

## Comment on Jill Khadduri's "Should the Housing Voucher Program Become a State-Administered Block Grant?"

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### *Abstract*

The stated goal of the Housing Act of 1949 is "a decent home and suitable living environment for every American family." It is time that we delivered on that commitment. Contrary to popular opinion, this does not require spending more money on housing assistance. It can be achieved without additional funds by shifting all funds from less cost-effective methods for delivering housing assistance to choice-based vouchers as soon as current contractual commitments permit and by gradually reducing the large subsidies to current voucher recipients. The proposal to replace the Housing Choice Voucher Program with a block grant to states can contribute to this goal by precluding the use of the block grant funds for project-based assistance, increasing the targeting of assistance to the poorest families, and including the fraction of recipients with extremely low incomes in the formula for determining the performance rating of state programs.

**Keywords:** Affordability; Housing assistance programs; Mobility

### **Introduction**

Jill Khadduri has provided a thorough and balanced analysis of the advantages and disadvantages of converting the Housing Choice Voucher Program to a program of block grants to the states. Her analysis brings to bear considerable knowledge of the systematic evidence on the effects of housing programs. Overall, she supports the conversion of the voucher program to a block grant to the states provided that certain conditions are met.

I intend to (1) amplify on her major point, namely, the importance of maintaining the choice-based nature of the program and (2) address a major shortcoming of the Housing Choice Voucher Program and indeed the entire system of housing assistance, specifically, its nonentitlement nature. An appropriately designed state block grant program can address both of these concerns.

In my judgment, if the conversion of the voucher program to a block grant does not specify explicitly that the money allocated to each state must be used exclusively for choice-based assistance, it will not be in the interest of taxpayers who are not directly involved in providing

project-based housing assistance and it will be extremely harmful to many of the poorest members of society. Its advantages will be swamped by the disadvantages of the shift from choice-based to project-based assistance that will surely result from leaving this decision to state housing agencies.

Khadduri (p. 255) notes that the “superiority of choice-based rental housing assistance for most types of households in most housing markets has been well established through years of research and program experience.” She does not, however, provide details or references to the literature. Since this information is central to the discussion and since the overwhelming majority of those currently involved in debates on housing policy have not seen it, reviewing this evidence here is important.

Unlike other major means-tested transfer programs, housing assistance is not an entitlement despite its stated goal of “a decent home and suitable living environment for every American family” (Housing Act of 1949). This feature of housing assistance is a historical accident related to the nature of the first major federal housing program, and it is not defensible given the methods currently available for delivering housing assistance. That is, it is impossible to reconcile this feature of the voucher program and all other low-income housing programs with plausible taxpayer preferences. If we provide housing assistance at all, it should be an entitlement to everyone who is eligible. If anyone is eligible, it should be the families with the lowest incomes. The third section of this article explains how we can convert the voucher program to an entitlement housing assistance program for the poorest families without spending more money and how a housing block grant can be structured to promote the movement of the program in this direction.

### **Limit the block grant to choice-based housing assistance**

The Housing Choice Voucher Program is by far the most cost-effective program of housing assistance in the United States. Four major studies have estimated both the cost per unit and the mean market rent of apartments provided by housing certificates and vouchers and the largest older production programs, namely Public Housing, Section 236, and Section 8 New Construction.<sup>1</sup> The cost per unit includes the tenant’s rent and all direct and indirect costs incurred by federal, state,

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<sup>1</sup> The studies are Mayo et al. (1980), Olsen and Barton (1983), U.S. Department of Housing and Urban Development (1974), and Wallace et al. (1981). Olsen (2000) provides a description and critical appraisal of the data and methods used in these studies, as well as a summary of their results.

and local governments. These studies are based on data from a wide variety of housing markets and for projects built in many different years. Two were expensive studies conducted for the Department of Housing and Urban Development (HUD) by a respected research firm during the Nixon, Ford, Carter, and Reagan administrations. They are unanimous in finding that housing certificates and vouchers provide equally desirable housing at a much lower total cost than any of these production programs, even though all of these studies are biased in favor of the production programs to some extent by the omission of certain indirect costs.

Table 1 summarizes the results of these studies. The studies with the most detailed information about the characteristics of the housing provided by the programs found the largest excess costs for the production programs. Specifically, Mayo et al. (1980) estimated the excessive cost of public housing compared with housing vouchers for providing equally desirable housing to be 64 percent and 91 percent in the two cities studied (Phoenix and Pittsburgh) and the excessive cost of Section 236 to be 35 percent and 75 percent in these same two cities. Another study with excellent data on housing characteristics estimated the excessive cost of Section 8 New Construction compared with tenant-based Section 8 certificates to be between 44 percent and 78 percent (Wallace et al. 1981).<sup>2</sup>

*Table 1. Excess Cost of Older Production Programs*

Program/Study	Localities	Projects Built	Excess Cost (%)
Public Housing			
Olsen and Barton 1983	New York City	1937–1965	14
Olsen and Barton 1983	New York City	1937–1968	10
HUD 1974	Baltimore, Boston, Los Angeles, St. Louis, San Francisco, Washington, DC	1953–1970	17
Mayo et al. 1980	Phoenix	1952–1974	64
Mayo et al. 1980	Pittsburgh	1952–1974	91
Section 236			
Mayo et al. 1980	Phoenix	1969–1975	35
Mayo et al. 1980	Pittsburgh	1969–1975	75
Section 8 New Construction/ Substantial Rehabilitation			
Wallace et al. 1981	National	1979	44–78

<sup>2</sup> This study made two predictions of the market rents of subsidized units based on different data sets containing information on the rent and characteristics of unsubsidized units. The study did not collect information on the indirect subsidies of the Section 8

The recently completed U.S. General Accounting Office (GAO) study produced similar results for the major active construction programs—Low-Income Housing Tax Credit (LIHTC), HOPE VI, Section 202, Section 515, and Section 811 (2001). Table 2 reports results based on the conceptually preferable life cycle approach.<sup>3</sup> The excess total cost estimates range from at least 12 percent for Section 811 to at least 27 percent for HOPE VI. These estimates are lower bounds on the excessive cost because some costs of the production programs were omitted. Most notably, the opportunity cost of the land and the cost of preparing the site are omitted from the cost of HOPE VI redevelopment projects. These are real costs to society. More generally, some costs of each production program were omitted. For example, some projects under each program receive local property tax abatements. The results ignore this cost to local taxpayers.

*Table 2. Excess Cost of Active Production Programs*

Program	Excess Cost (%)
LIHTC	16
Hope VI	27
Section 202	19
Section 515	25
Section 811	12

*Source:* GAO 2001, life-cycle approach.

The GAO study will not be the last word on the cost-effectiveness of the programs studied. Improvements in its implementation of the life-cycle methodology are possible and desirable. However, it provides the only independent cost-effectiveness analysis of these programs.

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New Construction Program. These indirect subsidies include Government National Mortgage Association Tandem Plan interest subsidies for Federal Housing Administration-insured projects and the forgone tax revenue due to the tax-exempt status of interest on the bonds used to finance state housing finance agency projects. On the basis of previous studies, the authors argue that these indirect costs would add 20 to 30 percent to the total cost of the Section 8 New Construction Program. The range of estimates reported in the text is based on the four combinations of the two predictions of market rent and the lower and upper limits on the indirect subsidies.

<sup>3</sup> The GAO study also reports the first-year excess costs of production programs. The first-year cost of a production program is the sum of the annualized development subsidies and the tenant rent and other government subsidies during the first year of operation. The GAO estimates of the excess cost of production programs based on this method are much higher than estimates based on the life-cycle approach. Olsen (2000) explains the shortcomings of first-year-cost methodology.

The preceding evidence combined with other evidence on the effects of alternative methods of delivering housing assistance makes a strong case for total reliance on choice-based assistance.<sup>4</sup> If we compare choice-based and project-based assistance programs that serve recipients equally well (that is, provide them with equally good housing for the same rent), the project-based programs will serve many fewer families with a given budget. Therefore, many eligible families and the taxpayers who want to help them will lose if project-based assistance replaces choice-based assistance.

Evidence clearly indicates that states would devote the bulk of an unrestricted housing block grant to project-based assistance. The HOME Investment Partnerships Program is a block grant to states and localities that permits either project-based or choice-based assistance. Contrary to the implications of the systematic evidence on the effects of different types of housing programs, states and localities have chosen to spend the bulk of their funds on project-based assistance. In 1995, states allocated 94 percent of their rental assistance to specific projects (Urban Institute 1999). Left to their own devices, it is reasonable to expect that states will do the same with the proposed block grant. Being close to the people does not provide any insight into the design of efficient housing programs. Therefore, it is essential that any conversion of the Housing Choice Voucher Program to a block grant should contain an explicit prohibition on the use of block grant funds for project-based assistance.

## **Encourage movement toward an entitlement program for the poorest families**

### *Background*

Unlike other major means-tested transfer programs, housing assistance is not an entitlement, despite its stated goal. Millions of the poorest families are not offered any housing assistance, while a smaller number of equally poor families receive large subsidies. For example, an assisted family with one child and an adjusted annual income of \$8,000 living in an area with an average fair market rent (FMR) would have received an annual housing subsidy of \$6,000 from the Housing Choice Voucher Program in 2002 if it occupied an apartment renting for the FMR. The majority of families who have the same characteristics and live in that

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<sup>4</sup> See Olsen (2003) for a summary of the evidence on a wide range of effects of housing programs. Section V analyzes the two major objections to exclusive reliance on tenant-based housing assistance.

locality would receive no subsidy from any low-income housing program. Furthermore, most of the poorest eligible families are offered no assistance, while many families with considerably greater incomes are helped. About 34 percent of the families who receive tenant-based vouchers and certificates are above the poverty line, while 70 percent of the families below the poverty line do not receive housing assistance from any HUD program.

The nonentitlement nature of housing assistance is a historical accident. Because the first significant housing program for low-income households involved the construction of housing, it was not possible to make it an entitlement for any significant number of families. Building millions of public housing units over a short time was not feasible. Income limits for eligibility were not designed to be consistent with the amount of money that Congress wanted to devote to housing assistance. Now that vouchers are used to provide such assistance, the impossibility of building enough units to serve an enormous number of families provides no justification for maintaining a nonentitlement program. Almost all families eligible for housing assistance already live in housing. Most of these units already meet housing standards. Other vacant units meeting housing standards are available, and many can be inexpensively upgraded to meet these standards. Little new construction is needed to provide adequate housing for all of the poorest families that would want to participate in an entitlement housing program that could be funded with the current budget for housing assistance.

In recent times, no one has attempted to explain why we should offer assistance to some, but not other, families with the same characteristics, and no one has provided a persuasive argument for denying assistance to the poorest families while providing it to otherwise identical families in the same locality whose income is two, three, or four times as large. It is often argued that we should not limit assistance to the poorest families because having a mix of incomes in subsidized housing projects is desirable. Obviously, this argument is not applicable to tenant-based assistance. Furthermore, the conflict between the desire to serve the poorest families and to avoid concentrating them in projects in other programs can be avoided by vouchering out these programs.

### *Taxpayer preferences*

It is difficult to reconcile these features of the Housing Choice Voucher Program and all other low-income housing programs with plausible taxpayer preferences. In determining whether housing assistance

should be an entitlement, it is helpful to think about how a nonrecipient who pays taxes to support housing programs feels about dividing a fixed amount of assistance between two seemingly identical families.

At one extreme, we could give one of the families the entire amount available. At the other extreme, we could divide it equally. The former is inconsistent, while the latter is consistent, with plausible assumptions about taxpayer preferences. To say that two potential recipients are the same in the taxpayer's eyes is to say that the taxpayer is willing to sacrifice the same amount for the same change in the consumption pattern of either family.

It is also reasonable to conclude that taxpayers place the highest value on helping the poorest families. Why else would almost all means-tested housing programs provide the largest subsidy to families with the smallest income?

### *Effect on homelessness*

Another strong argument for an entitlement housing assistance program for the poorest individuals and families is its effect on homelessness. The homeless are the poorest of the poor. Research indicates that an entitlement program of housing assistance for the poorest individuals and families would eliminate homelessness except for the chronically homeless with serious mental illness and/or substance abuse (Early and Olsen 2002).<sup>5</sup>

### *Common critiques*

The preceding argues strongly that a program of housing assistance should be an entitlement for the poorest families. The usual argument against making housing assistance an entitlement is that it would be too expensive. Those who make this argument seem to envisage using the current mix of housing programs and the current rules for the tenant's contribution to rent to deliver housing assistance to all currently

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<sup>5</sup> The chronically homeless require a more comprehensive approach. Existing supportive housing facilities will certainly be part of the solution to dealing with these people. Because of the time needed to determine eligibility, an entitlement housing assistance program for the poorest households will not eliminate the desirability of short-term facilities to house people who would otherwise live on the streets. Although we might want to fund them in a different manner, existing shelters would surely be among the short-term facilities used.

eligible families. This would indeed increase the amount spent on housing assistance greatly, although the magnitude has not been estimated. However, we do not have to make more than 40 percent of the population eligible for low-income housing assistance; we can reduce the fraction of housing assistance delivered through cost-ineffective programs, and we can reduce subsidies at every income level.<sup>6</sup> If we reduce the fraction of the population eligible for housing assistance, increase the fraction of families served by choice-based assistance, and reduce the subsidy at each income level under each housing program, the cost of an entitlement housing assistance program would be less than commonly assumed.

Indeed, it is possible to develop an entitlement housing assistance program at any level of cost. For example, we could have an entitlement housing assistance program without spending any additional money by a simple change in the Housing Choice Voucher Program: namely, reducing the subsidy available to each eligible family by the same amount. At current subsidy levels, there are many more families willing and able to use vouchers than can be funded. As we reduce the subsidy at each income level by the same amount, the number of families wanting to participate will decline and waiting lists will shrink. If we reduce subsidies sufficiently and adjust the number of families served so as to spend the same amount on the program, all families wanting to participate on the terms offered will receive assistance. We will then have an entitlement housing assistance program for the poorest eligible families, thereby eliminating the horizontal inequities of the current program.

In housing policy discussions, a common objection to this proposal is that no one would be able to find housing meeting the program's standards with the lower subsidies. This objection is logically flawed. We start from a position where many more people want to participate than can be served with the existing budget. If we reduce subsidy levels slightly, it will still be the case that more people will want to participate than can be served. If we decrease the subsidy levels so much that no one wants to participate, we have decreased them more than the proposed amounts.

A more sophisticated argument against this sort of entitlement housing assistance plan is that the poorest households will be unable to participate. The simple proposal described earlier calls for reducing the guarantee under the voucher program (called the payment standard), the

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<sup>6</sup> See HUD 2000 (table A-1) for the fraction of households eligible for housing assistance.

subsidy received by a household with no income. If the payment standard is less than the rent required to occupy a unit meeting the program's minimum housing standards, then a household whose income and assistance from other sources are just sufficient to buy subsistence quantities of other goods would be unable to participate. Previous studies (Cutts and Olsen 2002; Olsen and Reeder 1983) have shown that the payment standard exceeds the market rent of units just meeting the program's minimum housing standards in all of the many metropolitan areas and bedroom sizes studied. Between 1975 and 1993, the median excess varied between 33 and 80 percent. Although refined estimates have not been made with more recent data, a rough estimate is that the median excess over all combinations of metropolitan area and number of bedrooms was 68 percent in 2001 (Cutts and Olsen 2002). So a considerable reduction in the payment standard could occur almost everywhere without precluding participation by the poorest of the poor. However, the preceding proposal might lead to a particularly low participation rate by these households, a possibility that could be counteracted by a smaller reduction in the payment standard combined with an increase in the fraction of adjusted income that tenants are expected to contribute to their rent. For a given program budget, this would yield a higher participation rate by the poorest of the poor and a lower participation rate by other eligible households.

Since reducing current subsidies at each income level enough to immediately implement an entitlement housing assistance program for the poorest families would excessively disrupt the lives of current recipients, a phase-in period is essential. Cutts and Olsen (2002) discuss how the transition to an entitlement housing program for the poorest families might be handled.

### **Create a state housing block grant to support the entitlement program**

To contribute to the movement toward an entitlement housing assistance program for the poorest families, a housing block grant should contain strict targeting requirements and incentives for serving the poorest families. The fraction of new admissions whose incomes are less than 30 percent of the local median should be increased beyond current levels, all additional new admissions should be limited to families whose incomes are less than 50 percent of the local median, and the HUD secretary should not be given discretion to waive these rules. Incentives should reward states that serve a greater fraction of families whose incomes are less than 30 percent of the local median, perhaps through higher performance ratings. Ultimately, these measures would

result in a much greater focus of subsidy resources on the poorest households, while minimizing the disruption to current recipients.

## Conclusion

The stated goal of the Housing Act of 1949 is “a decent home and suitable living environment for every American family.” It is time that we delivered on that commitment. Contrary to popular opinion, this does not require spending more money on housing assistance. It can be achieved without additional funds by shifting all funds from less cost-effective methods for delivering housing assistance to choice-based vouchers as soon as current contractual commitments permit and gradually reducing the large subsidies received by current voucher recipients. Replacing the Housing Choice Voucher Program with a block grant to states can contribute to this goal by precluding the use of block grant funds for project-based assistance, increasing the targeting of assistance to the poorest families, and including the fraction of recipients with extremely low incomes in the formula for determining the performance rating of state programs.

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