Expanding Housing Demand Efficiently and Equitably

Robert I. Lerman[*], American University and Urban Institute

For presentation at

Association for Social Economics, Allied Social Science Association Meetings

January 5, 2010

Atlanta, Georgia

[*] Professor of Economics, American University and Institute Fellow, Urban Institute. The author thanks Katharina Moll and Sarah Cordes for excellent research assistance and thanks Jeffrey Lubell for providing some background information on the current Voucher Homeownership Program. Correspondence and questions may be sent to Robert I. Lerman, blerman@urban.org.

Introduction and Overview

Battered housing prices remain important as the economy struggles to recover from the 2007-2009 economic and financial crises. Toxic assets in the form of under wage mortgages are still worth far less than the loans on the books. The Obama Administration has been attacking the problem with a variety of measures to slow down foreclosures, including up to a $75 billion housing package and a financial fix involving potentially hundreds of billions to insure private investors against excess losses from their purchases of toxic assets. The President and Congress recently extended the homeownership tax credit with benefits available to couples with incomes exceeding $200,000. Unfortunately, measures to subsidize banks and homeowners to prevent foreclosures and to encourage home buying can be exceedingly costly and inefficient. For example, the prior homeownership credit will have subsidized purchases that would have taken place without the credit, resulting in a cost per new home purchase of $43,000 and a budget cost of $15 billion, or double what the Congress expected (Gayer 2009). Moreover, President Obama's Homeowner Affordability and Stability plan has reached only three percent of eligibles (Merle 2009) and eligibility requires that the new mortgage be no more than 105 percent of the home value.

A second issue is that the subsidies might prop up prices in areas due for price corrections from unsustainably high levels. After all, the geographic areas hardest hit by recent declines in home prices are mainly the areas with the highest price increases in the prior decade.[1] While vast taxpayer sums are directed to homeowners in these areas and the institutions that financed them, the country is missing a good opportunity to use more equitable and efficient methods for

[1] Using data on 104 large metro areas drawn from the Housing Price Index of the Federal Housing, I find a negative correlation of -.69 between housing prices from 1998-2007 and from 2007 and late 2008. The correlation drawn from the Case-Shiller index on 38 cities is -.49.

stimulating demand for owner-occupied housing in the short run and improving housing programs and housing outcomes in the long run.

This paper proposes to expand substantially the housing choice voucher program's Voucher Homeownership Program. Specifically, the plan is to encourage the purchase of owner-occupied dwellings using some of the existing 2 million rental vouchers and to finance an additional 1 million vouchers designated for homeownership. The approach is especially appropriate in the current environment because of the many geographic areas in which the monthly carrying costs of buying a home is less—sometimes considerably less—than the fair market rent (FMR) specified under the existing section 8 program. Although the existing Voucher Homeowner program administered by the Department of Housing and Urban Development (HUD) provides local housing authorities with homeownership options, the existing program operates at a very small scale, only about 2,000 units nationwide.

The initiative to expand and add flexibility to the Voucher Homeowner effort would take advantage of the recent decline in home prices relative to rent levels. Despite the 15 percent drop in the median price of houses sold between December 2007 and December 2008, the Bureau of Labor Statistics shelter index (which measures rents or the rental value of an owner-occupied home) actually increased by 3 percent in 2008. Since rent levels determine voucher subsidies, homes in an increasing share of the U.S. metropolitan areas have become affordable to low-income families receiving section 8 rent vouchers.

Under the existing and expanded Voucher Homeowner plan, current and new recipients of rent subsidies can use their subsidies to help pay the monthly mortgage, tax and insurance costs. The added costs would be modest for existing vouchers and about $7 billion per year for an additional 1 million vouchers. This expanded Voucher Homeownership (VH) proposal would generate a jump in demand for owner-occupied housing, while helping low-income families who qualify for housing assistance but are currently shut out because federal housing subsidies are rationed. It turns out that in well over 80 percent of the top 106 metropolitan areas, rents are currently being subsidized at levels that would make owner occupied housing affordable to Housing Choice Voucher recipients. The plan could create 1.5 million new potential homebuyers, or about 25 percent of the 6 million annual rate of new and existing home sales (as of September-November 2009).

The paper begins with a description of the plan and its rationale. Next, I present data looking at the affordability of homeownership for voucher-assisted households in about 100 metropolitan areas. The analysis compares the monthly costs of homeownership and FMRs across geographic areas. I then confront some of the arguments against the plan and some adjustments that might be appropriate. A natural question is: should low-income families be assisted to buy homes? Another key issue is the concern about extending income-testing and high marginal tax rates to a broad population. The paper then briefly describes some experience reported in local housing authorities with the homeowner voucher concept. I conclude with a discussion of policy implications.

The Expanded Homeownership Voucher Plan

The plan is to expand substantially the number of homeownership vouchers provided through Housing Choice Voucher program. As under the current homeownership option program authorized in 2000, holders of existing rent vouchers would be offered the opportunity to use the subsidy value embedded in the voucher to pay the costs of homeownership. In addition, the federal government would issue 1 million new vouchers specifically designated as homeowner vouchers. The financial terms of the program would be identical to existing vouchers, though the new vouchers might adjust time limits. Currently, homeownership vouchers are available as a local option and some local housing authorities have used the approach and the wide discretion allowed over the terms of homeowner voucher subsidies. The expanded program would operate at a much larger scale and involve some changes in federal guidelines.

Under the standard Housing Choice Voucher program, the maximum subsidy in a geographic area is the "fair market rent," established by U.S. Department of Housing and Urban Development (HUD) in each area at the 40^{th} percentile of local rents. In an area where the fair market rent (FMR) is $800 per month, a family renting a dwelling for that amount pays 30 percent of its countable household income up to the point where the subsidy phased out. A family with countable income of $1,000 per month would effectively receive a $500 per month subsidy and pay only $300 in rent.

The Voucher Homeowner (VH) program provides a subsidy for the carrying costs of homeownership on close to the same terms as the Housing Choice Voucher program. Participants in the VH program qualify for the FMR for their household size and pay 30 percent of their income to offset the subsidy. As in the case of rent vouchers, families contribute more toward housing costs as their incomes rose and would contribute less when their incomes fell. Like other income-conditioned programs, an expanded VH program can act as a type of automatic stabilizer but does impose benefit reduction rates that penalize added earnings.

The VH program already requires homeowners to complete a pre-assistance homeownership counseling program, which includes topics such as home maintenance, budgeting, credit counseling, and how to find a home. Other features of the homeownership option are more questionable, including the first-time homeowner provision, the minimum income provision, and the requirement of continuous employment in the prior year.

The expanded VH program would resemble the existing homeownership option and rent subsidy programs in limiting benefits to people below current eligibility limits and in requiring families to provide indications of their capability to sustain homeownership. To help with repairs, each month homeowners would be required to allocate a small amount toward an insurance pool managed by local housing authorities. Under the current section 32 homeownership programs, some PHAs already provide insurance for major systems of properties and/or require monthly payments into a maintenance reserve account. Other elements of the program might or might not depart from the standard Housing Choice rental vouchers. Entry requirements might extend beyond low income. Families might have to save enough to contribute to a down payment. Homeownership subsidies are now limited to 15 years, but might be extended under the HV program. Resale might involve some recoupment of government subsidies, especially for long duration participants. At a minimum, any government participation in providing payments on the loan's principal should be repaid.

The VH program has attractive equity as well as efficiency features. Unlike other large outlays on the housing market, the expanded HV program can be well-targeted and equitable. Except for modest administrative costs, the added government funding would all go to low-income families, often raising family incomes sufficiently to move families out of poverty.
The major long-term horizontal inequity in housing subsidy programs is that most of the 18 million eligible households receive no subsidy. Of low-income eligible renter families with children (those with incomes below 50 percent of the median income), only 28 percent receive a housing subsidy while about 70 percent of equally poor families who qualify for benefits receive

no subsidy (Turner and Kingsley 2008).[2] Expanding the subsidy program would reduce this inequity. An expansion of 1 million slots would raise the share covered to 43 percent of eligible families with children.

On the efficiency side, several questions arise. One is cost-effectiveness from a government budget point of view. We can define the criterion as annual costs of the housing subsidy or the present value of the costs per additional covered household. A second component would take account of the added value gained by potential recipients per dollar of government expenditure. Would families gain as much through a homeownership program as through the rental program? Although the causal evidence is mixed, we do know homeownership is associated with a variety of gains for families, children, and communities (Lerman and McKernan 2008). For this paper, I do not attempt to quantify the potential nonfinancial gains to families nor the potential benefits to communities from raising the share of people who become stable homeowners. Instead, I look only at the relative financial costs of government action to widen coverage of housing subsidies for eligible households.

A common question raised about this type of program is—should low- to lower-middle income families be homeowners? Is it not too risky for low-income families to own homes? Since homes represent a high share of net worth and prices vary, many see purchasing a home as a particularly risk investment, one that low-income families can ill afford. But, this approach fails to recognize the importance of homeownership as a hedge against increases in area housing costs, as indicated by rent levels. As Sinai and Souleles (2005) point out, owning a home with a fixed rate mortgages locks in the price of housing services for a long period, while prices for

[2] A recent bill reported out by the House Financial Services Committee (HR 3045: Section 8 Voucher Reform Act of 2009) calls for a modest increase in subsidized units (150,000) but also would increase further the benefits to existing rents, thereby exacerbating the differential between households with vouchers and equally poor households without vouchers.

housing services in one or several rental units can be highly variable. Although capital losses are possible, they are only damaging when you move to another location where home prices are not correlated with prices in your existing location. In line with their perspectives, Sinai and Souleles show that homeownership becomes more valuable and less risky where rents are most volatile and when spatial correlation is high.

The Sinai-Souleles analysis has distinctive implications for the value of homeownership to low-income families specifically. They find long time horizons lower the risks of homeownership relative to renting. Now, low-income households often have short time horizons and move often but they do tend to stay in the same geographic area. Moreover, the government should have a long time horizon and thereby favor locking in the cost of their subsidies. A second point is that households who apply a high share of their incomes to renting are particularly sensitive to rent risks, making homeownership a more attractive option for those with high rent-to-income ratios.

One interesting non-financial rationale for helping many low-income families own homes through this approach relates to marriage and family structure. As Kathryn Edin and Maria Kefalas (2005) point out, unmarried couples with children often choose to delay marriage until they can afford to live in their own home. Helping these couples make their way into owning homes can stabilize the relationship and encourage marriage.[3]

In addition, there are other non-economic benefits of homeownership found in various empirical studies (Lerman and McKernan 2008). Benefits have been detected for child outcomes, satisfaction, wealth accumulation, and political activity. Still, questions remain about whether the government can promote this goal at a reasonable cost and without setting off additional financial problems in the future.

---

[3] Thanks to Andrew Cherlin, the well-known family sociologist, for making this point.

Are Homes Affordable with Homeowner Vouchers?

To determine affordability, we begin by pulling together data on FMRs and on home values by county and metro area for nearly all of the largest 108 counties.[4] The FMR data comes from the Department of Housing and Urban Development (HUD) website (http://www.huduser.org/datasets/fmr.html). The data on home values comes from the 2007 American Community Survey detailed tabulations, updated for subsequent price trends as measured by both the Case-Shiller index and the OFHEO index. In addition, we compile estimates of taxes and homeowner's insurance relevant to each home.

Central to the issue of affordability is quality of the home. As a proxy for quality, I use the rankings of homes by market value. Although the families eligible for Housing Choice vouchers are below the 25th percentile of the income distribution, I base the primary analysis on their ability to buy a home at the 25th percentile of the distribution of values of owner-occupied homes. The FMR is based at a higher percentile of rents (the 40th), but since incomes of homeowners are well above incomes of renters, the income category of homeowners at the 25th percentile is generally substantially higher than the income category of renters at the 40th percentile. In fact, the median income of nonelderly households renting at about the 40th percentile is only about one-half of the median incomes of nonelderly households who own a home at the 25th percentile of home values.[5] For the U.S. as a whole, the median income of owners around the 25th percentile of home values was about $55,000 while the median income of renters around the 40th percentile of rents was only about $29,000. Since homes at the 25th percentile threshold are likely to be of higher quality than qualified rentals, the estimates will overstate the carrying costs of homeownership at the same quality level.

---

[4] I thank Katharina Moll for her excellent research assistance in compiling these data.

[5] These results come from tabulations by the author from the 2007 American Community Survey micro data.

Having specified a home value used for purposes of defining affordability, we calculate affordability by taking the absolute difference between FMR and the carrying costs of homeownership at the 25th percentile. Carrying costs include interest on a 30 year mortgage that finances the full purchase price of the home, plus taxes and interest payments. Inclusion of principal would mean that the government is not only providing a subsidy for shelter each month but providing a capital transfer as well.

Before looking at the data on a group of metro areas, let us consider the case of the provision of homeowner vouchers in a particular area—Allegheny County, Pennsylvania, which is part of the Pittsburgh metro area. Note it is not simply the central city. The area's population in 2000 was 1.3 million. As of mid 2009, the price of a home at the 25th percentile stood at $78,166. The fair market rent for a three-bedroom apartment was $883 per month. If a current renter borrowed the full $76,565 at 5 percent interest for 30 years, the full monthly mortgage payment would be only about $420 per month, about $463 less per month than the FMR. Of course, taxes and insurance add to the monthly costs, but the repayment of principal involves the accumulation of wealth. The pure carrying costs—not including principal but adding in taxes and insurance—amount to $493 per month, still nearly $400 less per month.

How unusual is Pittsburgh? Certainly, home prices in Pittsburgh are well below the average for the top 108 counties in large metro areas. But, the FMR in Pittsburgh is also well below average.

To determine affordability in mid 2009 across our large group of counties, we performed these calculations using 2007 observations on prices at the 25th percentile and assumed these prices changed in line with the overall OFHEO trends. In Figure 1, we plot these updated home values against the difference between the county's FMR and the carrying costs of the home. Surprisingly, affordability at the FMR is common in the vast majority of metropolitan areas. In over 85 percent of the top 100 metro areas, the current FMR would be sufficient to finance the interest, tax, and insurance costs of a home purchase at the 25th percentile of home values. The average monthly saving in the affordable areas is nearly $370. Affordability would jump further if participants could use the $8,000 first time homeowner credit available in 2009 for a down payment.

Using the Case-Shiller index, we can examine the patterns in 38 counties as of March 2009, assuming that each county's price trends reflects the associated price trends measured for the 20 metropolitan areas in the index. Figure 2 shows that in all but two counties (Kings and New York) the FMR for a three bedroom unit would more than finance a home at the 25th percentile. The average dollar gap between the FMR and monthly interest, tax, and insurance payments for the affordable 38 counties is $487 per month.

Areas with recent dramatic declines in prices are of special interest. In many of these areas, the homeowner voucher is now well above what is required to pay the home's carrying costs (see Table 1 for examples). In Miami, Florida (Dade County), the FMR for a three bedroom apartment is $1,479 while the carrying cost of the home at the 25th percentile (priced at $125,449) is only $646, a whopping $833 difference. Affordability is evident in most other counties experiencing large drops in home values, including several California, Arizona and other Florida counties. In most of the areas, significant amounts are left over from the housing subsidy and can be paid into a pooled fund for potential repairs or can be used to reduce government costs.

What about the riskiness of these loans and future foreclosures? In fact, lending through the Voucher Homeowner program can be less risky than normal because the monthly voucher (an amount more than enough to pay the mortgage) would go to the bank independently of the family's income. Wouldn't the new policy repeat past mistakes in encouraging homeownership? No. Because the loans have relatively low risks, they could be provided at low interest rates. The low-income owners would not lose their home because of unemployment since the income loss would lower the participant's contribution while the government maintained the subsidy payment. Of course, even where rents and home values are favorable for the homeowner voucher, not all families will be ready to assume the upkeep and other responsibilities.

From the federal government's perspective, the fixed rate, long-term mortgage will lock in the bulk of housing costs at today's levels. Instead of continuing to finance rentals at the FMR, which is likely to rise over time, the federal government would be less subject to the risks of rising rents. These risks are real—between 1983 and 2007, the monthly principal and interest payment on a median-priced existing home rose by 79 percent between 1983 and 2007, much less than the rental equivalence increase of 140 percent.[6] Thus, savings could be substantial.

For the existing 2 million rent voucher recipients, encouraging broad application of the homeowner voucher approach could expand demand for owner-occupied housing as well at modest administrative expenses. If 25 percent of voucher holders moved to the Voucher Homeowner program and government also scaled up the program with funding for additional 1 million households, the nation would have 1.5 million new buyers—enough to make a dent in home inventories. The inventory of vacant dwellings for sale was about 2 million in the second quarter of 2009, though about 3.5 million vacant dwellings were held off the market for potentially marketing reasons. In addition, about 4.4 million vacant units were available for rent (http://www.census.gov/hhes/www/housing/hvs/qtr109/q109ind.html, Table 4).

[6] Bureau of Labor Statistics, http://www.bls.gov/cpi/cpiqa.htm#Question_2

Geographic Differentials and Geographic Mobility

One serious concern is that the wide variation in Fair Market Rents leads to large differentials in federal subsidies to families with equal incomes that live in different metropolitan areas. Of course, the rationale for the policy is to allow section 8 voucher recipients to afford units at the same relative position in the rental market, whether the metropolitan area is as expensive as San Francisco, California or as inexpensive as El Paso, Texas. At the same time, section 8 is supposed to allow for mobility so that a recipient receiving a generous voucher in Nassau County, New York could use the voucher in much less costly markets. Although mobility is uncommon in practice and perhaps discouraged by local housing authorities, the issue might become especially significant for homeowner vouchers. Should a homeowner voucher recipient in an expensive market be allowed to use his or her generous subsidy to buy a house in an expensive housing market?

Several alternative policies might make sense, both in the context of the homeowner vouchers and existing Housing Choice rental vouchers. One is to gradually narrow the geographic differentials in what the U.S. government provides to local authorities. As in the case of food stamps and federal Supplemental Security Income (SSI) benefits, the federal component would ultimately become smaller across geographic areas. For example, the ultimate amount could be a weighted average of area and national FMR. Another approach is to encourage mobility but limit the positive differential between the high FMR in an originating location (where the family received the voucher) and the low FMR in a destination location (where the family actually rents or buys). As an incentive to moving to a low cost area, the government might allow the family to keep up to 50 percent of the difference. If a family moved from a low to a high FMR location, the government would not be obligated to make up the difference.

Dealing with the wide geographic differentials is a difficult problem that affects the current rental voucher system as well as the expanded homeowner voucher system.

Recoupment Issues

The issue of recoupment of potential capital gains arises under the homeowner voucher program in a way that does not apply to the standard Housing Choice voucher program. The rental payments pay for a flow of housing services and involve no buildup of equity, no matter what happens to local property values or rent levels. The flow of housing is a nondurable service. However, the homeowner voucher recipient would become an owner of the property providing housing services. As an owner, the recipient could presumably sell the property and reap a capital gain or loss. How should any gains or losses be allocated?

PHAs running various homeownership voucher programs have used a variety of *ad hoc* procedures for dealing with gains from appreciation. Some attempt to capture 100 percent of the gain; others do so only with homes sold within the first five years of occupancy. Still others recoup 50 percent of the net gain during the first 10 ten years of occupancy. Local authorities providing for homeownership subsidies sometimes allow subsidized owners to keep some percentage of gain in home values, but others limit the sale price subsidized homeowners can charge on grounds of trying to keep specific units “affordable”. The idea in these small local programs of maintaining a few affordable houses as a way of influencing housing costs for low-income families seems quixotic since broader market forces will determine home and rental prices.

In considering recoupment, it is important to keep in mind that the homeowner voucher approach proposed here differs from local affordable housing programs and somewhat from existing homeowner vouchers. Unlike local programs that provide deep subsidies to a few, the proposed expansion of the homeowner voucher program provides small monthly subsidies graduated on the basis of income; in dollar terms, they are equivalent to a rental subsidy. The VH approach allows qualified recipients to choose the home they purchase on a subsidized basis, so long as the home meets the usual inspection conditions and is purchased at no more than appraised value.

Although the VH program is not aimed at preserving specific units at low price levels, government help to homeowners raises issues of recoupment. From one perspective, there is no need for recoupment because the vouchers are income support that involves the same or lower cost to the government than providing the same support through expanded rent vouchers. This argument is most convincing in cases where the government maximum payment (the amount paid when the household has zero income) involves no payment toward the principal on the mortgage. Where the government is contributing toward the principal, it is providing a wealth transfer as well as a subsidy to monthly carrying costs. In this case, owners who sell their homes for more than the original cost should be asked at least to repay the principal on the dwelling. Even where government does not pay any amounts toward principal, it is contributing significantly to the recipient's ability to build equity in the home, both through the monthly subsidies and through providing a guarantee to lenders that allow recipients to borrow at low interest rates. From this perspective, the government should be able to recoup some of the potential capital gains. However, a reasonable reply is that the government requires no recoupment (not even through a capital gains tax) to many households that benefit from tax benefits built into the tax law.

Requiring some recoupment might be appropriate as an offset to potential capital losses. A decline in the value of the home will not necessarily alter government costs or recipient payments, since recipients would generally want to stay in their homes and limit their housing costs to no more than 30 percent of their income. But, what if they choose to move to another location? If the recipients are liable to pay off the mortgage but cannot do so, credit risks will rise, potentially jeopardizing the affordability of the program. An alternative is for the government to take ownership and either consider the loss a long-term debt that recipients might ultimately have to repay or allow recipients to walk away with no further subsidy. Either outcome would involves a loss to the government on an *ex post* basis whether they sell the property or lose the opportunity to buy a less costly dwelling. At the same time, the government could rent the property, with a gross cost that is probably less than the FMR since it would have locked in monthly costs at a rate below initial FMR levels. In addition, losses related to some homes can be offset by recouping some of the gains accruing to other households.

Costs and Benefits in a Comparative Context

The costs of the initiative will depend importantly on the incomes of the homebuyers in the program. According to the Congressional Budget Office (2009), the cost per existing voucher is about $7,500 per year. If homeowners have incomes that are $4,000 above the average, the costs would fall to about $6,200 per year. For the additional million vouchers, the costs would be about $6.2 billion per year. In all likelihood, these costs will fall over time, because at least nominal incomes of participants will rise while the subsidy amount will remain relatively fixed because of the fixed monthly costs of principal and interest, although taxes and insurance can increase. Assuming, conservatively, that per household subsidies decline 1.5 percent per year, the present value (discounted at 4 percent) of 20 years of subsidies for the 1 million added vouchers would be about $73.7 billion. This figure is slightly below the $75 billion the Administration was willing to spend to shore up mortgages. However, unlike the

Administration proposal, the homeownership subsidies would be much better targeted, would not artificially inflate prices, and would have an immediate impact on housing markets. Unlike the escalating cost of rental vouchers associated with growth in rents (partially offset by rising tenant contributions from the growth in their incomes), the gross costs per unit of homeownership vouchers will not increase while subsidy recipients will increase their contributions.

Much of the benefit will be distributional. One million more low-income families will now be able to afford decent housing in their communities. In addition, they will know they have a stable place to live that will not impose high sacrifices if they lose income from reduced employment or other sources. The externalities may be important as well, but they are hard to quantify. Children will be less likely to have to move from one school to another. Some couples might marry and establish a longer term, healthier relationship within or outside marriage. More low-income people may do more to participate in the democracy. In all likelihood, housing quality of recipients is likely to improve significantly, even beyond the levels that would accrue for new rent vouchers. As noted above, the incomes of people at the 40th percentile of rents are well below the incomes of people owning at the 25th percentile of home prices.

Other potential benefits arise from the potential macroeconomic impact resulting from the boost in demand for owner-occupied dwellings. Currently, low-income families cannot buy dwellings at prices that involve carrying costs below, sometimes well below, the rents they are paying. One reason is the limited amount of mortgage credit for low-income families. Banks have apparently over-learned their lesson from lending to highly unqualified households buying homes at unusually high prices. As a result, many low-income families that can afford to own a home at today's prices cannot obtain the credit to purchase a home. The VH expansion would offer such families the opportunity toward an affordable route to homeownership.

Examples from the Field

The use of subsidies to help low-income and lower-middle people become homeowners is by no means a new idea. As Edgar Olsen (2007) points out, HUD sponsored an Experimental Housing Allowance Program (EHAP) in the 1970s that subsidies homeowners as well as renters. In fact, 42 percent of the recipients were homeowners, even though only 16-21 percent of all households in the sites were eligible for assistance. There were no particular problems in applying the subsidy to homeowners but in this case the experiment was aimed at lowering housing cost burdens broadly and not stimulating homeowners.

Other past programs have a mixed record. Under the Section 502 Single Family Direct Loan Program, which has assisted rural low-income people buy homes and make monthly payments on them, the USDA has been paying the difference between the sum of property taxes, homeowners insurance, operating expenses, and principal and interest payments at the government's borrowing rate, and 20 percent of the household's adjusted income. It seems to have worked reasonably well (Quercia, McCarthy, and Stegman 1993). On the other hand, the section 235 urban program did not work as effectively as the 502 program. Section 235 was marked by scandals and high default rates (Carliner 1998).

Looking at recent uses of homeownership vouchers, one finds considerably variation, small scale, but generally successful programs. In some programs, people qualify for the homeownership voucher program after staying in the rental program at least one year. As preconditions for loans, the programs have classes to help people gain a good understanding of their mortgage loan, budgeting and saving as a homeowner, basic home maintenance, and avoiding foreclosure. Some report that people are eager to fulfill the requirements of employment and creditworthiness in order to become a homeowner. Foreclosures are rare, with some PHAs not reporting a single foreclosure.

Although the reasons few PHAs have undertaken homeownership voucher programs, one possibility suggested by Olsen (2007) is the higher administrative costs of homeownership relative to rental voucher programs. If so, a modest increase in administrative allowances might have a major effect on the effectiveness of homeownership programs. One potential reason for high administrative costs is that people are channeled to specific homes by the PHA. With a more open choice for recipients, the costs might fall. In any event, the evidence from existing programs indicates homeownership vouchers are feasible.

A Caveat and a Response

One potential drawback of the Homeowner Voucher expansion is the potential negative impact on work incentives. The cumulative marginal tax rate from food stamps, housing assistance, and the worker's social security tax adds up to over 60 percent.[7] The Earned Income Tax Credit (EITC) offsets these high tax rates in some ranges of earnings, but EITC phase-outs exacerbate the problem at a $16,000-$18,000 annual income.[8] To reduce the danger of program-induced work reductions, the Voucher Homeowner plan could impose a strong work registration component as well as an option to assign some portion of earnings gains to an escrow account available after participants leave the program.[9]

[7] The marginal benefit reduction rate on earnings is 24 percent for food stamps, 30 percent for housing, and 7.65 for the worker's contribution to payroll taxes).
[8] As of 2008, the EITC began phasing out at a 21 percent rate at $15,750 for single parents with 2+ children and at $17,750 for married parents with 2+ children. These families could qualify for food stamps and housing assistance, potentially raising their overall marginal rate to 80 percent.
[9] For an application of escrow accounts to dealing with work disincentives under public housing and rent subsidy programs, see Cramer and Lubell (2009).

Summing Up

Without modest additional government spending, the Homeowner Voucher approach offers a way to raise demand for owner-occupied dwellings and increase efficiency by removing a distortion. Expanding housing demand further through Homeowner Voucher requires added spending but at least the public would recognize the benefits would be distributed in an equitable and efficient manner.

The ability of housing authorities to scale up the Homeowner Voucher program quickly is unclear. However, the economic logic clearly supports a significant expansion in general and especially in today's housing market.

References

Carliner, Michael S. 1998. "Development of Federal Homeownership 'Policy'." *Housing Policy Debate* 9(2): 299–321.

Congressional Budget Office. 2009. "Cost Estimate for H.R. 3045: Section 8 Voucher Reform Act of 2009. As ordered reported by the House Committee on Financial Services on July 23, 2009. September 16.

Cramer, Reid and Jeffrey Lubell. 2009. **"**Rental Assistance Asset Accounts: An Opportunity to Support Work and Savings Among Recipients of Federal Housing Assistance." Washington, DC: New American Foundation. http://www.newamerica.net/publications/policy/rental_assistance_asset_accounts_0

Gayer, Ted. 2009. "Should Congress Extend the First-Time Homebuyer Tax Credit." Brookings Institution. http://www.brookings.edu/opinions/2009/0924_tax_credit_gayer.aspx

Merle, Renae. 2009. "Refinancing lifeline fails to reach most 'underwater' borrowers." *Washington Post.* Accessed October 27, 2009.
http://www.washingtonpost.com/wp-dyn/content/article/2009/10/23/AR2009102303472.html

Lerman, Robert I. and Signe-Mary McKernan. 2008. "Benefits and Consequences of Holding Assets." In *Asset Building and Low-Income Families*. Edited by Signe-Mary McKernan and Michael Sherraden. Washington, D.C.: Urban Institute Press.

Olsen, Edgar. 2007. "Promoting Ownership Among Low-Income Households," Washington, D.C.: Urban Institute. http://www.urban.org/publications/411523.html.

George Peterson. 2000. "Housing Vouchers: The US Experience" In *Vouchers and the Provision of Public Services*. Washington, D.C.: Brookings Institution. 139-175.

Roberto G. Quercia, George W. McCarthy, and Michael A. Stegman (1993) . Mortgage Default Among Rural, Low Income Borrowers. Working Paper No. 96. Annandale-on-Hudson, New York: The Levy Economics Institute of Bard College.

Sinai, Todd and Nicholas Souleles. 2005. "Owner-Occupied Housing as a Hedge Against Rent Risk." *Quarterly Journal of Economics.* 120:2. 763-789.

Turner, Margery Austin and G. Thomas Kingsley. 2008. "Federal Programs for Addressing Low-Income Housing Needs: A Policy Primer." Washington, D.C.: Urban Institute. December. http://www.urban.org/UploadedPDF/411798_low-income_housing.pdf.

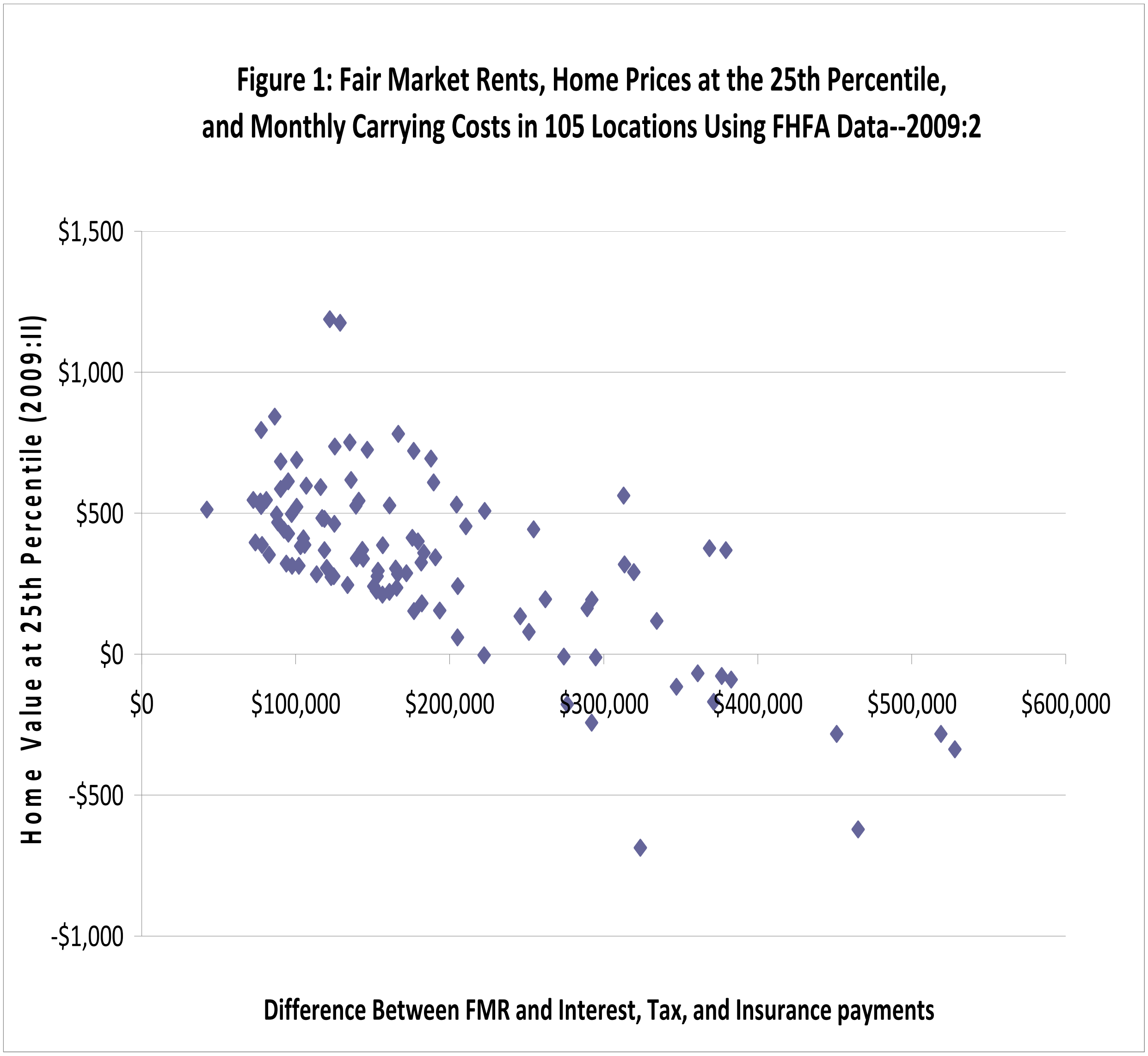
Figure 1: Fair Market Rents, Home Prices at the 25th Percentile,
and Monthly Carrying Costs in 105 Locations Using FHFA Data--2009:2
$1,500
$1,000
$500
$0
-$500
-$1,000
$0
$100,000
$200,000
$300,000
$400,000
$500,000
$600,000
Home Value at 25th Percentile (2009:II)
Difference Between FMR and Interest, Tax, and Insurance payments

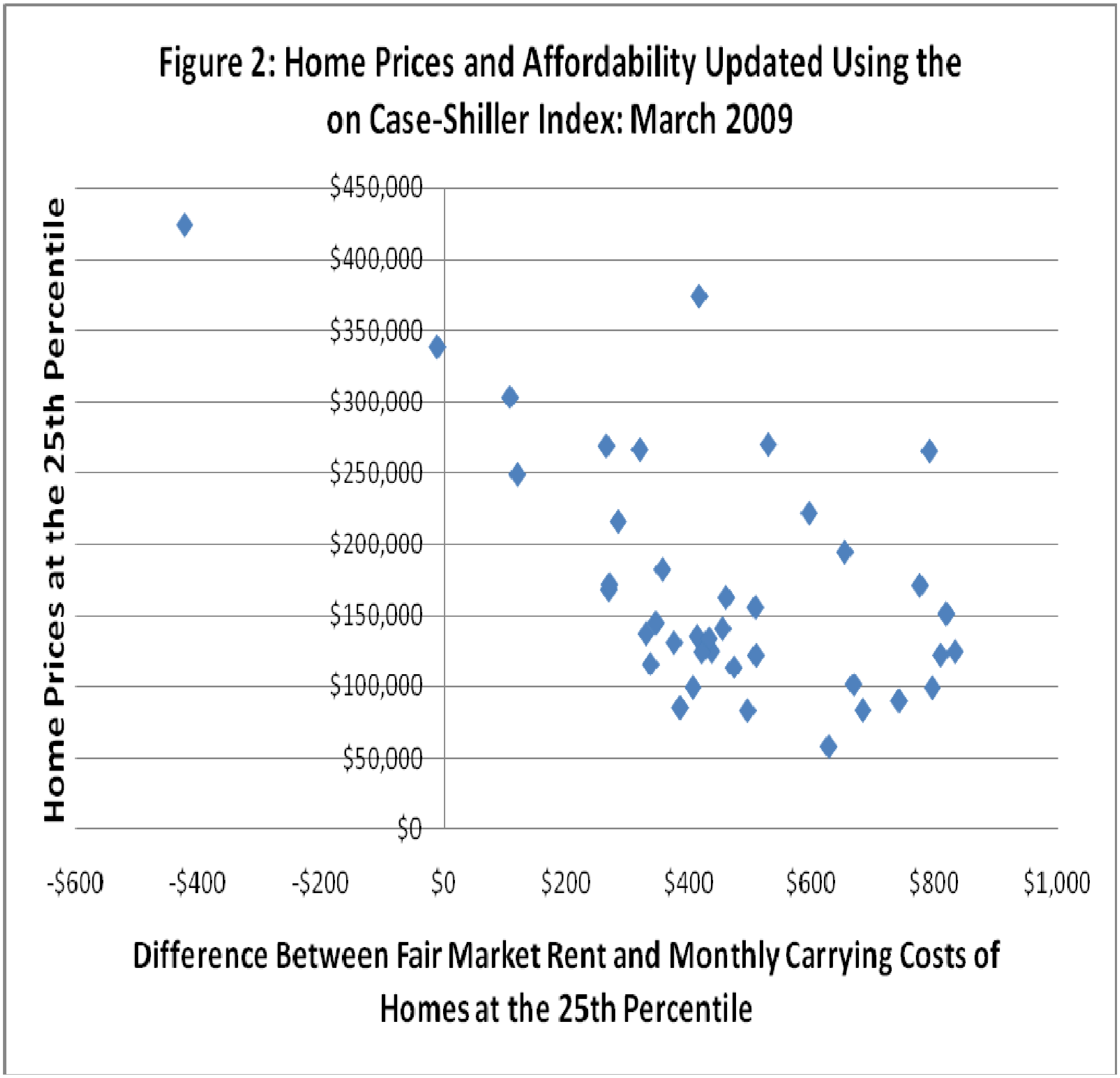
Figure 2: Home Prices and Affordability Updated Using the on Case-Shiller Index: March 2009
$450,000
$400,000
$350,000
$300,000
$250,000
$200,000
$150,000
$100,000
$50,000
$0
-$600
-$400
-$200
$0
$200
$400
$600
$800
$1,000
Home Prices at the 25th Percentile
Difference Between Fair Market Rent and Monthly Carrying Costs of Homes at the 25th Percentile

Table 1: Selected Home Prices, Fair Market Rents and the Affordability of Homes, by County

Main City	County	Home Prices 25th, Case-Shiller Updates	Fair Market Rent-3 Bedroom	Difference Between FMR and Interest, Taxes, and Insurance
Detroit	Wayne County, Michigan	$58,631	$968	$627
Dallas	Dallas County, Texas	$83,756	$1,201	$683
Cleveland	Cuyahoga County, Ohio	$85,533	$890	$384
Tampa	Pinellas County, Florida	$90,274	$1,199	$741
Phoenix	Maricopa County, Arizona	$99,309	$1,277	$796
Atlanta	DeKalb County, Georgia	$114,194	$1,069	$472
Charlotte	Mecklenburg County, North Carolina	$116,522	$954	$336
Minneapolis-St. Paul	Ramsey County, Minnesota	$122,798	$1,143	$508
Las Vegas	Clark County, Nevada	$123,030	$1,408	$810
Miami	Miami-Dade County, Florida	$125,449	$1,479	$833
Chicago	Cook County, Illinois	$141,332	$1,227	$454
Denver	Denver County, Colorado	$156,097	$1,265	$507
New York City	Bronx County, New York	$171,257	$1,615	$776
Portland	Multnomah County, Oregon	$171,800	$1,178	$269
Washington, DC	Prince George's County, Maryland	$194,306	$1,647	$653
Seattle	King County, Washington	$249,134	$1,395	$119
San Diego	San Diego County, California	$265,383	$2,067	$791
New York City	Queens County, New York	$266,372	$1,615	$319
Boston	Suffolk County, Massachusetts	$268,879	$1,609	$265
Los Angeles	Los Angeles County, California	$269,830	$1,828	$529
San Francisco	San Francisco County	$373,586	$2,213	$416
New York City	New York County	$424,066	$1,615	-$423

Source: Tabulations by author from the 2007 American Community Survey, the Case-Shiller indices and HUD data on Fair Market Rents. The Case-Shiller updates incorporate data through the second quarter of 2009.