PRICE INCREASES CAUSED BY HOUSING ASSISTANCE PROGRAMS

C. PETER RYDELL,

JOHN E. MULFORD, LAWRENCE HELBERS

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HOUSING ASSISTANCE SUPPLY EXPERIMENT

Sponsored by

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PREFACE

This report is based on a briefing given to Donna E. Shalala, Assistant Secretary for Policy Development and Research, U.S. Department of Housing and Urban Development, on October 5, 1979. It draws on research conducted by The Rand Corporation as part of the Housing Assistance Supply Experiment, which is sponsored and funded by the Office of Policy Development and Research, U.S. Department of Housing and Urban Development, under Contract No. H-1789. The report is a product of research on the market effects of housing allowances under HUD Contract No. H-1789 and of basic research on housing market behavior under HUD Grant No. H-5099RG. The help of G. Thomas Kingsley, Ira S. Lowry, Charles E. Phelps, and W. Eugene Rizor in preparing the report is gratefully acknowledged. Jan Newman typed the various drafts; Karen J. Stewart was the production typist. Penny Post edited the report and supervised its production.

SUMMARY

A major criticism of federal subsidies to privately owned housing for low-income households is that the subsidy accrues to landlords through price increases, rather than to tenants through increased housing consumption or reduced rent burdens. Two contrasting methods of subsidizing existing housing are "housing allowances," which rely on the discipline of the market to control price increases, and "Section 8 assistance" provided by Section 8 of the Housing and Community Development Act of 1974, which uses institutional regulations to control price increases. Contrary to preprogram predictions, evidence from actual program operations shows that the market outperforms regulation. Housing allowances cause a 1.2 percent increase, while Section 8 assistance causes a 26 percent increase, in the price participants pay for housing services. The housing allowance program shows how the Section 8 program could be revised to prevent the price increases: by restructuring the subsidy formula so that tenants pay the marginal rent dollar; by paying the subsidy directly to tenants so they know they are paying the marginal rent dollar; and by removing the rent ceiling so it can no longer act as a rent target. Restructuring the subsidy formula is the key change, because it alone would probably prevent most price increases.

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I. INTRODUCTION

Federal assistance to low-income housing used to be targeted primarily toward subsidizing construction and substantial rehabilitation. In the last decade, however, its application has shifted toward greater support of privately owned existing rental housing.[1] The purpose of the revised strategy is to distribute available funds more equitably, providing standard housing to many eligible households instead of above-standard housing to only a few households.

The government first displayed expanded interest in existing housing when it authorized the Experimental Housing Allowance Program (EHAP) through the Housing and Urban Development Act of 1970. Four years later, Section 8 of the Housing and Community Development Act of 1974 created a national program of similar intent.

One major criticism of the new approach focused on the expectation that the subsidies would benefit landlords through increased rents, rather than tenants by way of better housing and lower rent burdens.[2] Fears of rent inflation led the U.S. Department of Housing and Urban Development to sponsor preprogram studies to predict results before the actual effects of either program were observed. HUD also sponsored the Housing Assistance Supply Experiment as a part of EHAP to monitor rents under a full-scale housing allowance program, and established a project to evaluate the Section 8 Existing Housing Assistance Program on a nationwide scale for the same purpose.

This report compares the price increases attributable to the housing allowance and Section 8 programs in 1976. Comparable data exist only for that year. However, the housing allowance program has not changed since then, and the Section 8 program has changed only in minor ways (noted in the text), so the report's conclusions are not limited to that year. The report finds that differences in the two programs' rules caused markedly different price increases. Further, its findings strongly contradict the predictions of preprogram analytical studies.

DIFFERENCES BETWEEN HOUSING ALLOWANCES AND SECTION 8 ASSISTANCE

The two current methods of subsidizing existing privately owned housing address the rent inflation problem in radically different ways. The housing allowance program, currently subsidizing over 9,000 households in two north central metropolitan areas,[3] depends upon the

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[1]In 1970 only 5 percent of subsidized rental units for low-income households were privately owned existing units not previously rehabilitated. By 1977 the percentage had risen to 25 percent. Of the 650,000 additional units subsidized between 1970 and 1977, 52 percent were privately owned existing housing. See *HUD Statistical Yearbook* (1971), Table 149; and (1977), Tables H85 and H125.

[2]Barnett and Lowry (1979) document the inflation concerns that housing policymakers and analysts expressed in the early 1970s, and review the assumptions underlying those concerns.

[3]Brown County, Wisconsin, containing the city of Green Bay, and St. Joseph County, Indiana, containing the city of South Bend, are served by the Housing Assistance Supply Experiment (HASE). Individuals in other cities were given housing allowances by the now completed Housing Allowance Demand Experiment (HADE) and Administrative Agency Experiment (AAE), although only the HASE counties received full-scale housing allowance programs. The three experiments together constitute the Experimental Housing Assistance Program (EHAP). Allowances began in 1974 for Brown County and in 1975 for St. Joseph County. They are funded by a ten-year annual contributions contract between HUD and the public housing authority in each location. The *Fourth Annual Report of the Housing Assistance Supply Experiment* (1978) reviews the Supply Experiment's purposes, scope, and preliminary conclusions. The count of 9,000 households was reached in February 1979.

discipline of the market to prevent price increases. The Section 8 Existing Housing Assistance Program, currently subsidizing over 520,000 renter households nationwide,[4] depends on institutional regulation to combat price increases. This report compares the effects of the housing allowance and Section 8 programs on prices of existing rental housing. The HASE housing allowance program also assists owner-occupied housing and other parts of the Section 8 program assist new construction and major rehabilitation. Zais, Goedert, and Trutko (1979, pp. 55-58) exhaustively compare the two programs. Table 1 outlines the specific differences relevant to this discussion.

Table 1

COMPARISON OF THE HOUSING ALLOWANCE AND SECTION 8 PROGRAMS

Item	Housing Allowance Program	Section 8 Existing Housing Assistance Program
Subsidy	$S - .25Y$	$R - .25Y + (S - R)\ (.25Y/S)$
Payment	To tenant	To landlord
Maximum rent	No maximum	S

SOURCE: James P. Zais, Jeanne E. Goedert, and John W. Trutko, *Modifying Section 8: Implications from Experiments with Housing Allowances*, The Urban Institute, Washington, D.C., UI-240-10, January 1979, pp. 55-58.

NOTE: R = total actual rent, Y = adjusted gross household income, S = standard cost of adequate housing (denoted by R^* or C^* in the housing allowance program and by *FMR*, for "Fair Market Rent," in the Section 8 program).

In the housing allowance program, recipients get the difference between the standard cost of adequate housing[5] and one-fourth of their adjusted income. The housing allowance office pays the subsidy to the tenant, and the tenant pays the full rent to the landlord. Recipients can live in any unit that meets program standards.

In the Section 8 Existing Housing Assistance Program, recipients get the difference between the actual rent of their unit and one-fourth[6] of their adjusted income, plus a "Rent

[4]The Section 8 Existing Housing Assistance Program began in 1974 and is still expanding. The count of 520,000 units was reached in February 1979 (*Housing and Community Development Reporter*, 30 April 1979, p. 1094).

[5]"Adequate housing" is a dwelling that passes periodic evaluations by the housing allowance office to determine spaciousness, presence of essential facilities in good working order, and absence of hazards to health or safety. The specific standards were adapted from American Public Health Association standards and Building Officials and Code Administrators' model codes. "Standard costs" are estimates of the typical full market price of rental dwellings that meet the standards. The estimates are based on periodic surveys of local housing markets.

[6]For certain families (those very large in size or with very low incomes or exceptional medical expenses) the household contributed 15 percent instead of 25 percent (Zais, Goedert, and Trutko, 1979, p. 58). In October 1980 the minimum household contribution was raised from 15 to 20 percent (*Federal Register*, 1980, pp. 59309-59310).

Reduction Credit" if the actual rent is less than an administratively set rent ceiling called "Fair Market Rent" (see Table 1). The local public housing authority administering the Section 8 program pays the subsidy directly to the landlord and the tenant pays the landlord only the unsubsidized portion of rent. Recipients must live in a unit that not only meets program standards but whose rent is also no greater than the Fair Market Rent ceiling.[7]

In the housing allowance program, the rent does not affect the subsidy that the tenant receives.[8] If rent goes up a dollar, the subsidy remains unchanged. In other words, tenants pay the marginal rent dollar. Consequently, the usual market process of tenants bargaining with landlords determines rents.

In contrast, in the Section 8 program rent always affects the subsidy. If rent goes up a dollar, the subsidy increases by up to a dollar. Tenants pay only part of the marginal rent dollar; the public housing authority pays the rest.[9]

Consequently, the usual market process of tenants bargaining with landlords does not determine rents in the Section 8 program. Rather, institutional regulation of the negotiation between tenants and landlords determines rents. The process has three steps:[10] First, a tenant who has been certified to receive assistance has 60 days to find an acceptable unit. Second, the tenant and landlord submit the rent they have negotiated, together with a description of the unit, to the public housing authority for approval. Finally, the public housing authority must find the proposed rent "reasonable"[11] before it executes a Housing Assistance Payment (HAP) contract with the landlord for the subsidy it will pay on the unit.

The rent standards adopted by the two programs (HASE standard cost and Section 8 Fair Market Rent) have similar definitions. Both are "typical" costs of housing that meets the minimum requirements set by the assistance programs. Table 2 compares the two sets of rent standards (in the Brown and St. Joseph counties' housing markets in 1976) and shows that they are approximately the same.

However, the two programs use the rent standards very differently, and that use is the key to the different price impacts of the programs. The housing allowance program uses the standard cost of adequate housing to establish subsidy levels. Only indirectly, via increased housing consumption, does the standard cost affect program rents. In contrast, the Section 8 program uses the Fair Market Rent to establish permitted rent levels. Only indirectly, via the influence on housing prices, does the Fair Market Rent affect subsidy levels.

PREPROGRAM PREDICTIONS OF PRICE IMPACTS

The most comparable and carefully documented of the preprogram studies were carried out by The Urban Institute. For housing allowances, they concluded: "In seven of the eight cases

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[7]In special cases units renting for 10 percent more than the Fair Market Rent may join the Section 8 program. See Drury, Lee, Springer, and Yap (1978), p. 29.

[8]Occasionally rent does affect the amount of the subsidy in the housing allowance program via a program rule requiring that the subsidy not exceed the rent. Less than 4 percent of the housing allowance program recipients are affected by this restriction.

[9]However, most tenants did not understand the Rent Reduction Credit. They believed that the public housing authority pays all of the marginal rent dollar. In October 1980, HUD eliminated the Rent Reduction Credit because a nationwide survey showed that no more than 14 percent of the tenants understood it (*Federal Register,* 1980, pp. 59308-59309). The public housing authority now pays the entire marginal rent dollar.

[10]Greenston, James, Yap, and Sadacca (1977), p. 8.

[11]The public housing authority must certify on a case-by-case basis that the rent being approved is reasonable in relation to comparable units in the private market and not in excess of rents being charged by the owner for similar units on the same property (*Public Housing Agency Administrative Practices Handbook for the Section 8 Existing Housing Program,* 1979, p. 6-9).

Table 2

RENT STANDARDS IN HOUSING ASSISTANCE PROGRAMS, 1976

Size of Unit (bedrooms)	Monthly Amount ($) per Housing Unit	
	Housing Allowance Program	Section 8 Existing Housing Program
Brown County, Wisconsin		
0	125	114
1	145	131
2	175	155
3	195	180
4	210	196
St. Joseph County, Indiana		
0	115	130
1	140	149
2	160	177
3	175	205
4	185	225

SOURCE: *Fifth Annual Report of the Housing Assistance Supply Experiment*, The Rand Corporation, R-2434-HUD, June 1979, p. 22; and *Federal Register*, Vol. 41, No. 1, 29 March 1976, p. 13042.

NOTE: In descriptions of the housing allowance program the rent standard is denoted by R^* or C^*, in descriptions of the Section 8 program it is denoted by FMR (for "Fair Market Rent"). The Section 8 program's rent standard also varies by the presence or absence of elevators, but since there are few elevator buildings in these housing markets, only the rent standards for non-elevator buildings are given in the table.

(simulations) . . . housing prices for recipients of the housing allowance rise. They rise by more than 10 percent in five of the eight cases. . . . The three cases in which prices rise by less than 10 percent are elastic supply cases, and the supply parameters in these cases are more conducive to an allowance without inflationary impacts than any of our empirical results suggest. The results thus do confirm the fear that a large-scale allowance program carries the danger of upward pressure on prices . . ." (de Leeuw and Struyk, 1975, p. 131).

For Section 8 assistance, they concluded that ". . . even a large-scale Section 8 program will, in general, cause only small market disruptions" (Struyk, Marshall, and Ozanne, 1978, p. 90). Only two out of their fifteen simulations of the Section 8 Existing Housing Assistance Program predicted price increases over 10 percent; and the average price increase forecast for recipients across all simulations was only 3.4 percent.[12]

However, we are no longer dependent on preprogram predictions. Actual operation of the programs now provides a clear-cut comparison of the discipline of the market vs. institutional regulation.

[12]Struyk, Marshall, and Ozanne (1978), p. 136. The predicted price effects are the ratio of the price indexes of estimated participant rents in the Section 8 Existing Housing Program to their rents before the program.

II. MARKET VS. REGULATION

The market wins handsomely over regulation in this instance: Housing allowances cause a short-run price inflation of no more than 1.2 percent, while Section 8 assistance causes 26 percent. Both numbers are average rent increases experienced upon joining the program by recipients who had not moved and whose dwellings did not require repairs to meet program standards. The first number comes from the Housing Assistance Supply Experiment, the second number comes from the nationwide evaluation of the Section 8 Existing Housing Assistance Program (see Table 3).

The "no-move, no repair" situation provides the sharpest possible evidence of price increases because the quantity of housing remains constant. The tenant does not move, but simply joins the program. The housing unit does not change because no repairs are needed to meet program standards. The entire rent increase is a price increase.

Table 3

AVERAGE PERCENTAGE RENT INCREASES UPON JOINING A HOUSING ASSISTANCE PROGRAM

Situation	Housing Allowance Program			Section 8 Existing Housing Assistance Program
	Brown County	St. Joseph County	Average	
No move, no repair	1.6	.7	1.2	26
No move, repair	2.5	1.7	2.1	32
Move	34.0	45.0	40.0	71

SOURCE: Housing Allowance Program records for Brown and St. Joseph counties; Margaret Drury, Olsen Lee, Michael Springer, and Lorene Yap, *Lower Income Housing Assistance Program (Section 8): National Evaluation of the Existing Housing Program*, Office of Policy Development and Research, U.S. Department of Housing and Urban Development, Washington, D.C., November 1978, p. 66; and Lorene Yap, Peter Greenston, and Robert Sadacca, *Lower Income Housing Assistance Program (Section 8): National Evaluation of the Existing Housing Program--Technical Supplement*, Office of Policy Development and Research, U.S. Department of Housing and Urban Development, Washington, D.C., November 1978, p. 87.

NOTE: The table reports the percentage change from average pre-program gross rent (contract rent plus direct tenant payments for utilities) to average program gross rent. "No move" households did not change units when joining the program, and "no repair" units did not require repairs to meet program standards.

The other two situations in Table 3 provide less direct evidence because the quantity of housing does not remain constant. Housing consumption increases when households repair their units to meet the program's health and safety standards and it increases when they change units to meet the program's space standards. The rise in consumption accounts for some, possibly all, of the rent increase, obscuring any increase due to price alone. However, if we assume that the consumption increases are approximately the same in both programs, then we can determine the differential price increase caused by the programs. Note that the Section 8 rent increase exceeds the housing allowance rent increase by 29.9 percent in the repair situation and 31.0 percent in the move situation. Those differences are roughly of the same magnitude as the 24.8 percent gap in the no-repair situation, suggesting that the differential price increase caused by the Section 8 program is similar in all three situations.

DOES SECTION 8 CAUSE PRICE INCREASES?

The evidence in Table 3 establishes that substantial price increases occurred in the Section 8 program. However, that does not necessarily mean that the program caused the price increases.

Olsen and Reeder (1980) suggest that the differential price inflation under the program is caused by market forces removing price discounts, rather than the Section 8 program itself. Their argument has four steps: (a) At any given time in a housing market some units are underpriced and others are overpriced relative to the marketwide average. (b) The rent ceiling provision leads to a larger proportion of underpriced units joining the Section 8 program than the housing allowance program. (c) As new leases are signed (a requirement for joining either program) the rent of underpriced units goes up more than overpriced units. (d) Consequently, the Section 8 program has larger average price increases than the housing allowance program.

If the removal of price discounts were a major cause of the observed price increases, controlling for preprogram rent levels would show the percentage increases as similar. However, the increases categorized by level of preprogram rent are dramatically different.

Section 8's rent ceiling screens the units admitted to the program by allowing only those units whose preprogram rents are less than that amount to join. Consequently the preprogram rent of those units tends to be lower on average than those of units in the housing allowance program. For example, of the households receiving assistance who neither moved nor repaired, over 14 percent in the Section 8 program but less than 1 percent in the housing allowance program occupied units whose preprogram rents were below $50 per month (see Table 4).

Some of the low preprogram rents in both programs were due to price discounts (provided, for example, as private charity to relatives or elderly households).[1] In those cases, landlords might have raised rents to the market level when housing assistance became available to the tenants. However, most low rents presumably reflect the housing unit's quality relative to the rest of the market rather than landlord benevolence.

Whatever the reason for some very low preprogram rents, they were affected differently by the housing allowance and Section 8 programs. Table 5 shows that preprogram rents below $50 per month rose by an average of 11 percent under the allowance program and 267 percent

[1]About 9 percent of renters in the housing allowance program reported that they paid less than "full rent" before joining the program. Comparable information is not available for recipients of Section 8 assistance, but the screening argument suggests the Section 8 percentage is higher. By "price discounts" we mean both voluntary underpricing (landlords giving low rent to favored tenants) and involuntary underpricing (landlords setting rent below that of comparable units due to market imperfections).

Table 4

PERCENTAGE DISTRIBUTION BY PREPROGRAM RENT: NO-MOVE, NO-REPAIR UNITS

Preprogram Rent ($/Unit/Mo)	Housing Allowance Program			Section 8 Existing Housing Assistance Program
	Brown County	St. Joseph County	Average	
5-50	.9	.4	.7	14.4
51-150	35.9	50.7	43.3	43.1
More than 150	63.2	48.9	56.0	42.5
All rents	100.0	100.0	100.0	100.0

SOURCE: Housing Allowance Program records for Brown and St. Joseph counties; distribution calculated from information published in Margaret Drury, Olsen Lee, Michael Springer, and Lorene Yap, *Lower Income Housing Assistance Program (Section 8): National Evaluation of the Existing Housing Program*, Office of Policy Development and Research, U.S. Department of Housing and Urban Development, Washington, D.C., November 1978, p. 66; see Appendix B of this report.

under the Section 8 program. For preprogram rents between $51 and $150, the corresponding increases were 3 and 33 percent. Only preprogram rents which exceeded $150 received small increases in both programs.

Even if the housing allowance program had the same distribution of units by preprogram rents as the Section 8 program, the average rent increase under HASE would have been only 0.9 percent more than it was. Weighting the housing allowance program's rent increases according to that program's distribution of units shows an average rent increase of 1.2 percent (see Table 3). Weighting the same rent increases by the Section 8 program's distribution of units[2] yields an average increase of 2.1 percent. Consequently only 0.9 percent of the 24.8 percentage point gap between the price increases under the two programs can be attributed to the different mixtures of units the programs serve.

Only a very small part of the differential price increase under Section 8 is explained by market forces; the bulk of the increase must therefore be due to nonmarket forces—that is, to the program's regulations.

[2]It is also necessary, of course, to weight by the average preprogram rent in each preprogram rent category. The overall average rent increase equals

$$\sum_i n_i r_i f_i / \sum_i r_i f_i$$

where n_i is the average rent increase in category i, r_i is the average preprogram rent in category i, and f_i is the fraction of units in category i. The average preprogram rents in the three program rent categories for no-move, no-repair units in the housing allowance program were 43, 120, and 193 (see Tables B.1 and B.2 in Appendix B).

Table 5

AVERAGE PERCENTAGE RENT INCREASES BY PREPROGRAM RENT: NO-MOVE, NO-REPAIR UNITS

Preprogram Rent ($/Unit/Mo)	Housing Allowance Program			Section 8 Existing Housing Assistance Program
	Brown County	St. Joseph County	Average	
5-50	9.6	11.9	10.8	267
51-150	3.4	1.5	2.5	33
More than 150	1.0	.1	.6	4
All rents	1.6	.7	1.2	26

SOURCE: Housing Allowance Program records for Brown and St. Joseph counties; and Margaret Drury, Olsen Lee, Michael Springer, and Lorene Yap, *Lower Income Housing Assistance Program (Section 8): National Evaluation of the Existing Housing Program*, Office of Policy Development and Research, U.S. Department of Housing and Urban Development, Washington, D.C., November 1978, p. 66.

ARE THE SECTION 8 PRICE INCREASES UNDESIRABLE?

Before either the housing allowance or the Section 8 programs had begun, there was wide agreement that program-induced price increases, if they occurred, would be extremely undesirable. The reason is that price increases divert subsidy dollars from their intended recipients—households with certified low incomes—to landlords. Moreover, the percentage of the subsidy that goes to the landlord is larger than the percentage increase in rent. For example, the average preprogram rent of Section 8 units is about $135, while the average subsidy per unit is $103. A 26 percent price increase means a rent increase of $35, which is 34 percent of the subsidy. The one-fourth price increase causes one-third of the subsidy to be diverted to landlords.

Nevertheless, after program experience showed that the Section 8 program caused a 26 percent price increase, some commentators offered reasons why the price increase might not be bad, after all. Drury et al. (1978, p. 65) suggest that additional services might be provided in the future in return for the price increases: "Though the initial upgrading of the low-income housing stock appears to be modest, future maintenance levels may be higher as a result of increased rents coupled with the change in the tenant-landlord relationship instilled by the program, and the oversight of the local PHA." Olsen and Rasmussen (1979, pp. 18-19) suggest that in spite of the price increases, "... the initial evidence suggests that Section 8 rents are reasonable for the quality of housing received ... there is little reason to expect Section 8 Existing units to rent for much more than comparable unsubsidized units." The argument, as elaborated by Olsen and Reeder (1980), is that the preprogram prices of units entering the Section 8 program may have been sufficiently below the marketwide average for program prices to be reasonable even after the 26 percent price increase.

However, neither of these arguments justifies the Section 8 rent increases. The Drury argument does not justify them because improved maintenance levels in the future, when and if they occur, only justify future price increases, not those of the present or past. The Olsen argument does not justify the increases because, however reasonable Section 8 rents are, they would have been more reasonable if the price increases had not occurred. A price increase is a price increase whether it starts from a low or a high level, and any price increase causes subsidy diversion.

WHY SECTION 8 CAUSES PRICE INCREASES

The Section 8 program causes price increases because it removes the tenants' incentive to bargain with landlords for market rents. Section 8 tenants know that they will pay no more than one-fourth of their income to the landlord, no matter how high the rent. They also know that the higher the rent, the greater the chance that the landlord will agree to join the Section 8 program. Consequently, the tenant-landlord interaction provides little restraint on Section 8 rent increases.[3]

The Section 8 program attempted to preserve the tenants' incentive to bargain for market rents by offering them a "Rent Reduction Credit." The credit reduced the tenant's rent payment by a fraction of the difference between actual gross rent and the official Fair Market Rent figure (see Appendix A).

However, the Rent Reduction Credit failed to restrain rent increases for three reasons. First, it was not adequately explained to tenants; although 46 percent of participating families received credits, only 14 percent understood the credit system (*Housing and Community Development Reporter,* 20 August 1979, p. 260). Second, it gave tenants too small a share of the rent saving (an average of only 40 percent) to motivate hard bargaining. Third, it gave the smallest shares of the rent saving to tenants with the lowest incomes, whose increases were therefore likely to be largest.[4] The nationwide evaluation of the Section 8 program concluded: "The Rent Reduction Credit has not functioned as planned. Very few certificate holders . . . made a specific effort to lower rents, and participants' understanding of it . . . was found to be very limited . . ." (Drury et al., 1978, p. 39).

With tenants indifferent to the rent charged, landlords are free to seek the maximum rent allowed by the local public housing authority. Moreover, the landlord knows the exact maximum rent allowed for a particular dwelling because the Fair Market Rent schedules are publicly available.[5]

Comparing the preprogram rents that rose by large amounts with the Fair Market Rent levels reported in Table 2 reveals that the larger the gap between preprogram rent and Fair Market Rent, the larger the Section 8 rent increases. Apparently, the Fair Market Rent acts as a rent ceiling only for landlords deciding what units they want subsidized by the Section

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[3]The theoretical objection that an economically rational Section 8 household would simply move to a housing unit worth the Fair Market Rent overlooks the high cost of searching for any type of housing unit, let alone one that is exactly worth a given rent.

[4]See Appendix A for a detailed discussion of the three reasons.

[5]The Fair Market Rent for the unit size that fits a family's space requirements is written on the Certificate of Family Participation that tenants carry to prove they are eligible for Section 8 assistance (see Appendix A). Tenants almost certainly show that certificate to prospective landlords, but should they not do so the Fair Market Rent schedule is available from the housing authority and is also published in the *Federal Register*.

8 program. For units that are approved for the program, the Fair Market Rent becomes a target, rather than a ceiling.[6]

Nevertheless, the Section 8 program's encouragement of landlords to treat the rent ceiling as a target figure does not necessarily explain the program's rent increases. If the ceiling is truly a "fair market" price, why should preprogram rents differ from it? One explanation is that administrative formulas can state market rents correctly on average, but do not necessarily do so in specific cases.

The Section 8 program's Fair Market Rent for a given year and geographic area depends only on the number of bedrooms in a housing unit and whether it is in an elevator building. The Fair Market Rent does not depend upon the unit's quality (except that it must pass the program's minimum standards to be approved for the program). Landlords with high quality units whose rents exceed Fair Market Rent do not join the Section 8 program, because they can do better in the open market. However, landlords whose units are in poor enough condition for their market rents to be below Fair Market Rent (though good enough to meet minimum standards) will readily join the program because they can then raise those rents. The nationwide evaluation showed that 63.8 percent of program rents exceeded 90 percent of Fair Market Rent. Moreover, the reason given by 37.4 percent of landlords for their rent increases was "meeting the Fair Market Rent" (Yap, Greenston, and Sadacca, 1978, pp. 93 and 105).

The designers of the Section 8 program foresaw the possibility that the Fair Market Rent might become a rent target rather than a ceiling. To counter it, they required local public housing authorities to check for "rent reasonableness" as well as whether the rent was below the program's rent ceiling. However, in practice, the public housing authorities had great difficulties in defining and enforcing the rent reasonableness criterion.[7] In fact, they did not even always find it possible to require the clear-cut Fair Market Rent ceiling: 16.2 percent of program rents exceeded the ceiling (Yap et al., 1978, p. 105).

In a 1979 audit, HUD's Office of Inspector General found that at "21 percent of the projects reviewed, the PHAs did not make rent reasonableness determinations prior to approving the project rents . . . at 18 percent of the projects reviewed, PHAs allowed project rents to exceed the published Fair Market Rent limitations . . . at 6 percent of the projects reviewed, PHAs automatically increased rents *without* owner requests for rent increases . . . [and] at 4 percent of the projects reviewed, PHAs allowed owners to charge more rent for subsidized units than for similar unsubsidized units" (*Report on Special Operational Survey, Section 8,* 1979, p. 20). The nationwide review of the Section 8 program concluded: "It is highly unlikely that the rent reasonableness test has had a large effect on the units subsidized" (Drury et al., 1978, p. 38). Subsequent to the nationwide evaluation, a notice from HUD instructed local public housing authorities to exercise more care in determining rent reasonableness. Specifically, rent increases of over 10 percent must now be "fully documented" (*Housing and Community Development Reporter,* 9 February 1979, p. 897). There is as yet no evidence on how much the documentation requirement stiffens the rent reasonableness constraint on rent increases.

In short, implicit bargaining between the landlord and the local public housing authority establishes rents in the Section 8 program, and the landlord comes out ahead in that bargaining process. The only restriction on rent increases is the Fair Market Rent ceiling, but that constraint actually turns out to cause price increases by acting as a rent target for landlords

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[6]Appendix A shows how HUD regulations signal the landlord that rent increases up to the Fair Market Rent ceiling are acceptable. Appendix C shows that the tendency of landlords to raise prices toward the FMR ceiling remained consistent from 1976 to 1979.

[7]Under Section 8, the public housing authorities apply to HUD for a specific number of housing units by type (Greenston et al., 1977, p. 40). This procedure provides no incentive for them to strictly enforce the rent reasonableness criterion because economizing provides no additional units.

who join the program. Landlords whose preprogram rents exceed the ceiling tend not to join the program, and landlords whose preprogram rents are less than the ceiling tend to join the program and raise their rents toward the maximum allowed.

WHY HOUSING ALLOWANCES DO NOT CAUSE PRICE INCREASES

The housing allowance program does not cause price increases because, unlike the Section 8 program, it preserves the tenants' incentive to bargain with landlords for market rents. The subsidy tenants receive depends on the standard cost of adequate housing rather than on the actual rent of the residence they occupy. Therefore, tenants pay the marginal rent dollar out of their own pockets and negotiate rent with their landlords just as they would without a subsidy.

However, even though design of the housing allowance program insures that recipients will pay market rents, critics of the program feared that the program would drive market rents up. They argued that the program would greatly increase the demand for standard housing services and that the supply of those services is inelastic. Consequently, rents would have to rise to equilibrate supply and demand, at least in the short run.

That fear has been proven groundless by the Housing Assistance Supply Experiment: No measurable increases in the price of housing services occurred.[8] Additional demand induced by the program is not as great and the supply of housing services is not as inelastic as the critics of housing allowances feared.

The demand shift caused by the program was not as great as many anticipated for two reasons. First, at any given time no more than half of the eligible households are in the allowance program; the dynamics of poverty create much movement in and out of program eligibility, and newly eligible households join the program at a slow pace.[9] Second, the income elasticity of housing demand is considerably less than 1.0, indicating a very modest added demand from the households that are in the program.[10]

Of course, the program's requirement that recipients live in standard housing does cause a significant increase in demand for that type of housing. However, the supply of standard housing services turns out to be very elastic, even in the short run. Much substandard housing can readily be upgraded to standard condition,[11] and the vacancy rate for standard housing services can decrease.[12] Those supply responses absorb additional demand for standard housing services, and prevent the housing allowance program from causing serious short-run price increases.

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[8]See Barnett and Lowry (1979) for the evidence that the housing allowance program caused no significant price increases in either the tight (4 percent rental vacancy rate) Brown County housing market or the loose (9 percent rental vacancy rate) St. Joseph County housing market.

[9]Rydell, Mulford, and Kozimor (1979) show that the participation rate (fraction of eligibles that are in the allowance program) has risen gradually with time since the program began, reaching 40 percent at three years and 50 percent at equilibrium.

[10]Mulford (1979) estimates that the income elasticity of demand for rental housing is 0.2, which means that a 10 percent increase in household income results in a mere 2 percent increase in housing consumption.

[11]McDowell (1979, pp. 18-21) reports that three-quarters of renters who lived in substandard housing before joining the housing allowance program repaired their housing to standard condition (or persuaded their landlord to repair it) rather than move to find standard housing.

[12]The overall vacancy rate for housing services can decrease in either of two ways: First, existing households can move from small housing units into larger ones, and second, existing households can subdivide so that each new one consumes more housing services per capita. The vacancy rate for standard housing services also decreases when existing households move from substandard units to standard units.

Surveys of the two HASE counties provide dramatic evidence of the vacancy rate's[13] ability to absorb demand shocks and prevent short-run variation in the price of housing services. Table 6 compares market conditions, rents, and property values in the experimental sites before the allowance program began.[14] Because of rapid population growth, the 1973 vacancy loss rate was low in Brown County's rental market—about 4 percent. St. Joseph County has a segregated rental market; most of the county's black population lives in central South Bend.[15] The 1974 rental vacancy loss rate in central South Bend was 13 percent, compared to 6 percent in the rest of the county. The high rates resulted from declining job opportunities followed by population losses—especially from central South Bend—during the sixties and early seventies.

Table 6

EFFECT OF DEMAND SHIFTS ON RENT AND CAPITAL VALUE

Location	Vacancy Loss Rate (%)	Rent ($/Unit/Yr)	Capital Value ($/Unit)
Central South Bend	13.2	1,727	6,862
Rest of St. Joseph County	6.1	1,732	9,315
Brown County	4.2	1,764	12,316

SOURCE: Housing Assistance Supply Experiment, rental housing in Brown County, Wisconsin, 1973, and St. Joseph County, Indiana, 1974. See C. Peter Rydell, *Shortrun Response of Housing Markets to Demand Shifts*, The Rand Corporation, R-2453-HUD, September 1979, p. 3.

NOTE: Rents and capital values have been adjusted to control for variation in building age and size, and the Brown County figures have been adjusted for price inflation during 1973-74.

The difference in vacancy loss rates between Brown County and central South Bend reflects about a 10 percent difference in demand, relative to the housing supply in each location. Rents differ by 2 percent, however, whereas the value of rental properties in St. Joseph County is 44 percent lower than in Brown County.

A theory of housing market behavior that explains the findings reported above (Rydell,

[13]"Vacancy rate" in this discussion is the fraction of housing services not used. It is measured operationally by the fraction of rent lost due to vacancies.

[14]The evidence was presented three years ago in Rydell (1977), and has since been sharpened by using the vacancy loss rate rather than the traditional vacancy rate to measure market condition (Rydell, 1979, pp. 2-4).

[15]Central South Bend includes all but the fringes of the city of South Bend. It has three-fourths of South Bend's rental units and one half of St. Joseph County's rental units.

1979) provides assurance that the minor price effects of the housing allowance program in Brown and St. Joseph counties would be replicated in other housing markets. Of course, the exact demand shift caused by such a program would depend on the proportion of low-income households in a given housing market. However, even doubling the demand shock caused in Brown and St. Joseph counties would result in very small price increases.

The salient points of the theory are that (a) landlords find it more profitable to accept vacancy losses than to cut prices enough to fill every unit, (b) therefore it is mostly changes in vacancy rates, rather than changes in rents, that bring supply and demand for rental housing into equilibrium, and (c) landlords do not escape the consequences of a demand shift because changes in vacancy losses are capitalized into changes in the value of rental properties. That is why, when market conditions change, rent changes little, relative to the change in capital value.

III. CONCLUSIONS

The experience gained from operating and studying the experimental housing allowance program and the national Section 8 Existing Housing Assistance Program provides an unambiguous answer to the two programs' effect on rent inflation. The discipline of the market held price increases to only 1.2 percent in the allowance program, while institutional regulation allowed prices to increase by 26 percent in the Section 8 program.

The housing allowance program prevents price increases by preserving tenants' incentive to bargain with landlords for market rents. Moreover, the Housing Assistance Supply Experiment has shown that the link between demand shifts and rent increases is weak enough so that even a full-scale allowance program does not drive up market rents.

The Section 8 Existing Housing Assistance Program causes price increases by removing the tenants' incentive to bargain, substituting regulations administered by the public housing authority. Those regulations take away the usual market link between tenant payments and rent, allowing price increases to occur. Moreover, the regulations establish a Fair Market Rent target which encourages landlords to raise their prices.

The crucial difference between the two programs is that housing allowance subsidy depends upon the standard cost of adequate housing while Section 8 subsidy depends upon the actual rent of recipients' housing. The first subsidy method makes the tenant pay the marginal rent dollar, so that the usual tenant-landlord bargaining process keeps rents at market levels. The second subsidy method makes the public housing authority pay the marginal rent dollar, and it turns out that the public housing authority does not bargain as hard with landlords as tenants do.

It is ironic that the housing allowance program has not been implemented nationally partly because of fears that it would cause price inflation; while the Section 8 program has been implemented nationally (and is being expanded) even though it does cause price inflation. From the perspective of this discussion, the two programs differ only in that housing allowances give subsidies exclusively to low-income tenants while Section 8 assistance gives a substantial portion of the subsidy to landlords.

These findings suggest two morals, one for analysis of housing policy and the other for housing policy itself. The first moral is that housing market theory does not always adequately support policy analysis. The preprogram simulation analyses were carefully constructed, state-of-the-art efforts, yet they concluded that housing allowances would cause substantial price increases and Section 8 assistance would not. Only when actual evidence on program operation became available from the housing allowance experiment and the national evaluation of Section 8 was it clear how the programs affect rent.

The other moral is that substituting regulation for market discipline, while it may sometimes be appropriate, does not always work well. The Section 8 program's regulations were designed to prevent price increases without having to trust the market. However, it turned out that not only was the market trustworthy, but the regulations were not.

This report should not be interpreted to mean that Section 8 is a bad housing program. A recent comprehensive evaluation of the program concluded: "Section 8 Existing is a fundamentally sound program. The program serves all the stated housing goals to a certain extent, but as with most new programs there exist opportunities to improve its performance" (Olsen and

Rasmussen, 1979, p. 27). We agree with that evaluation, and merely point out that one area where performance can be improved is in the prevention of price increases.

It may be feasible to improve the regulatory system so as to forestall the large price increases that now occur in the Section 8 program. For example, Khadduri (1979, pp. 49-50) suggests enforcing rent reasonableness tests more rigorously, by requiring documentation that justifies rent increases in terms of increased management or maintenance costs. She also recommends giving public housing authorities a positive incentive to prevent price increases by making rent savings (the difference between actual rents and Fair Market Rent) interchangeable with administrative costs. However, enlarging the regulatory system would surely entail more work for local housing authorities and HUD, and would therefore increase program costs. Moreover, there is no evidence that this approach would succeed in preventing the increases.

In contrast, the housing allowance program provides evidence that, without compromising program objectives, Section 8 rules could instead be revised to use market discipline as an administratively simple way to control unwarranted price increases. Comparison with the housing allowance program suggests that three changes would be sufficient: (a) *change the subsidy formula* to use the Fair Market Rent standard, rather than the actual rent of a recipient's unit, to compute the subsidy, (b) *pay the subsidy directly to the tenant* instead of to the landlord, and (c) *remove the rent ceiling,* allowing recipients to choose any unit that meets the program's housing standards (see Table 1 in the Introduction.) The first change would make the tenant pay the marginal rent dollar, restoring the usual tenant-landlord bargaining process. The second change would insure that tenants knew that they were paying the marginal rent dollar. The third change would remove the rent ceiling as a target toward which landlords are motivated to raise their prices.

The question remains whether all three changes are necessary to prevent price increases. That question cannot be answered with evidence from HASE because the housing allowance program differs from the Section 8 program in all three ways. Nevertheless, we suspect that the first change alone—simply altering the subsidy formula—would do the lion's share of the job. Tenants might well realize that they were paying the marginal rent dollar even if the subsidy were paid to the landlord by the public housing authority. Landlords would probably not be able to raise prices toward the Fair Market Rent target if tenants had to pay the marginal rent dollar.

Neither the second change (paying subsidy to the tenant) nor the third change (removing the rent ceiling) would help control price increases unless the first change was made, however. Changing the recipient of the subsidy payment without altering the subsidy formula would probably not affect price increases because tenant incentives would remain unchanged. Removing the rent ceiling without altering the subsidy formula would most likely make price increases larger because under the current subsidy formula the rent ceiling is the only control on price increases.

Hence, we judge that altering the subsidy formula is the key to preventing price increases in the Section 8 program. However, if the formula were modified, the other two changes could well be justified for reasons other than their effect on price increases. For example, paying subsidies directly to tenants would reduce administrative costs, and removing the rent ceiling would allow tenants to spend more of the subsidy on housing consumption. Those reasons and others are extensively discussed in Zais, Goedert, and Trutko (1979).

To sum up: Price increases caused by the current Section 8 program cause a diversion of

a substantial portion of the program's subsidy dollars to landlords.[1] The housing allowance program shows how the Section 8 program could be revised to prevent the price increases: Structure the subsidy so tenants pay the marginal rent dollar; pay the subsidy directly to tenants so they know they pay the marginal rent dollar; and remove the rent ceiling so it can no longer act as a rent target. Restructuring the subsidy formula is the key change, because it alone would probably prevent most price increases. Adding the other two changes would insure that price increases were prevented, but neither would be helpful on its own. Paying the subsidy directly to the tenant while keeping the current subsidy formula would probably leave price increases unchanged, because tenant incentives would not be changed. Removing the rent ceiling while keeping the current subsidy formula would probably make price increases even larger, because under the present formula prices tend to increase until rents approach the rent ceiling.

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[1]Roughly 34 percent of total subsidy payments are diverted to landlords because of the price increases (the 26 percent rent increase becomes a 34 percent subsidy diversion because subsidy payments are only about 76 percent of preprogram rent). At the February 1979 program level of 520,000 units (and using the 1976 average subsidy of $103 per unit per month), this diversion amounts to $218.5 million annually.

Appendix A

THE SECTION 8 RENT INCREASE SIGNAL

This appendix shows how the Section 8 program systematically encourages landlords to raise rents to the program's published rent ceiling. Encouragement comes from the information provided on the "certificate of family participation" (reproduced here) entitling the tenants to housing subsidies provided that they find an acceptable housing unit within 60 days. Tenants almost certainly show this form to prospective landlords when persuading the landlord to join the Section 8 program.

The certificate of family participation presents three pieces of information on rent payments. It gives the maximum rent the program allows the landlord to charge ("Fair Market Rent" in item 3), the maximum contribution to rent the tenant need make ("Gross Family Contribution" in item 4a),[1] and a rule for dividing the rent saving between the tenant and the local public housing authority if the rent is less than Fair Market Rent ("Rent Credit" in item 4b).

Those three pieces of information send a strong signal to the landlord: Both the public housing authority and the tenant will accept any rent up to the ceiling, regardless of the percentage increase from preprogram rent. Announcing an explicit rent ceiling invites landlords to treat it as a rent target, especially when it is called "Fair Market" rent rather than "maximum allowable" rent. Fixing the tenant's contribution to rent without regard to total rent shows the landlord that the tenant has no reason to object to a rent increase. Finally, calling the difference between Fair Market Rent and actual rent a "rent reduction" or a "rent saving" further encourages landlords to think of the Fair Market Rent as the correct rent to charge under the program.

Table Certificate

CERTIFICATE OF FAMILY PARTICIPATION, SECTION 8 EXISTING HOUSING ASSISTANCE PROGRAM (HUD FORM 52578, AS REVISED 6/76)

1. Certification. The undersigned Public Housing Agency ("Agency") hereby certifies that the Family headed by _____ _____ is authorized to participate in the Section 8 Housing Assistance Payments Program of this Agency. Under this program, the Agency makes housing assistance payments on behalf of participating Families toward their rents to Owners of Decent, Safe, and Sanitary dwelling units selected by the Families.

2. Dwelling Unit. If the Family finds a dwelling unit meeting its space requirements and otherwise suitable to its needs, which is in Decent, Safe, and Sanitary condition, the Family should submit to the Agency the "Request for Lease Approval," together with the required inspection reports and a proposed lease. Prior to approval of the proposed lease, the Agency will inspect the dwelling unit or cause it to be inspected.

3. Lease Rent. The monthly rental provided in the Lease must be determined by the Agency to be reasonable; and generally this rent, plus the Allowance approved by the Agency for any utilities and services payable directly by the Family, may not exceed the Fair Market Rents for a _____ bedroom dwelling unit, which are $_____ for elevator buildings and $_____ for non-elevator buildings.

[1]Usually equal to 25 percent of adjusted gross income.

Certificate of Family Participation (continued)

4. Family Portion of Rent.

   (a) Gross Family Contribution. Under the rules and regulations of the Housing Assistance Payments Program, the Family will be obligated to pay $_____ toward the monthly lease rental (Gross Family Contribution); however, this amount will be reduced (1) by any Allowance for utilities and services to be paid directly by the Family, and (2) by any Rent Credit as described in paragraph (b) below. Any such reduction will be reflected in the amount payable by the Family as specified in the Lease.

   (b) Rent Reduction Incentive.

      (1) As an incentive to the Family to find the most economical housing suitable to its needs, and subject to the other provisions of this paragraph (b), if the Family selects a dwelling unit for which the proposed monthly lease rental plus any applicable Allowance is below the applicable Fair Market Rent, the Family will be given a Rent Credit by a reduction in its Gross Family Contribution. The amount of this credit will be that percentage of the Gross Family Contribution which the Rent Saving is of the Fair Market Rent. The Rent Saving is the amount by which the Fair Market Rent exceeds the monthly lease rental (plus any applicable Allowance) approved by the Agency.

      (2) No Rent Credit under this paragraph (b) will be allowed if the dwelling unit is one which receives the benefit of Federal, State, or local subsidy, unless a specific exception has been approved by HUD.

      (3) If the dwelling unit selected by the Family is of a size or type for which HUD had previously approved a maximum rent higher than the Fair Market Rent, this higher maximum rent will be used instead of the Fair Market Rent for purposes of determining the amount of the Rent Credit under the provisions of paragraph (b)(1).

   (c) Changes in Family Income and Other Factors. The amount of the Family's required Gross Family Contribution is subject to change by reason of changes in Family income, composition, and extent of exceptional medical or other unusual expenses and changes in the Allowance for Utilities and Other Services and the Contract Rent.

5. Agency Portion of Rent. Pursuant to a Housing Assistance Payments Contract with an Owner, the Agency will pay to the Owner on behalf of the Family an amount equal to the difference between the Family portion of the rent to the Owner and the monthly lease rental.

6. Agency Approval of Lease.

   (a) After receipt of a Request for Lease Approval, the Agency will notify the Owner and the Family whether or not the proposed lease is approvable. This notification will be given within _____ working days from the date of availability for inspection as stated in the Request for Lease Approval.

   (b) The Agency, upon issuing this Certificate of Family Participation, anticipates that if a lease meeting the requirements of this program is submitted for approval, the Agency will have funds available for a Housing Assistance Payments Contract with the Owner; however, the Agency is under no obligation to the Family, to any other Owner or to any other person to approve any submitted lease, nor does the Agency incur any liability by reason of issuing this Certificate.

7. Conditions. The Family agrees to perform all its obligations under the Housing Assistance Payments Program, including the obligations to (a) provide such Family income information and records as may be required in the administration of the program, (b) permit inspection of its dwelling unit at reasonable times after reasonable notice, and (c) give at least 30 days notice to the Agency of the Family's intention to vacate the unit.

8. Equal Housing Opportunity. If the Family has reason to believe that, in its search for suitable housing, it has been discriminated against on the basis of race, color, creed, religion, sex, or national origin, it may file a complaint with the HUD Regional Office. Fair Housing Complaint Forms (Forms HUD-903) are available from this Agency.

9. Expiration Date. A Request for Lease Approval may be submitted to this Agency no later than _____ (60 days from the date of this Certificate). If a Request for Lease Approval is not submitted by such date, this Certificate shall expire unless extended by the Agency in writing.

_____
(Name of Public Housing Agency)

BY _____
(Signature and Title)

Date _____

Telephone Number: _____

_____
(Name of Family Representative)

BY _____
(Signature of Family Representative)

Date _____

_____
(Present Address)

Telephone Number: _____

Two aspects of the certificate of family participation partially counteract the encouragement given to landlords to raise rents. First, the initial sentence in item 3 requires that rents must be "reasonable," suggesting that the local public housing authority might resist rent increases. Second, the rent reduction credit offered in item 4b suggests that tenants might resist rent increases.

However, the first restraint on rent increases is very weak because no definition of "reasonable" rent is given. In fact, a quick reading of the form could easily leave the impression that any rent not exceeding the stated Fair Market Rent is reasonable, regardless of the quality of the unit in question.

The rent reduction credit fails to restrain rent increases because tenants only receive part of the rent saving and, more importantly, few tenants have any idea of how much of that saving they will get.

The certificate of family participation defines the rent reduction credit precisely, but abstractly. It uses language that requires algebra to find the fraction of rent saving tenants will get. In contrast to the explicit notice of Fair Market Rent and Gross Family Contribution, the fraction of rent savings going to the tenant is left implicit.

As defined in item 4b, the rent reduction credit to the tenant is "that percentage of the Gross Family Contribution which the Rent Saving is of the Fair Market Rent." In symbols the definition is:

$$C_t = \left[\frac{S-R}{S}\right] P \tag{A.1}$$

where C_t = rent reduction credit to tenant,
R = gross rent,
S = Fair Market Rent (given in item 3),
P = Gross Family Contribution (given in item 4a).

Using algebra, the fraction of the rent saving the tenant gets to keep, $C_t/[S-R]$, can be shown to equal the ratio of the Gross Family Contribution to the Fair Market Rent, P/S, and the tenant's net contribution to rent, $P-C_t$, can be shown to equal the gross contribution times the ratio of actual rent to fair market rent, $P[R/S]$.

It is not clear why tenants were not told explicitly that the ratio of the number in item 4a to the number in item 3 gives the fraction of the gap between actual rent and Fair Market Rent that they get to keep. The ratio could easily have been computed for the tenant and entered on the form in item 4b.[2]

Of course, it is possible that even if more tenants had understood how the rent reduction credit works, the incentive would have been too small to prevent rent increases. Table A.1 shows that in 1976 the average tenant in the Section 8 program kept only 40 percent of any rent saving (the average Gross Family Contribution was $71 per month per unit, the average Fair Market was $181 per month per unit, and their ratio is 0.4). Moreover, the poorest tenants had smaller than average Gross Family Contributions (which equaled 25 percent of income)

[2]It is interesting to note that when revising the certificate of family participation in October 1978, HUD chose to be less rather than more explicit about the rent reduction credit. The new form did not even offer a complete abstract definition, but simply stated that "The Family may be allowed a Rent Credit if the rent plus the allowance for tenant-paid utilities and services for the selected unit is less than the maximum amount approvable by the PHA. The PHA will determine the amount of the Rent Credit." In October 1980, HUD eliminated the rent reduction credit from the Section 8 program, arguing that it did not reduce rents enough to be worth the cost in increased subsidies (*Federal Register*, 1980, pp. 59308-59309).

and hence would only get to keep a smaller than average fraction of any rent saving. The poorest tenants were likely to be living in the lowest quality housing where market rent was likely to be furthest below Fair Market Rent; thus the rent reduction credit provided the weakest restraint on rent increases precisely where the largest rent increases could occur.

Table A.1

AVERAGE RENT PAYMENTS IN THE SECTION 8 EXISTING HOUSING ASSISTANCE PROGRAM

Item	Symbol	Average Monthly Amount ($) per Unit
Tenant Rent Payment		
Gross family contribution	P	71
Rent reduction credit to tenant	$-C_t$	-4
Total		67
Authority Rent Payment		
Fair Market Rent	S	181
Rent reduction credit to authority	$-C_a$	-7
Gross family contribution	$-P$	-71
Total		103
Total Rent Payment		
Gross rent	R	170

SOURCE: Margaret Drury, Olsen Lee, Michael Springer, and Lorene Yap, *Lower Income Housing Assistance Program (Section 8): Nationwide Evaluation of the Existing Housing Program*, Office of Policy Development and Research, U.S. Department of Housing and Urban Development, Washington, D.C., November 1978, pp. 31, 39, and 70.

NOTE: The averages in this table are for all renters in the housing assistance program, movers as well as nonmovers. By definition $C_t + C_a = S-R$, and the cited pages show that $R = [0.94]F$ $C_t = [0.48][8]$, $P-C_t = 67$ and $R-P + C_t = 103$, on average. Solving those five equations yields $F = 181$, $R = 170$, $P = 71$, $C_a = 7$, and $C_t = 4$.

Appendix B

SUPPLEMENTARY TABLES: RENT INCREASES IN THE HOUSING ALLOWANCE AND SECTION 8 PROGRAMS

The additional information in Tables B.1 through B.4 reinforces the text's message that the Section 8 program causes large price increases while the housing allowance program causes only small ones, even when controlling for preprogram rent level. These tables give average rents as well as the percentage changes reported in the text, and cover the no-move, repair situation as well as the no-move, no-repair situation reported in the text.

Table B.1

RENT INCREASES UPON JOINING THE HOUSING ALLOWANCE PROGRAM: BROWN COUNTY, WISCONSIN

Preprogram Rent Interval ($/Unit/Mo)	Average Preprogram Rent ($/Unit/Mo)	Average Program Rent ($/Unit/Mo)	Average Rent Increase (%)
No Repair			
5-50	43.95	48.15	9.6
51-150	119.11	123.15	3.4
More than 150	191.08	192.93	1.0
All rents	163.88	166.54	1.6
Repair			
5-50	44.38	54.84	23.6
51-150	117.51	122.55	4.3
More than 150	184.50	186.97	1.3
All rents	151.16	154.93	2.5
All Units without Occupant Turnover			
5-50	44.08	50.16	13.8
51-150	118.44	122.90	3.8
More than 150	189.07	191.11	1.1
All rents	159.40	162.45	1.9

SOURCE: Housing Assistance Supply Experiment, Housing Allowance Program records for Brown County through year 3.

NOTE: Rent in this and subsequent tables is gross rent (contract rent plus direct tenant payments for utilities). The sample includes households in regular rental units who paid at least $5/mo. gross rent at enrollment and were authorized for payments in their enrollment units.

Table B.2

RENT INCREASES UPON JOINING THE HOUSING ALLOWANCE PROGRAM: ST. JOSEPH COUNTY, INDIANA

Preprogram Rent Interval ($/Unit/Mo)	Average Preprogram Rent ($/Unit/Mo)	Average Program Rent ($/Unit/Mo)	Average Rent Increase (%)
No Repair			
5-50	41.74	46.71	11.9
51-150	121.56	123.42	1.5
More than 150	194.63	194.78	.1
All rents	156.93	157.97	.7
Repair			
5-50	44.23	53.62	21.2
51-150	118.65	122.74	3.4
More than 150	187.68	188.70	.5
All rents	152.08	154.71	1.7
All Units without Occupant Turnover			
5-50	43.34	51.15	18.0
51-150	120.17	123.10	2.4
More than 150	191.27	191.84	.3
All rents	154.60	156.40	1.2

SOURCE: Housing Assistance Supply Experiment, Housing Allowance Program Records for St. Joseph County through year 3.

NOTE: See Table B.1.

Table B.3

RENT INCREASES UPON JOINING THE SECTION 8 EXISTING HOUSING ASSISTANCE PROGRAM

Preprogram Rent Interval ($/Unit/Mo)	Average Preprogram Rent ($/Unit/Mo)	Average Program Rent ($/Unit/Mo)	Average Rent Increase (%)
No Repair			
5-50	37.8	138.8	267
51-150	109.1	145.1	33
More than 150	175.0	182.0	4
All rents	126.9	159.9	26
Repair			
5-50	46.6	170.6	266
51-150	106.0	156.0	47
More than 150	185.7	198.7	7
All rents	131.3	173.3	32
All Units without Occupant Turnover			
5-50	39.7	145.7	267
51-150	107.9	148.9	38
More than 150	180.0	189.0	5
All rents	128.6	164.6	28

SOURCE: Margaret Drury, Olsen Lee, Michael Springer, and Lorene Yap, *Lower Income Housing Assistance Program (Section 8): Nationwide Evaluation of the Existing Housing Program*, Office of Policy Development and Research, U.S. Department of Housing and Urban Development, Washington, D.C., November 1978, p. 66.

NOTE: The reference gives the rent increase, D, and the percentage rent increase, P. The preprogram rent, R_1, and the program rent, R_2, were computed from that information by solving the equation $R_2-R_1 = D$ and $[R_2-R_1]/R_1 = P/100$. The exercise exposed a typo in the referenced report which is corrected here (47 percent was typed as 27 percent).

Table B.4

Percentage Distribution by Preprogram Rent: Units Receiving Housing Assistance Without Occupant Turnover

Preprogram Rent ($/Unit/Mo)	Housing Allowance Program			Section 8 Existing Housing Assistance Program
	Brown County	St. Joseph County	Average	
No Repair				
5-50	.9	.4	.7	14.4
51-150	35.9	50.7	43.3	43.1
More than 150	63.2	48.9	56.0	42.5
All rents	100.0	100.0	100.0	100.0
Repair				
5-50	.7	.8	.8	8.1
51-150	48.3	49.9	49.2	54.2
More than 150	51.0	49.3	50.0	37.7
All rents	100.0	100.0	100.0	100.0
All Units without Occupant Turnover				
5-50	.8	.6	.7	12.1
51-150	40.4	50.3	45.3	47.8
More than 150	58.8	49.1	54.0	40.1
All rents	100.0	100.0	100.0	100.0

SOURCE: Housing Assistance Supply Experiment, housing allowance program records for Brown and St. Joseph counties; and Margaret Drury, Olsen Lee, Michael Springer, and Lorene Yap, *Lower Income Housing Assistance Program (Section 8): Nationwide Evaluation of the Existing Housing Program*, Office of Policy Development and Research, U.S. Department of Housing and Urban Development, Washington, D.C., November 1978, p. 66.

NOTE: Having computed preprogram and program rents (see Table B.3) the distribution of units by preprogram rent intervals was found by solving the equation for average rent. For example, for units requiring no repairs, where X and Y are the fractions of units having preprogram rents from 5-50 and 51-150, the equations are: $37.8[X] + 109.1[Y] + 175.0[1-X-Y] = 126.9$, and $138.8[X] + 145.1[Y] + 182.0[1-X-Y] = 159.9$.

Appendix C

RECENT REEVALUATION OF THE SECTION 8 EXISTING HOUSING ASSISTANCE PROGRAM

As this report was going to press, the draft of a 1979 reevaluation of the Section 8 program became available (Wallace, Bloom, Holshouser, Mansfield, and Weinberg, forthcoming in 1981). The reevaluation confirms the central message of this report—that Section 8 regulations cause landlords to raise the price of housing services toward the FMR ceiling.

One part of the reevaluation covered households who applied to the Section 8 Existing Housing Program during the summer of 1979 (and joined it within three months of applying) in 15 selected metropolitan areas.[1] Table C.1 compares the average preprogram and program rents to FMR in this 1979 sample with those of the original 1976 nationwide evaluation (the original evaluation's results are converted to 1979 dollars in the table). Both studies show that landlords of units requiring no repairs raised their rents to 92 percent of FMR, on average. The price increase mechanism of the Section 8 program appears to have operated consistently during 1976-79.

There is a difference between the two findings, however. In the original evaluation preprogram rents averaged 73 percent of FMR, while in the reevaluation they averaged 86 percent of FMR. Because the rents in the reevaluation started from a higher level but ended up at the same level (with respect to FMR), the price increases found by the reevaluation were smaller: 6 percent as opposed to the 26 percent in the original evaluation.

If the higher preprogram rents in the reevaluation sample could be accepted as representing the national program, then we might conclude that three-fourths of the characteristic Section 8 price increase observed in 1976 had disappeared by 1979. However, that conclusion is inappropriate for three reasons. (1) The reevaluation covers only 15 metropolitan areas that explicitly do not represent the national Section 8 Existing Housing Program. (2) The sample of households was chosen prospectively rather than retrospectively, so that the agencies administering the program knew which cases were being tracked; supervisors may have been especially reluctant to approve large rent increases for cases in the study panel. (3) The average constant-dollar income of Section 8 recipients in the national program did not change appreciably after 1976,[2] so the average constant-dollar preprogram rent in the national program probably did not change appreciably.

The reevaluation whets one's appetite for more facts. From Section 8 administrative reports, HUD could regularly assemble statistics on average preprogram rent, average program rent, and average Fair Market Rent for all households in the national Section 8 Existing Housing Program (making the usual distinctions between mover and stayer households and between units requiring and not requiring repairs). Such statistics not only would reveal any

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[1]This reevaluation of the Existing Housing Program was incidental to the main purpose of the study, which was an analysis of the Section 8 New Construction Program.

[2]Yap et al. (1978, p. 45) report that the average annual income of Section 8 Existing Housing Program participants in 1976 was $3,533. Adjusted to 1978 dollars by the national CPI it is $4,049. That amount is only slightly lower than the $4,213 average annual income of all families certified for occupancy in the Section 8 Existing Housing Program during 1978 (*HUD Statistical Yearbook*, 1978, p. 229).

Table C.1

AVERAGE PREPROGRAM, PROGRAM, AND FAIR MARKET RENTS FOR DWELLINGS THAT REQUIRED NO REPAIRS AND WHOSE OCCUPANTS DID NOT MOVE WHEN JOINING THE SECTION 8 PROGRAM

Rent	Original Nationwide Evaluation of the Section 8 Program		Recent Partial Reevaluation of the Section 8 Program	
	$/Unit/Month, 1976 data in 1979 dollars	Percent of FMR	$/Unit/Month, 1979 data	Percent of FMR
Preprogram rent[a]	161.8	73.0	211.0	86.1
Program rent[a]	203.9	92.0	224.0	91.5
Fair Market Rent[b]	221.6	100.0	244.8	100.0

SOURCE: Margaret Drury, Olsen Lee, Michael Springer, and Lorene Yap, *Lower Income Housing Assistance Program (Section 8): National Evaluation of the Existing Housing Program*, Office of Policy Development and Research, U.S. Department of Housing and Urban Development, Washington, D.C., November 1978, pp. 31 and 66; and James E. Wallace, Susan P. Bloom, William L. Holshouser, Shirley Mansfield, and Daniel H. Weinberg, *Participation and Benefits in the Urban Section 8 Program*, Abt Associates, Cambridge, Mass, AAI-80-135, forthcoming in 1981, Table 6-17.

[a]The national Consumer Price Index rose by 27.5 percent during 1976-79, so the average preprogram and program rents in Table B.3 were multiplied by 1.275 to transform them to 1979 dollars, (126.9)(1.275) = 161.8 and (159.9)(1.275) = 203.9.

[b]Drury et al. (1978, p. 31) report that the average program rent for stayer units was 92 percent of FMR; hence the average FMR for the original evaluation is 159.9/.92 = 173.8, and converting to 1979 dollars it is (173.8) (1.275) = 221.6. Olsen and Rasmussen (1979, p. 17) report that FMRs increased 12.1 percent per year during 1975-78 so we estimate that the average FMR in the reevaluation is (173.8) $(1.121)^3$ = 244.8.

changes in the program-induced price increases, but also would show whether the changes were caused by different preprogram rents or different program rents.

Possibly such statistics would show that the Section 8 price increases have become larger since 1976, because the Fair Market Rent target has been increasing faster than background price inflation (Olsen and Rasmussen, 1979, p. 17). If the program changes suggested in Sec. III of this report were implemented, the new statistics would show whether the changes had the desired result of bringing the program-induced price increases under control.

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