occupants of tax credit projects capture a small fraction of the subsidies provided to developers. This evidence indicates that the present value of the rent saving to tenants (the difference between the market rent of the unit and the rent paid by its tenant) is less than a fourth of the present value of the subsidies provided to developers. However, the quality of this evidence is far less than it ought to be given the magnitude of the public subsidies involved.

If I controlled a large budget for research on housing policy, studying the cost-effectiveness of different approaches to providing housing assistance would be my top priority. Specifically, I would fund a study of the highest quality that compared the cost-effectiveness of different types of tax credit projects with the cost-effectiveness of housing vouchers. The types of tax credit projects that I have in mind are those involving the renovation of privately-owned subsidized projects, those involving public housing redevelopment, and new construction projects that involve neither.

I hasten to add that the type of cost-effectiveness analysis that I've just described isn't the only type possible or desirable. It concerns the cost-effectiveness of a program in providing housing. The Family Options Study is excellent example of another type. This study estimates the cost and a wide range of effects of alternative approaches to dealing with homelessness. We should have more studies of this type.

How Cost-Effectiveness Varies with Market Conditions

Finally, to produce better housing policies, research needs to address the most influential disagreements in housing policy debates. One of the most important is whether different types of housing assistance work better in different types of housing markets. Specifically, many people believe that housing vouchers work better than subsidized construction in the loosest and least regulated housing markets but subsidized construction works better in the tightest and most regulated. Others believe that housing vouchers outperform subsidized construction programs in all housing markets. The effects of market conditions on the relative performance of housing vouchers and subsidized construction has never been studied systematically for any aspect of performance.

I can give you some empirical and theoretical reasons to believe that housing vouchers are more cost-effective than subsidized construction even in the tightest and most regulated markets.

Empirically, the data underlying the old cost-effectiveness studies isn't limited to markets with high vacancy rates and little regulation. It comes in part from cities such as NYC, L.A., Boston, and S.F.

Theoretically, there are good reasons to expect excessive cost in all market conditions for programs that subsidize **selected** developers to build housing projects. In part, the excess cost results from excess profits to developers who are awarded tax credits. That is why many more developers submit proposals than can be funded with the tax credits allocated to the state. It's why developers of tax credit projects spend so much on their proposals. It's why they commit all of the units in their buildings to the tax credit program. It's why some pay bribes to get their projects approved.

Another reason to expect the tax credit program to have an excess cost for the housing provided is that it badly distorts the mix of inputs used to produce housing. The tax credit subsidy is proportional to the project's development cost. The program provides no subsidy for land or later maintenance. Indeed, it incentivizes construction in neighborhoods where land is cheap. This leads to the construction of expensive buildings in areas with low land prices. Unsubsidized developers don't build housing anything like tax credit projects in the neighborhoods where most tax credit projects are built because unsubsidized households aren't willing to pay enough in rent for housing of that type at these locations to repay the cost of building and operating it. Furthermore, the program's structure also leads to poorly maintained units.

While these arguments have persuaded many housing policy analysts that housing vouchers are likely to be more cost-effective than subsidized construction programs in all market conditions, they haven't persuaded all housing policy analysts, let alone policy makers. If I were allocating HUD's research budget, I would insist that the cost-effectiveness study of the tax credit program versus housing vouchers that I proposed earlier be designed to determine the difference in their cost-effectiveness in markets that differ substantially in their average vacancy rate and other respects. The effects of market conditions on other aspects of the relative performance of housing vouchers and subsidized construction would also be high on my research agenda.