HOUSING POLICY INNOVATION THROUGH EFFECTIVE EXPERIMENTATION

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EXECUTIVE SUMMARY

Broadway plays open out of town.
Baseball players play spring training; football has exhibition games.
Software developers send out free or cheap beta test versions of software.
Fast-food chains test-market new menu items.
New pharmaceuticals go through extensive FDA testing.
Hollywood movies open in Canoga Park before final editing.

In many fields of human endeavor, designers use piloting or experimental approaches because they have found that no amount of knowledge-based analysis can replicate the practical insights gained from interacting with real customers in a real marketplace. Yet among these crucial fields, legislative policymaking and program development do not systematically incorporate piloting and experimentation even though the consequences are every bit as sweeping in scope and often longer-lived in time. Even within the narrower public-policy universe of affordable housing, piloting and experimentation are often haphazard. Why is this so, and what can we learn from housing pilot programs used, consciously or not, throughout the US? Two primary questions regarding affordable housing pilot programs form the focus of this PAE:

I. When is an experimental approach appropriate? What are the conditions that signal it is appropriate?

II. Assuming the decision to create a pilot or demonstration program has been made, what factors contribute to its success and what to its failure?

In order to create a factual and anecdotal basis for a response to these questions, the development of five affordable housing programs in the United States is outlined in terms of their relevance to an experimental approach to housing policy innovation.

1. **Section 8 and the Experimental Housing Allowance Program**
2. **Mark-to-Market Demonstration Program**
3. **Urban Development Action Grants**
4. **Low-Income Housing Tax Credits**
5. **Nehemiah Homes Program**

The cases are categorized in terms of where innovation is created on the ladder from local to central government. Cases in which innovation occurred through the management of the program by a central authority are termed more "top-down" while

those in which innovation occurred as the result of independent experimentation by ambitious local organizations are termed more "bottom-up."

I. When is piloting appropriate? Experimentation is appropriate in general under the following conditions:

1. Goals are clear, strategies are not.
2. Multiple goals are desirable, but their interactive achievability is opaque.
3. Useful information will be provided.
4. The pilot will offer broad applicability.
5. No easy alternative exists.
6. Irreversible impacts are considered.

In particular, every experimental approach faces tradeoffs in terms of the challenges it must confront operationally versus its potential to benefit society. A more top-down approach is likely to be fruitful under the following conditions:

7. A strong central authority exists.

With the following advantages:

8. Some programs must be national.
9. The potential for high internal validity exists.

A more "bottom-up" approach is appropriate under these conditions:

10. Central authority is willing to devolve control.
11. Knowledge-sharing institutions exist.
12. Local conditions vary widely and dramatically.

With the following advantages:

13. No burdensome central planning.
14. Easier transition.
15. More politically resilient.

Ii. What factors contribute to piloting success or failure? Experimentation in general is more likely to be successful in general under the following conditions:

16. Policy debate is just beginning.
17. Findings are visible.

And in particular, the cases support the notion that a policy experiment is more likely to be effective in creating new knowledge and understanding the closer it is to the ends of the experimentation spectrum – either highly centralized or highly decentralized. Approaches near the middle of the spectrum are primarily useful as stopgap measures when urgent political issues demand immediate attention.

In addition, a top-down approach is more likely to be effective under the following conditions:

18. The focus is clear.
19. Results are well-communicated.
20. The political landscape is stable.
21. Careful planning is performed.
22. Transition issues are anticipated.
23. Expertise is available.

A bottom-up approach is more likely to be effective under the following conditions:

24. Scaling issues are anticipated.
25. Risk-aversion is mitigated.
26. Expectations are realistic.

Finally, approaches near the middle of the spectrum are likely to be facilitated by the following circumstances:

27. Regulation is minimal.
28. External bureaucratic constraints are minimal.
29. Internal bureaucracy is minimal.
30. Opportunities for innovation are exploited.

INTRODUCTION

Background

Many of the problems that housing policy attempts to address are complex and policymakers often do not have the information necessary to accurately anticipate the impact of a new policy approach. It therefore seems prudent to evaluate new policy proposals through controlled experimentation before devoting the resources necessary to implement them on a large scale. In many situations, there is no close substitute for real-world trial-and-error in determining the effectiveness of a novel line of attack.

In addition, an experimental approach has many advantages over other research designs. For example, the results of a well-designed experiment are more convincing than any predictions based on analysis alone. In addition, the planning and implementation of an experiment forces each detail of a new policy approach to be carefully thought through. The course of an experiment may even reveal flawed assumptions that would never have been questioned otherwise.

Because experimentation can be such a useful tool for policy analysis, the development of a systematic framework for evaluating the decision to experiment and determining how it can best be facilitated would certainly be useful. Towards this end, two primary questions regarding housing policy experimentation form the focus of this PAE:

1. When is an experimental approach appropriate? What are the conditions that signal it is appropriate?

2. Assuming the decision to experiment has been made, what factors contribute to an experiment's success and what to its failure?

This report investigates the factors that make experimentation useful in terms of the factors that are "prerequisites" and observable before the program starts (to answer question 1) and the factors that facilitate the success of an experimental program after the decision to begin has been made (to answer question 2).

Methodology

Approach. This PAE takes a "case study" approach whereby five cases of policy experimentation are investigated using a combination of historical research and

interviews. These cases then form the factual and anecdotal basis from which observations and recommendations can be drawn to shed light on the questions motivating the PAE.

Case Selection. An effort was made to select cases which were distributed in time over the later twentieth century (see Table 1 below) and which had grown large enough that useful observations about their effectiveness could be made. In addition, the cases are distributed in type according to the taxonomy developed below.

Table 1: Case Selection

Case	Year Started
Experimental Housing Allowance Program	1970
Urban Development Action Grants	1977
Nehemiah Homes	1981
Low-Income Housing Tax Credits	1986
Mark-to-Market	1996

Operational Definitions. For the purposes of this PAE, a "demonstration program" will be considered a type of pilot program in which the details of a program's implementation are being piloted, but not the program itself. The term "pilot program" will therefore broadly refer to any type of experimental program.

In addition, this PAE assumes that the goal of a pilot is to provide information that is relevant and useful to the policy problem at hand and that informs policy decisions. The approach that is being piloted doesn't need to succeed for the pilot to be successful, but useful knowledge should be extracted from the approach's success or failure and the process should ensure that this information affects policy formation. A pilot is considered "effective" if it achieves these goals, and a pilot is "appropriate" if it is likely to be effective and there are no similarly effective but cheaper policy tools available.

A Taxonomy of Experimentation

A policymaker can employ many different flavors of experimentation so in order to make sense of the available options, they are categorized below in terms of where innovation is created on the ladder from local to central governments. For example, in a large-scale social experiment like the Experimental Housing Allowance Program (EHAP), innovation is driven from the "top down" by the management of the experiment. Conversely, in an initially small-scale program like Nehemiah Homes, innovation is created by an organized local community from the "bottom up."

Figure 1 illustrates this spectrum of top-down versus bottom-up experimentation in terms of five categories of experimentation on the left and the five cases discussed in this PAE on the right. A point at the absolute top of this spectrum might represent the creation of a large-scale national housing policy by a strong central government after systematic experimentation. A point at the bottom of the spectrum represents the development of numerous small community housing programs without guidance from a central government. Each of the five categories on the left will be described in turn and the position of each category and case along the spectrum will be explained briefly.

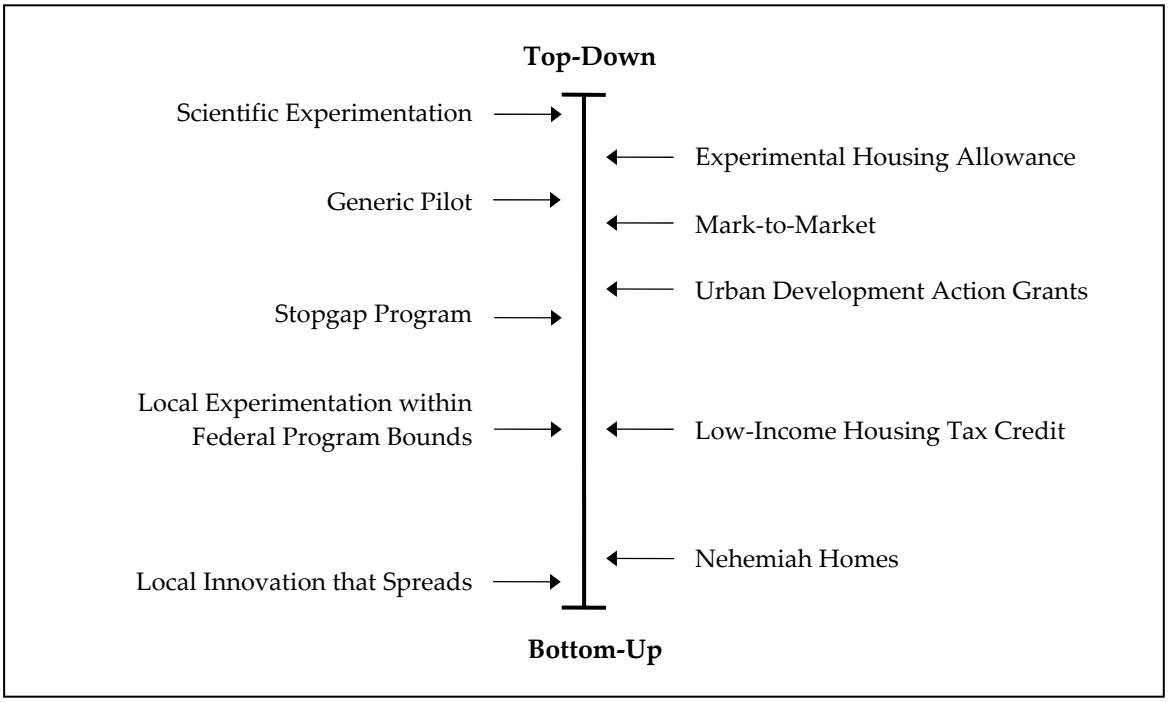

Figure 1: Spectrum of Experimentation in Housing Policy

Note that the size of the experiment is not relevant to this taxonomy, however, and many small-scale federal experiments could also be populated here. Indeed, an extended approach to plotting the history of pilots might involve three dimensions:

- Control: Top-down/ bottom-up, as here.
- Scale: National / small experiments.
- Time: Before, during, or after program development.
- Regulation: Extent of bureaucratic regulation imposed on the process.

Scientific Experimentation. This category represents pure "top-down" experimentation in which a strong central authority performs a systematic experiment that compares the effectiveness of the most reasonable policy approaches. Several treatments are tested and their impacts compared.[1] EHAP is the case that comes closest to this model, but the

federal government was not patient enough and the scientific process was derailed by political forces.

Generic Pilot. A "generic" pilot is one where innovation is managed and created by people who participate in the business arena (as opposed to the managers of a scientific experiment), and it is often not implemented in a scientifically systematic way. For example, there may be no alternative treatments or control group. It may arise in an ad hoc manner as the concept of a new approach gains popularity and acquires enough support to become codified into a pilot. For example, the approach in the Mark-to-Market Demonstration was not being debated, but had gained enough support to become a pilot so the details of the implementation could be worked out. In some sense, every "permanent" program has a similar initial phase where implementation details are unsettled, but the experimentation is not very scientific.

Stopgap Program. A "stopgap" program is created in order to address a problem that demands immediate action. It often involves a small administrative team that works primarily to manage the distribution of resources among local organizations that are attempting to address the problem of interest. Innovation therefore occurs as a result of the administration of the program interacting with local organizations, and the program lies close to the middle of the top-down versus bottom-up spectrum. In a stopgap, as opposed to other pilot forms, innovation may not be recognized as valuable in its own right. UDAG was an effort to contribute federal resources to urban development in response to dissatisfaction with urban renewal.

Local Experimentation within Federal Program Bounds. When a federal program provides resources and creates a set of rules within which state and local organizations have room to try new approaches, innovation occurs more locally. The Low-Income Housing Tax Credit created a large federal program which state and local organizations have taken advantage of in a range of ways that has been much more diverse than anticipated.

Local Innovation that Spreads. At the bottom of the spectrum, housing programs are created by local organizations to address their needs, and the successful approaches tend to be replicated nationwide. The Nehemiah Homes program was the development of a novel approach by a local community group which resulted in a program so successful that it was replicated and became the model for a short-lived national program.[2]

These categories are not meant to represent an exhaustive scientific taxonomy of all policy experimentation but to capture the most common forms. There are many programs that could reasonably belong to more than one of the categories above based on one's interpretation about where innovation occurred. For example, a court-ordered racial desegregation program known as the Gautreaux program formed the basis for the

federally funded and experimentally designed Moving to Opportunity (MTO) for Fair Housing demonstration program.[3] If a federal experiment is based on a local experiment, it is not immediately clear where the responsibility for innovation lies.

In addition, the unit of observation need not be a national government. A local government project that is managed by a strong local authority which uses the program's results to develop its housing policy would lie at the top of the spectrum. For example, a state government might create a social experiment and subsequently roll out a new state program. From the perspective of a federal policymaker, this project lies near the bottom of the spectrum since it represents the development of a new program by a local authority, while from the perspective of a state official attempting to determine how to guide state policy development, it lies at the top.

Each of the cases discussed below represents an alternative approach to policy experimentation and illustrates important characteristics of the spectrum developed above. As each case exists on a different point on the experimentation spectrum, each case also differs in terms of its likelihood for creating innovation and its ability to successfully navigate the political process.

CASE 1: SECTION 8 AND EHAP

Background

Before 1937, the Federal government had little involvement in housing policy, which was left largely to a hodgepodge of charitable organizations, employer programs, and local initiatives. Housing policy in the US first emerged at a Federal level during the 1930's as a response to the economic instability of the Great Depression. The landmark 1937 Housing Act sought not only to stabilize homeownership (via FHA and FmHA) but also to embark on the first great wave of slum clearance and urban blight removal.

Federal intervention began by adopting a primarily project-based approach.[4] Residential construction was subsidized and the housing was then made available to the poor at below-market rents. Unfortunately, this approach was plagued by numerous problems and often criticized for allowing too much of the subsidy to be absorbed by project sponsors and other middlemen before reaching the poor.

Then in the mid-1960's, as political interest in housing policy was again heightened, the failure of construction-based programs began to receive attention due to several infamous disasters such as the Pruitt-Igoe Public Housing Project in St. Louis.[5] Proposals for alternative approaches began to receive serious consideration and legislators began to shift towards the use of housing allowances whereby low-income households are given a direct cash subsidy to enable them to obtain adequate housing.[6]

The Housing and Urban Development Act of 1964 introduced the Section 23 leased housing program in which the government paid the difference between the price of a residential unit leased by a local housing authority and the amount that it determined a low-income household could afford to pay.[7] One important aspect of this approach was that in contrast to government housing project residents, Section 23 program recipients were not necessarily tightly clustered geographically. Section 23 was rolled out without experimentation, but it was always intended to be a small program.[8]

In 1968, President Johnson's Committee on Urban Housing supported a housing allowance program, but indicated concerns about the program causing rental price inflation and the impact of other issues such as racial discrimination on its effectiveness.[9] Therefore, it advocated the development of an experimental program.

Experimentation

In the late 1960's, the housing allowance approach was incorporated to a limited extent into parts of the federally funded Model Cities Program.[10] Then with the passage of the 1970 Housing Act, the Department of Housing and Urban Development set out to organize a set of experiments to answer questions about the creation of a federal housing allowance program. The first experiment to emerge was aimed at investigating the effects of different forms of housing allowances on household behavior and it evolved into the "Demand Experiment."[11] In late 1971, in order to study the market effects of an allowance program, an effort to develop models of urban housing markets was established and became known as the "Supply Experiment." Finally, an investigation into the administration of an allowance program was created, the "Administrative Agency Experiment." By the spring of 1972, the three experiments were planned and labeled collectively as the Experimental Housing Allowance Program (EHAP).[12]

As EHAP was getting started, the nation's economy was heading into recession and the Nixon administration in 1973 suspended many federal housing subsidies for the poor and announced the search for more effective programs.[13] EHAP became an important part of this search, but before it could deliver any conclusions, Congress enacted the Section 8 subsidy program without paying much attention to EHAP.[14] Section 8 was flexible in that it could be used either to promote new construction or to help citizens pay for housing in the manner of a housing allowance.

According to William Apgar, former Assistant Secretary of Housing at HUD, EHAP was part of Nixon's attempt to create a general income transfer program – known then as the Family Assistance Plan. Under this reasoning, housing was seen as an in-kind transfer program. For some, EHAP served to send these demand side approaches off to a study that would never report back, while for others, it was a way to keep the idea alive. Section 8 project-based subsidies were the biggest supply side subsidies of them all with guaranteed rents and generous tax breaks that ensured developers would have to work hard not to profit. The Section 8 existing program was included just to give the appearance of balance.

Outcomes

With a total cost upwards of $163 million (see Table 2), EHAP represented an enormous undertaking and created a landmark within the developing art of policy evaluation through social experimentation.[15] Within the handful of national experiments that the U.S. federal government has organized, EHAP is particularly notable for its ambitious size and complexity.

Experiment	Household Payments	Administration	Research and Monitoring	Total
Demand	3.6	2.0	25.6	**31.2**
Supply	42.5	18.5	41.7	**102.7**
Administrative Agency	9.8	3.4	9.2	**22.4**
Overall Design and Analysis	0	0	6.8	**6.8**
Total	**$ 55.9**	**$ 23.9**	**$ 83.3**	**$ 163.3**
Percentage	**34%**	**15%**	**51%**	**100%**

Table 2: Estimated Cost of EHAP Experiments (in millions) [16]

The program costs allocated to research and monitoring -- 51% of the total funds -- is quite striking, especially as comparison with later programs that allowed little or no cost for such services.

Before the program started, many debates about housing assistance could not be resolved, and there was little confidence in predictions about how many households would participate, how many would move, or how rental prices would be affected. In fact, many of the common assumptions about housing allowance programs were upended.[17] EHAP found that participation would be much lower than expectations drawn from previous limited enrollment housing programs; the incentive of assistance would not be strong enough to encourage many households to move; and rents would not be inflated by the program because of the small number of households that make any significant change to their housing. In general, households were reluctant to move and chose to live in housing of marginal quality in order to save on rent.

Housing allowances were successful in helping families with heavy financial burdens but participating families were reluctant to increase their rent outlays and therefore did not meet HUD's hopes of urban revitalization and increased housing supply. As a result of EHAP and the similar experience of the Section 8 existing-housing program, HUD began to move towards a Section 8 program for new construction and rehabilitation.[18] It became clear that housing allowances were useful for certain goals, but construction-based approaches were still the most effective tool for improving the housing stock.[19] Section 8 currently involves both a tenant-based voucher program and project-based assistance.[20]

At the time Section 8 was getting started in the 1970's, however, the results of EHAP did not affect its implementation in any significant way. According to Edgar Olsen who was a visiting scholar at HUD during the Carter Administration and reviewed the final reports from EHAP, the general success of EHAP facilitated the rapid expansion of Section 8, but since Section 8 was established before the results of EHAP were known, it did not directly affect the implementation.[21] For example, Section 8 certificates were limited to apartments whose rents fell below a market-specific "fair market rent," but EHAP had no such limit. Several years later in 1983, a Section 8 variant – vouchers –

was introduced that reversed the dynamics by allowing renters to live anywhere, but capping their subsidy, so that in effect the renter had a "shopper's incentive".[22] Vouchers started smaller than certificates but eventually the two were consolidated, with the voucher shoppers-incentive principle prevailing.

In addition, the external validity of the experiments has been questioned. EHAP was performed during a period of depressed rental markets, when landlords nationwide were scrambling for tenants and rents were flat or falling. The results might have been very different if the experiments had been performed in the 1990's instead of the 1970's[23] – indeed, voucher utilization rates have fluctuated widely.

Intellectual Echoes. Strikingly, although EHAP by itself was not used to design a new program, EHAP-type principles suffused the Nixon Administration's portable Section 8 proposals that were in fact taken up in law. Since 1985, Congress has given HUD no new production-based programs, but has steadily expanded the supply of portable vouchers. Today portable Section 8 assists over 2.1 million households.[24] Some, such as Edgar Olsen, would indeed trace Section 8's origins to EHAP.

CASE 2: MARK-TO-MARKET

Background

In November 1994, control of Congress passed from Democratic to Republican hands, and HUD began to face significant pressure to rein in its massive budget. One of the fastest growing federal departments in terms of domestic discretionary spending, it had accumulated a total of $223 billion in unexpected budget authority, exceeding even the Department of Defense ($199 billion). Through the successful sale of mortgage loans, HUD was able to improve its budget somewhat, but in November of 1994, a memo by Stephen Kohashi, chief clerk of the Senate VA/HUD Appropriations Subcommittee and thus newly designated senior funder, outlined the overwhelming financial burden faced by HUD, concluding that

> "Funding constraints will make it impossible to maintain the existing inventory in F.Y. 1996, or soon thereafter… Failure to directly confront this budgetary and programmatic problem with a defined strategy and approach will only permit greater losses in affordable housing stock since generally applied annual funding reductions will first devastate public housing, then lead to losses in the Section 8 tenant-based and project-based inventory."[25]

Subsidized low-income housing was the largest component of HUD spending and a practice of renewing expiring Section 8 contracts meant that no units were being eliminated. In addition, many Section 8 contracts were supporting above-market rents which represented not only a significant financial burden but also a threat to the long-term viability of those projects.[26] Late in 1994, it was suggested that expiring above-market contracts would simply not be renewed, but this plan would threaten the viability of the affected projects, abandon a large number of low-income households, and potentially cause a significant number of mortgage defaults.

Some speculated that instead of canceling the contracts altogether, HUD might be able to renegotiate the inflated rents down to market levels. This notion was the essence of an approach labeled Mark-to-Market (M2M), and in April of 1995, David A. Smith of Recapitalization Advisors testified before the Senate on the costs associated with this strategy. He estimated that marking all FHA-insured Section 8 rents to market would cost the federal government at least $8.5 billion comprised of $12.4 billion in claims against the FHA insurance fund and $3.9 billion in recoveries after assignment.[27] The magnitude of federal losses in this estimate were surprising because FHA insurance claims detracted significantly in the short-term from the benefits of lower long-term

outlays due to reduced Section 8 payments. However, it was estimated that $920 million per year would be saved in annual Section 8 subsidies so the program would pay for itself in 9 years or less.

In 1995, HUD ended up facing the problem by attempting to phase Section 8 into a voucher program in the hope the market would correct inflated rents, the efficient projects would survive, and the inefficient projects would either be forced into efficiency or fail. HUD also argued that vouchers, in that they provided rents at FMR, would protect all current residents by allowing them seamlessly to migrate into the purely private markets. Stakeholders on all sides of the spectrum – from far left to far right, with everything in between -- categorically rejected a premise of vouchering out the entire inventory. HUD, meanwhile, was adamant that only on that basis should M2M proceed. Therefore, no legislative action was taken in 1995.

Nevertheless, Section 8 contracts were expiring, forcing the issue. Facing these challenges, Congress adopted a demonstration program, creating a set of options for the first year's worth of expiring contracts, and tacked this demonstration onto the appropriations funding Departments of Veterans Affairs and Housing and Urban Development and Independent Agencies Appropriations Act, 1996.[28]

Experimentation

In effect, the 1995 M2M demonstration was formulated by a handful of people at OMB, HUD, and the Senate, each acting with limited collaboration with the others. The resulting demonstration program was created primarily to experiment with the details of implementation.[29] Foremost among the decisions that had to be piloted was the choice of restructuring agent (eventually termed a Participating Administrative Entity or PAE) because, in the words of David A. Smith, "if you can find the right person to do the complicated open-heart surgery, everything else falls into place."

The three primary candidates were HUD field offices, state housing finance authorities, and private-sector organizations which had a financial motivation to participate. The demonstration program divided up its allotment of Section 8 contracts among the three categories of potential PAEs using an auction structure (with the stipulation that the private-sector participants be non-profit and possess a sufficient set of skills).

Each restructuring was run by a partnership of which HUD was the 90% limited partner and the PAE was the 10% general partner. HUD contributed to the partnership its rights under the mortgages on individual properties whose owners volunteered to go through the program. The potential PAEs bid for their portion of the partnership, but they also received an administrative fee from HUD. Operating under minimal procedural rules,

the PAE's were given significant leeway in developing their own approach to each deal, making the demonstration more "bottom-up" than EHAP.

Outcomes

In 1996, a permanent program was proposed but not passed, and the demonstration was extended for a year. Then in 1997, a statute was enacted that brought more expiring contracts into the demonstration, but did not create a permanent program. During this time the demonstration program was becoming increasingly effective, and the Multifamily Assisted Housing Reform and Affordability Act of 1997 (MAHRA) finally established M2M as a permanent program which became effective in time for Section 8 expirations occurring in fiscal year 1999.[30]

The demonstration program was valuable for working out the details of the implementation of the permanent program even though the overall programmatic outcomes were never debated and the permanent program began before there was much time to evaluate the results of the demonstration.[31]

Intellectual Echoes. Beyond the original M2M, mark-to-market principles are spreading their way throughout the HUD inventory. Even before M2M had fully rolled out, Congress and HUD concluded that if marking rents *down* to market made sense, so too should expiring contracts have the opportunity to go *up* to market, and HUD introduced the Mark Up to Market (MUM) program, and its non-profit corollary, Mark Up to Budget (MUB). Similar principles are influencing the Section 8 voucher debate today, and the proposed Public Housing Reinvestment Initiative. So concepts are being applied broadly that were first pioneered in M2M.

CASE 3: URBAN DEVELOPMENT ACTION GRANTS

Background

In the 1960's, dissatisfaction with large-scale urban renewal projects began to grow and by the early 1970's, many major cities had developed an established opposition to urban renewal campaigns. Many projects were criticized for displacing low-income communities in order to provide land for the private development of office buildings, hotels and convention centers.[32] In addition, the inflation and economic recession that developed during the Ford administration compelled federal policymakers to search for new ways to reduce unemployment and stimulate economic activity.

In response, the Housing and Community Development Act of 1974 created the Community Development Block Grant Program (CDBG), an attempt to combine six categorical urban programs (urban renewal, Model Cities -- itself a superannuated pilot, water and sewer facilities, open space, neighborhood facilities and public facilities loans) into one local government block grant program.[33]

CDBG was shrewdly positioned politically: it received *liberal* support because it compelled local governments to reduce poverty, and *conservative* support because it placed substantial control in the hands of private investors while also reducing the role of government.

During its first few years, CDBG was criticized for not getting enough program dollars to its intended low-income beneficiaries and the perception emerged that additional funding would need to be available for cities to create any substantial redevelopment. Patricia Harris, the HUD Secretary at the time, testified before Congress in support of an additional grant program:

> "Local government, like a business, must be able to move quickly to take advantage of opportunities for coordinated economic and community development when and where such opportunities arise... I am proposing initiation of an urban development action grant program...to provide this much needed capability."[34]

Experimentation

In 1977, amendments to the 1974 Housing and Community Development Act revised CDBG and authorized the Urban Development Action Grant Program (UDAG). Seen primarily as a complement to the revised CDBG, UDAG was intended to provide larger grants for larger projects awarded competitively to "severely distressed" areas.[35] The grants were given to cities to be distributed as loans to urban development projects, and as the loans were repaid, the funds were used to finance additional projects. As illustrated in Figure 2: UDAG's Intended Impacts below, the grants were intended to ultimately benefit the city by increasing the tax base, creating jobs, improving the housing supply, and spurring other economic activity.

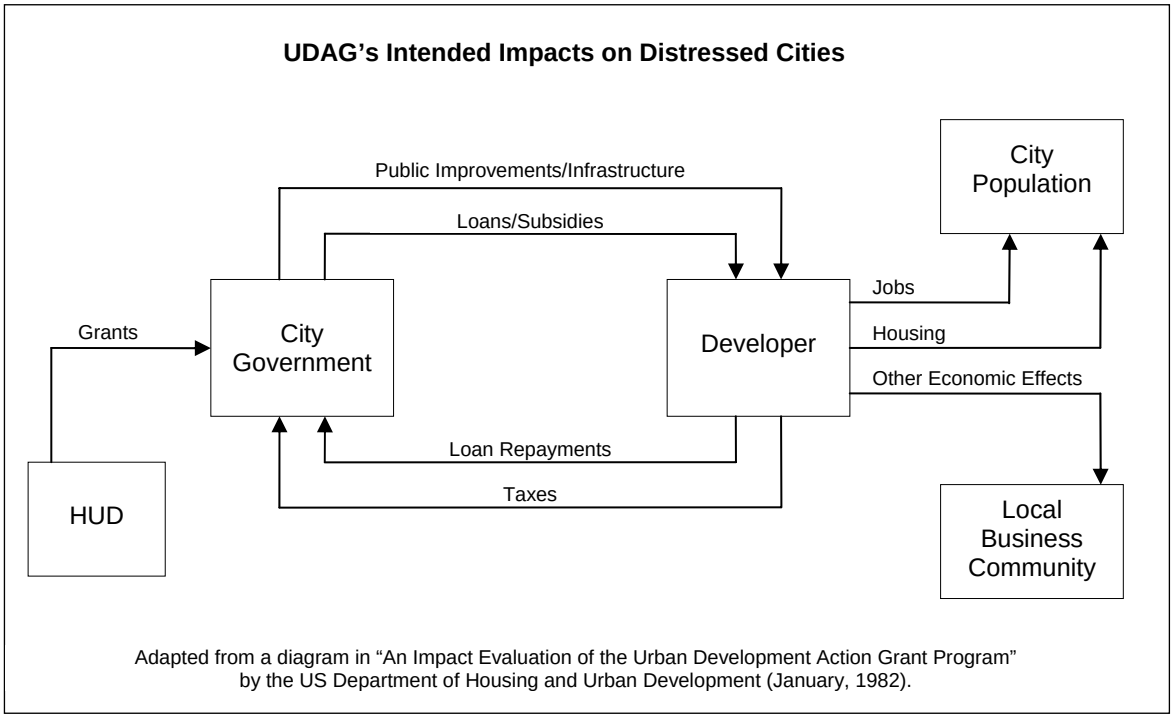

Figure 2: UDAG's Intended Impacts

UDAG was uniquely unburdened by regulatory constraints, and it therefore started very quickly. The only regulations to significantly impact the program's administration pertained to the eligibility of cities for grants (based on poverty indices) which became important because there was significant demand for the grants. The rest of the regulatory framework surrounding UDAG consisted primarily of guidelines. For example, there was a rule that grants should be split evenly between residential, industrial, and commercial projects but this became primarily a guideline.

The minimal regulatory burden contributed to the effectiveness of the program for several reasons. First, the staff was small so that operations could be closely monitored and the benefits of flexibility outweighed the benefits of procedural safeguards. "The quality control was in the hiring and not in the regulations."[36] Second, the staff was exceptionally competent so regulations designed to prevent basic mistakes were not necessary. Third, administration was centralized so leadership could maintain tight control without having to resort to regulatory oversight. Finally, the program's project portfolio grew very quickly and defining a set of rules to govern the administration of such a varied group of projects represented a much tougher challenge than maintaining the quality of the staff.

Because of the small regulatory burden, the UDAG administrators could act as a "private investment house in the bowels of HUD."[37] This flexibility became a significant advantage over other programs which were effectively "paralyzed" by regulatory oversight. However, it also meant that the administrators were responsible for developing their own internal policy to guide project decisions consistently. "There was the challenge of being fair and balanced while making up our own rules because there were no rules."

For example, UDAG administrators came to the conclusion that cities should not be given money to invest directly. In almost all cases – except subsidized affordable housing – the deals did not require direct grants to proceed. Instead, subordinate debt or equity were often enough to make the projects viable. By focusing on what was really needed to implement a project, UDAG was able to better allocate its resources, and this approach became one of the cornerstones of urban development, creating the "but-for" rule: "But for the support of UDAG, this project would not go forward." UDAG was unique in that grant agreements involved contractual enforcement that prevented the private sector from pulling out of a project and incorporated a "but for" clause which required a judgment by federal officials that the project would not have occurred without UDAG funds.

A significant portion of the development ideas that received UDAG support were first conceived in the private sector and a larger portion without a preconceived interest in UDAG funds.[38] Typically the first person to identify a project idea as a UDAG candidate was a city official. The Washington UDAG staff provided assistance and guidance in making project applications more acceptable for funding, often taking a direct role in negotiating with private developers.

Outcomes

UDAG played a prominent role in federal urban policy and was somewhat successful in assisting distressed cities and urban counties in promoting economic development. A

1982 impact evaluation of UDAG by the Department of Housing and Urban Development indicated that the program had been "substantially fulfilling its mandate."[39] UDAG projects were generating more private investment than expected and about the same amount of housing as anticipated. Relatively little resident displacement occurred and substantial financial and relocation assistance was provided. In the words of Charlie Kendrick who worked in the UDAG office at HUD during the early 1980's, "UDAG is a fantastic example of how you take something from a standing start and turn it in a short period of time into a very effective federal program."

Created by Carter's liberal Democratic administration, it was able to maintain political support under a conservative Republican administration. Since there were enough UDAG's awarded that most states had one, it had the resources to win political popularity. In addition, the program was one of the first examples of a "fast-track" program that made grant application decisions very quickly so it was extraordinarily flexible in surviving a changing political landscape.

UDAG grants also enabled and inspired new approaches invented by local officials to solve their unique combination of issues. Over thirty million dollars of UDAG funds subsidized the New Homes Program of New York City in the 1980's.[40] New Homes attempted to leverage limited public investment through private construction and financing to create a novel public/private partnership model. The program ended up being so popular that it became a national model, inspiring similar projects in Puerto Rico, Hawaii, and New Jersey.

Several state and local housing development programs were also created that provide project-specific capital grants or other kinds of front-end construction cost write downs as would be required to make a project financially feasible.[41] Using vernacular popularized by the UDAG program, these programs often use the "but-for" test. Many states adopted them as their primary production vehicles. The upfront subsidies make them look expensive in the short-run, but they are more cost effective than continuous subsidy projects over the long-run, and they are also more flexible. Maryland and Hawaii both created similar programs.

The results of UDAG did not quite meet the original expectations, however. According to the 1982 HUD assessment, only seventy-seven percent of the anticipated employment and fifty percent of the anticipated tax revenues were generated.

Given that many of the benefits of UDAG developments are indirect and long-term, however, measuring the aggregate economic impact of the program is difficult and individual measures must be incorporated into a holistic evaluation.

When projects failed to achieve anticipated benefits, it sometimes meant that the project probably could have proceeded without UDAG funds or overly optimistic predictions

were made, but it was more often because of unforeseen financial problems. Due to changes in the national economy or the risks inherent to development, about one in ten projects faced a problem serious enough to jeopardize its success (as of June, 1981).[42] Doubts about the effectiveness of the program were compounded by frequent objections to its spatial impact and the political nature of the contract negotiations.[43] In some instances federal funds were awarded for projects that would have been completed without the funds, and estimates of anticipated benefit were overstated in some circumstances.

Under the Reagan administration, conservatives denounced the UDAG program for subsidizing development that would have occurred anyway and its legitimacy was repeatedly questioned.[44] In response to constant criticism, the program's goals were forced to broaden from a focus on physical distress to economic distress in general, and the program's eligibility requirements were broadened such that by the 1980's over 50% of the largest cities qualified as "severely distressed."[45] Emerging from a perceived need to broaden the distribution of federal funds to maintain political support for the program, these changes diluted the program's effectiveness but maintained its appropriations until 1988.

Intellectual Echoes. Unlike UDAG, CDBG continues today – as does HOME, a local-level block-grant funded gap financing source. Low Income Housing Tax Credit allocators tacitly adopt a but-for approach to sizing their resource awards. For three years running, the Administration has proposed block-granting Section 8 vouchers entirely, in exchange for substantial deregulation of process. All these principles are in effect extensions of ideas first used widely in UDAG.

CASE 4: LOW-INCOME HOUSING TAX CREDITS

Background

Before 1986, rental real estate had provided attractive tax incentives to investors through lenient allowances for depreciation; these allowed investors either to shield cash flow from tax, or even (predominantly) to take taxable non-cash deductions. As a result of this tax shelter benefit stream, investors were willing to provide equity contributions, typically ranging from 20-25% of total development cost, into new construction and substantial rehab affordable housing properties even though these properties would have fifteen to twenty years of regulated operations with minimal projected cash flow return.[46]

But by the early 1980's, the use of non-cash deductions, especially accrued but unpaid interest, was criticized as an uncontrollable loophole tax expenditure, and it was difficult for housing advocates to distinguish Federally mandated advantages for affordable housing from the larger tax shelter boondoggle. In response, the Tax Reform Act of 1986 significantly reduced many property tax benefits, primarily by reducing the allowable rate of depreciation and creating passive-loss rules. In addition to reforming general real estate tax incentives, the Act aimed to improve incentives for low-income housing and created the Low-Income Housing Tax Credit Program (LIHTC).

> "There was not a lot of foresight to the housing credit… there were no hearings or proposals – someone had just suggested it at some point and the idea made it into the final bill. In the beginning, it was rolled out on a temporary basis, but at a large scale… There was a lot of satisfaction with the previous program, and the idea was to more tightly tie the grant of tax benefits with the policy of encouraging affordable housing development."[47]

Experimentation

LIHTC provided tax credits to owners of housing occupied by households with less than fifty to sixty percent of the area median income.[48] LIHTC also requires that a minimum of ten percent of the funds allocated to each state support projects developed by local non-profit corporations.[49] Because non-profits are tax-exempt, however, they must partner with for-profit investors who then gain a vested interest in the success of the project.

The program gives states general guidance on how to consider needs and costs, but the states are required to have an allocation plan that identifies the states' priority housing needs and contains selection criteria for awarding credits to help those in need. The state agency is required to evaluate projects based on the reasonableness of development costs and the sources and uses of project funds.

After a state allocates credits to developers, the developers typically offer the credits to private investors who use them to offset taxes otherwise owed. The private investment enters the project as equity financing to fill the gap between a project's development costs and the non-tax credit financing sources available. Investors can claim the credits to offset taxes for each year of a 10-year period called the "credit period" as long as a minimum percentage of the projects' units are rented to low-income tenants at affordable rents for a 15 year compliance period.

State agencies are also responsible for monitoring the projects for compliance with federal requirements concerning household income, rents, and habitability. In dealing with issues of noncompliance, the IRS may recapture or deny credit for previously used for issued tax credits. In addition, the IRS regulates state monitoring requirements and requires annual reports from the states on the amount of tax credit allocations mad in total and amounts awarded to individual projects.

Outcomes

Representing a novel application of the tax credit subsidy approach, the LIHTC quickly became a fundamental financing tool for multifamily affordable housing. A 1997 evaluation of the LIHTC prepared for the National Council of State Housing Agencies reported that the program was remarkably prolific, having created over 900,000 apartments while becoming more efficient and cost-effective over time.[50] It serves tenants with average incomes well below the maximum income levels permitted under Section 42, and increased competition has created apartments that will remain affordable for longer periods of time. In addition, the structure of the program gives states a strong incentive to negotiate better affordability and it creates benefits that demand-side programs like Section 8 cannot.

The Credit has also evolved considerably in the process. It is so flexible that it has come to be used in a variety of projects, and feedback from States has encouraged its development. In a 1997 analysis, the GAO reported that projects varied widely in resident and property characteristics as well as the cost to build the projects.[51] Monitoring procedures vary from state to state. The developments varied from urban to suburban, garden-style to high-rise, and from new construction to rehabilitation. The states were allowed wide latitude under which to define and weight the credit award selection criteria and they exhibited significant variation in their implementation.

In addition to being flexible, the Credit serves to complement the other financing sources available to affordable housing projects. A 2003 report by HUD on projects placed in service through 2001 indicated that units developed in the program received a broad array of other federal, state, and local assistance, and the credits were put to a wide array of diverse uses.[52] However, the more complex deals which packaged subsidies from a variety of sources needed to be monitored carefully for their cost-effectiveness and possible over-subsidization.

Intellectual Echoes. Today the LIHTC is the country's dominant form of Federal assistance for affordable multifamily housing production – as much as 90% or more of all affordable production accesses it in one form or another. The program has been made permanent, increased (from $1.25 to $1.75 per capita), and indexed for inflation. More than a dozen states have developed state-level tax credits that piggyback onto the Federal credit, an intriguing example of idea proliferation and additionality anchored by the Federal credit.

CASE 5: NEHEMIAH HOMES

Background[53]

During 1960's and 70's, New York City underwent a number of significant demographic changes. The population of Manhattan increased twenty percent while also becoming significantly poorer. In addition, the repercussions of falling employment in the areas surrounding Manhattan could be witnessed in the condition of the housing stock and standard of living. In this environment of decline, traditional approaches to public housing seemed to be failing.

Critics argued that focusing scarce resources on the most needy was exacerbating the problem and subsidizing only rental housing was depriving low-income households of the benefits of homeownership. A subsequent decline in federal support for affordable housing in the 1970's forced concerned citizens to search for new approaches to addressing their housing needs.

In addition, during the mid 1970's New York City underwent a severe fiscal crisis which precluded any significant financial contribution to affordable housing projects. However, the City did possess significant amounts of land acquired through foreclosures, and much of this land was in areas that would benefit from affordable housing, providing some opportunity for the development of new projects.

Experimentation

In 1981, a New York City community group called the East Brooklyn Churches (EBC) was having some success organizing its constituents and reviving their neighborhoods. It hoped to have similar success in tackling the community's problems with a poor housing stock so EBC contacted retired builder I. D. Robbins to help organize the effort. As a writer for the *New York Daily News*, Robbins had described plans to develop brick rowhouses that would be affordable to households earning as little as $12,000 per year. His extensive experience in construction and City politics lent weight to the promise of his plan.

The lead organizer of the EBC met with Robbins and promised to raise twelve million dollars for the project. The two then worked out a set of principles that would guide the Nehemiah Plan, named after the biblical official who restored the city of Jerusalem from a state of desolation.[54] First, they would construct only owner-occupied single-family

homes because Robbins believed that "single-family homeownership encourages stable and responsible family living." Second, the homes would be built as long tracts of townhouses to reduce construction costs and create whole new neighborhoods. Robbins drew his inspiration from Levittown, an enormous development of suburban homes built to house the growing families of soldiers returning from World War II. Finally, direct government grants would not be accepted to avoid a sense of charity and maintain more control over the program.

The project acquired financial contributions from various religious groups, and the substantial community support enjoyed by EBC provided the project with political capital sufficient to win support from the City in the form of interest-free loans, tax deferral, and free land. In October 1983, the first building permits were issued, and in June 1984 the first homeowners moved in.

Outcomes

By the middle of 1993, the project was perceived to be a substantial success. Over two thousand homes had been constructed in Brooklyn, and they were occupied exclusively by first-time homebuyers with minimum incomes of $20,000. Many of the residents were members of EBC congregations who heard about the program though their participation in the group and many also came from public housing projects.

Nehemiah's success in Brooklyn inspired similar developments not only in the nearby South Bronx, but also in Baltimore, Los Angeles, and Philadelphia. The model went national when Congress passed the Housing and Community Development Act of 1987, creating the Nehemiah Housing Opportunity Grant Program.[55] Nonprofit organizations were given grants to assist moderate-income families in becoming homeowners of newly built or rehabilitated housing in lower-income areas. Assistance was provided in the form of interest-free second mortgages of not more than $15,000. For fiscal year 1989, appropriations were authorized for $100 million for the program. Not all elements of the New York program were incorporated into the federal version, however. For example, the grass-roots organizing approach to getting the City to donate free land seemed to disappear in favor of what seemed to be more of a regular loan program.[56]

Despite its success, the program was not free from controversy. Critics complained that some households were displaced to make room for Nehemiah's continuous-tract construction, a common complaint of urban many renewal programs. More significantly, the townhouse construction reduced the density of residential areas that were designed by city planners to support greater public service utilization. In response to fears that infrastructure underutilization would undermine the cost-effectiveness of the program, Nehemiah eventually agreed to build three-story condominiums in certain areas.

In the end, Nehemiah was successful in building the homes necessary to encourage community revitalization, but the communities that Nehemiah was trying to help were facing a combination of social ills that one program could not resolve. The national program was short-lived, terminated in the Cranston-Gonzalez National Affordable Housing Act of 1990 under the presumption that its purposes would be better served through the HOME program.[57]

Intellectual Echoes. In effect, Nehemiah has not been terminated, in that it contributed to the creation (with national funding) of the HOME program, which persists today and remains popular.

RECOMMENDATIONS

This PAE is fundamentally motivated by the problem of how to acquire the knowledge and understanding necessary to make an informed decision about how to confront a set of complex issues. When the situation is too complicated to sort through analytically or critical data does not exist, some form of policy "experimentation" is necessary to acquire enough knowledge to make intelligent choices.

Since all policy experimentation can be placed somewhere on the spectrum of experimentation developed earlier and the manner in which a project is managed has meaningful implications for its appropriateness and likelihood for success, the rest of this paper will focus on the differences between idealized top-down and bottom-up approaches. In analyzing any particular program, these recommendations should be weighted in terms of how close the project is to the top or bottom of the spectrum.

Question I: Appropriateness

Returning to the first question motivating this PAE, experimentation in general is appropriate under the following conditions:

1. Goals Are Clear, Strategies Are Not. When a serious policy problem is demanding attention but the situation is too complex to resolve analytically or important information is missing, policy goals may be clear but it may be impossible to make an intelligent decision about how to achieve them. Policy experimentation provides a tool for discovering the potential of new approaches and comparing their effectiveness. For example, when EHAP was created, there was a clear desire to improve access to decent and safe housing, but more information was needed to make an informed decision about whether a housing allowance would be likely to help achieve that goal.

2. Multiple Goals Are Desirable, but Their Interactive Achievability Is Opaque. Resolving any one political issue may involve pursuing several distinct goals, but understanding the interactions involved in simultaneously attempting to achieve those goals is a difficult analytical problem. Policy experimentation allows a policymaker to explore the interaction between the various issues and remedies involved in a policy problem, and make a more intelligent decision about the best way to proceed. For example, M2M involved a large set of interacting goals whose interactions were difficult to anticipate. Underwriting was a difficult and risky job so each PAE should be qualified, but a high volume of properties needed to be addressed quickly and HUD would keep costs low by opening the bidding process as widely as possible. Policymakers chose to qualify bidders individually before allowing them to bid and to

create a partnership that shared financial risk between each PAE and HUD, and the approach turned out to be successful, but the right way to deal with each set of interacting goals was not clear at the beginning.

3. Useful Information Will Be Provided. In order for an experiment to be useful, it must provide information that is important to a policy debate. Richard P. Nathan, a Professor of Political Science and Public Policy at the University of Albany, argues that "demonstration studies are most effective when policymakers care about a particular issue, are genuinely uncertain about how to handle it, and are willing to wait for the findings of a research project." [58] Incorrectly assuming that policymakers will be interested in the results undermines the potential of many well-intended experimental projects. For example, Congress didn't wait for the results of EHAP to enact a voucher program because it was not really interested in the results.

4. The Pilot Will Offer Broad Applicability. The utility or robustness of conclusions reached in an experiment depends on the breadth of other environments (up to 100%, fully national in all environments) where those conclusions still yield useful results. Experiments that work only under narrowly controlled circumstances have dubious validity. For example, Nehemiah was not as successful outside of New York in part because no other place will have the same mix of individuals in terms of age, gender, race, social attitudes, religious affiliation, or numerous other factors. Similarly, EHAP succeeded but was tested only under ideal conditions for it to succeed -- when markets were soft and landlords were hungry -- without testing under more challenging circumstances. This argues for diversifying the sites for experiments (as the M2M demonstration did) to reveal variability of goal achievability.

5. No Easy Alternative Exists. If the solution can be readily obtained, it is too easy to warrant a pilot; if the input variables or task complexity are low, it does not require the overhead of putting in place a proper experimental structure. An experiment should yield information that could not have been more cheaply or easily procured through other means. For example, Harvey S. Rosen and others argue that if the goal of EHAP was to obtain new and improved estimates of the behavioral response to housing allowances, an experiment was not necessary and the money would have been better spent augmenting conventional data sources. [59] However, it is unclear whether conventional data sources would have been able to so thoroughly document the behavior observed during EHAP.

6. Irreversible Impacts Are Considered. Experimental programs by definition have a real-world impact, and the extent of this impact should be fully anticipated since the potential to detrimentally affect whole communities is very real. For example, the Supply Experiment raised concerns among local officials that it might impact the local housing market in ways that would be difficult to reverse if the program would have to be wound down. Officials in Brown County, Wisconsin worried that inflation would

occur and that the county would become a "magnet for the poor" attracting people in need of housing relief.[60] These concerns should be expressed and carefully considered.

Assuming that these conditions are met, we now consider the circumstances in which different types of experimentation are appropriate, first turning the appropriateness of a top-down approach.

The Top-Down Approach

Appropriateness

7. A Strong Central Authority Exists. An approach closer to the top of the spectrum is appropriate when there exists a central authority strong and patient enough to see a systematic experiment through its full course. It requires months to plan, assemble the staff, pretest the procedures, and implement a systematic policy experiment. The program must then run for a sufficiently long period of time that useful data is collected, and it may have to be modified along the way. Analysis and interpretation of results again take several months and political forces must remain sufficiently aligned throughout this process such that useful knowledge is gained and that it informs policy formulation. After all, if policy is never influenced by the experiment, it is a failure.

Advantages

8. Some Programs Must Be National. Some policies cannot be created at the community level because some degree of national coordination is necessary. For example, a municipal government might not have the resources to enact a meaningful housing allowance program or the program might have macroeconomic effects on housing prices that would not emerge until the program was replicated widely enough. A national experiment would have access to the necessary resources and might operate on a scale large enough to capture some macroeconomic effects.

9. The Potential for High Internal Validity Exists. Experimental programs are touted for their strong internal validity in comparing program impacts because random assignment, if correctly implemented, ensures that treatment and control groups will differ by chance alone.

The Bottom-Up Approach

Appropriateness

10. Central Authority Is Willing to Devolve Control. While a top-down approach requires a strong central authority, a bottom-up approach requires a central authority willing to devolve control to state and local governments. Local organizations clearly require access to the resources and authority necessary to create innovative programs, and a dominant central authority can stifle their efforts. In the U.S. during the 1980's, the federal government significantly withdrew resources and reshaped commitments to housing policy.[61] Building on a history of strong local authority, more aggressive state and local governments began to take a role in providing affordable housing by creating their own programs.

LIHTC is a good example of devolved control because it is not specified by housing statute but by Internal Revenue Code. It therefore is free from much of the regulatory burden that would face a statutory program, and in practice, many issues are either precisely specified by the Code or left wholly to the States. This leaves the States with substantial room to determine what is appropriate for them and experiment with new approaches.

11. Knowledge-sharing Institutions Exist. In order for bottom-up experimentation to be effective, successful programs must replicate and knowledge about successful approaches must have ways to spread. As another consequence of diminished federal involvement in housing policy in the 1980's, private foundations became more aggressive in their efforts to develop a network of nonprofit housing developers.[62] In particular, the Local Initiatives Support Corporation (LISC) and the Enterprise Foundation were created specifically to address the issue of capacity-building in the nonprofit sector and both organizations provide financial and other assistance in support of neighborhood-based housing. A system of local intermediaries also began flourishing at this time, encouraged by national and local foundations and local governments. In the U.S., a history of strong local authority and retreat from housing policy by the federal government encouraged the growth of a network of institutions that are enabling bottom-up innovation.

12. Local Conditions Vary Widely and Dramatically. When local conditions vary widely, a bottom-up approach encourages local organizations to create programs that meet their unique combinations of needs. For example, the Nehemiah Homes program developed to address community development during a time of meager local financial resources, and instead of financing, the City provided land to support the project. A top-down program might restrict roles such that a program becomes less able to deal with widely varying circumstances.

Advantages

13. No Burdensome Central Planning. The primary benefit of a bottom-up approach is the lack of any central planning necessary for the process to occur. As long as the necessary knowledge-sharing institutions are in place, no central guidance is needed. In fact, the process produces a wider variety of information the more freedom it is given.

14. Easier Transition. In contrast to large-scale national projects, there are fewer administrative issues involved in the transition to a mature, large-scale program. Successful approaches are replicated and as earlier programs mature, the lessons they learn will spread to those that follow. The only issues involve unanticipated macroeconomic effects of the scale-up – for example, real estate price inflation from a rental allowance.

15. More Politically Resilient. The experimental process is more resilient to a changing national political landscape because only local interest is required to maintain a program and local politics involve a smaller set of political forces that is easier to keep pinned down. William Apgar, former Assistant Secretary of HUD, believes that grassroots efforts are more resilient to change not because politics is less intense locally, but because local groups are often more nimble than larger national entities. Indeed, because the tasks they face are highly complex, they are able to work only at small scale solving their individual combination of problems. A "laboratory" consisting of hundreds of similar experiments, each acting independently, creates a rich body of information from which a national decision-maker can infer principles. The national decision-makers have to worry more about setting precedents that have implications for entities in diverse communities across the country while local officials can settle on changes that simply solve the problem at hand.

Conclusion

Every experimental approach faces tradeoffs in terms of the challenges it must confront operationally versus its potential to benefit society. A more top-down approach is likely to be fruitful in the presence of a strong, patient central authority that can effectively manage it while a more bottom-up approach is appropriate in the presence of a central government willing to provide local authorities with the control and freedom they need to explore new methods.

Question 2: Effectiveness

Turning to the second question motivating this PAE, experimentation in general is more likely to be effective if the following conditions hold:

16. Policy Debate Is Just Beginning. Experiments have a better chance of informing policy decisions if they are developed early in the policy process when policymakers are uncertain about the impact of potential alternatives and "policy windows" are open. In addition, to compensate for the lag between an experiment's planning phase and the publication of results, an early starts helps to ensure that the information will affect policy.

17. Findings Are Visible. The more policymakers are aware of knowledge gained through recent experimentation, the greater the chance that the knowledge will inform policy formulation. Top-down projects should focus on the clarity and dissemination of their research findings while successful bottom-up projects should similarly work to spread word of their achievements. It has been suggested that the advocacy of research results may be crucial to the use of the findings.[63]

Top-Down versus Bottom-Up

In terms of which experimental types are more likely to be successful, the cases support the notion that a policy experiment is more likely to be effective in creating new knowledge and understanding the closer it is to the *ends* of the experimentation spectrum.

As an experiment slides down from the top of the spectrum, control of the innovation process slips from the hands of the scientists managing the experiment into the hands of those involved in the day-to-day operation of it. This is harmful because the process becomes less scientific and those in charge of innovation are likely to be too close to the action to have a good grasp on the big picture. In addition, one might think that the day-to-day experience of running a program would provide a sufficient basis for improving it, but an operating program often does not involve a broad enough variation in approaches to allow conclusions to be drawn about alternative combinations of approaches.[64]

Conversely, as an experiment creeps up from the bottom of the spectrum, resources begin to come under the control of the central government which both limits the scope of new innovation and creates room for national politics to hijack the experimentation process.

Unfortunately, approaches near the middle of the spectrum are the most politically feasible because they offer the most flexibility in meeting the short-term desires of influential political constituencies. The collaboration between central and local authorities creates local political support by sending national resources to local organizations and central political support by ensuring centralized control over the process. At the top of the spectrum resource distribution is influenced minimally by politics because the process is managed by a strong central authority and local organizations are likely to resent their lack of input. At the bottom, only local resources are in play and the central government relinquishes control to local authorities.

Figure 3 illustrates the tradeoff. The likelihood for effectively creating innovation is highest at the top and bottom of the spectrum while the political feasibility of a project is highest in the middle.

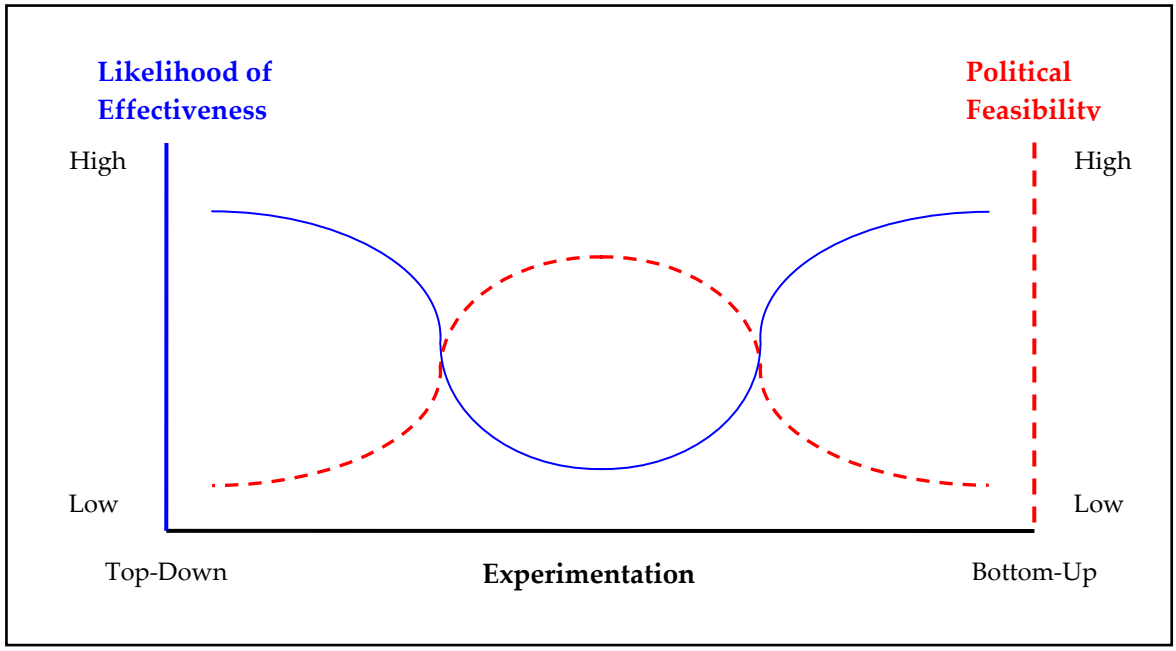

Figure 3: Tradeoff between Effectiveness and Feasibility

Therefore, once the decision to pilot has been made, a national policymaker should determine which side of the spectrum would be most feasible given the nature of his or her governmental structure (strong central versus local authority) and then attempt to create a program as near as politically practical to either end of the spectrum.

In terms of each end of the experimentation spectrum, the specific attributes which contribute to a project's success are described below.

The Top-Down Approach: Attributes of a Successful Program

18. The Focus Is Clear. The Supply Experiment was aimed at both evaluating the effectiveness of a housing allowance program and at providing data for basic housing market research. Combining these goals brings some drawbacks, however.[65] The data may not be ideally suited for basic research since the behavior of the market was affected by the allowance program. In addition, the administrative burden involved in collecting the extra data made program evaluation more difficult, delaying results and hindering the ability to improve policy formulation. Furthermore, any dilution of the focus can create the perception of ulterior motives and threaten political support.

19. Results Are Well-Communicated. Policymakers are not skilled at interpreting the results of a complex research project. It is therefore vital that either skilled policy analysts are available to translate the results of an experiment into understandable terms or the experiment is deliberately structured so that its results have clear implications. Like EHAP, many experiments involve a confusing variety of treatment options – sometimes because of a lack of agreement about the most reasonable options and other times because an experiment's scale attracts the interest of advocates for a wide variety of treatments.

20. The Political Landscape Is Stable. Maintaining the alignment of political forces necessary to see a top-down experiment through to fruition is difficult for the leadership of any nation but seems particularly tough in the constantly changing environment of a modern democracy. Nicolas Retsinas of the Joint Center for Housing Studies believes that the era of US large-scale federal experimentation in housing is behind us because the Executive no longer enjoys the political patience necessary to see a housing policy experiment through. In the absence of strong central leadership, it is unlikely that a top-down project would be able to endure the changing tides of Congressional politics.

Anthony Downs, a Senior Fellow at the Brookings Institution, believes that maintaining political alignment and interest is a problem in any democracy.[66] Conditions present at the beginning of a program lasting several years are not likely to be around at the end of it. Downs argues that "public attention rarely remains sharply focused upon any one domestic issue for very long – even if it involves a continuing problem of crucial importance to society," and instead there is a systematic "issue-attention" cycle where a problem "suddenly leaps into prominence, remains there for a short time, and then – though still largely unresolved – gradually fades from the center of public attention."[67] Attempting to ensure that an experimental program has enduring relevance is therefore a serious issue for any project.

21. Careful Planning Is Performed. A policy experiment is never a small-scale endeavor and its administration is inevitably complex. Careful planning is necessary to ensure that the process is logical and deliberate so that the full benefits of the experiment are realized. For example, it is particularly important that the alternative policy options to evaluate are chosen carefully so that a sufficiently wide range is tested.

22. Transition Issues Are Anticipated. The transition from a centrally administered experimental program to a large-scale permanent program is difficult for two sets of reasons. First, there are obvious administrative challenges involved in creating any large-scale program. For example, as a program matures, processes and roles must be standardized and regulated properly. Second, the results of a small-scale pilot may not always apply to its large-scale version if the participants or processes change for some reason. For example, James J. Heckman has argued that participants in small-scale demonstration programs are not representative of individuals who participate in ongoing, full-scale programs.[68] Certain individuals might be reluctant to subject themselves to random selection, additional resource constraints in full-scale programs that result in administrators restricting participants on the basis of certain criteria. The behavior of individuals in a pilot program may therefore not always be a good predictor of the behavior of participants in a subsequent permanent program.

23. Expertise Is Available. The range of human talent needed to implement a centrally administered experiment is quite extensive, but social experimentation is a new field and the appropriate expertise is in limited supply. A project that procures administrative staff with a background in experimental program development would have a clear advantage.

The Bottom-Up Approach: Attributes of a Successful Program

24. Scaling Issues Are Anticipated. Although the bottom-up replication of successful programs does not present the administrative burden of top-down transition into a large-scale program, there are nonetheless issues involved in scaling up. For example, Charles Manski, a Professor of Economics at Northwestern University, has suggested that some policy approaches intended for widespread adaptation cause changes in community attitudes and norms which, in turn, influence the approach's success.[69] He argues that feedback effects and information diffusion will not occur unless the policy is adopted on a large scale, and therefore will not be observed in small-scale tests.

25. Risk-Aversion Is Mitigated. The lack of a need for central planning reduces the administrative burden, but unfortunately, it also creates the risk that useful innovation may not occur. If no local organizations with the necessary resources are willing to take the risk to attempt a novel policy approach, nothing new will be learned. In describing the process of deliberate social experimentation, the authors of *Social Experimentation: A Method for Planning and Evaluating Social Intervention* explain why it is necessary in a top-down experiment to carefully test a wide range of approaches:

> "Unless deliberate efforts are made to plan informative alternative versions of the programs, the range of variation is likely to be narrow and to be determined by administrative convenience, budget, custom, or side-related factors. Accordingly, even when such variations do occur, the treatment effects may be confounded by special characteristics of the recipients, by geography, or by the way the program was administered. One cannot be sure on the basis of such cause experience whether the program was a success; and if one could be, there would be no way of telling whether it succeeded because of the inherent effectiveness of the treatment, the charisma of an administrator, or some attributes of the treated units."

A bottom-up experiment clearly faces the same risk of producing a narrow window of innovation and slow progress. Ideally, it should be mitigated by a culture that encourages novel approaches and is relatively lenient with well-administered and novel but unsuccessful projects.

26. Expectations Are Realistic. Despite the Nehemiah program's success in building new homes and encouraging community development, it was unable to completely revitalize the neighborhood. Since the range of difficulties affecting a community can be very broad, an affordable housing program alone cannot cure all its ills. If expectations are unrealistically optimistic, a program that could have been very successful as part of an integrated approach to community development will not succeed on its own and be false deemed a failure.

Facilitating a Middling Approach

An approach near the middle of the spectrum brings a lower likelihood of creating useful new knowledge and requires significant resources to maintain. It should therefore only be attempted if immediate action is demanded by a set of urgent political issues. To ensure that such a program can ameliorate pressing concerns in the short-term, however, several conditions are important:

27. Regulation Is Minimal. Unique as the first fast-track grant program of its kind, the minimal regulatory burden faced by UDAG administrators allowed the program enough flexibility to work quickly and effectively. Some regulation is inevitable, however, to specify goals and measures of achieving them, for example.

28. External Bureaucratic Constraints Are Minimal. Early on, the most difficult challenge that UDAG administrators faced involved dealing with the bureaucratic processes required to hire the seasoned real estate lenders and investors that were vital to the project's success.[70] It was so difficult to hire people quickly enough that early administrators had to devise techniques for getting new employees through the process more quickly. Even though the program was exceptionally unregulated, overcoming the "tremendous bureaucratic quagmire" that initially faced UDAG was a substantial burden to getting the program started.

29. Internal Bureaucracy Is Minimal. UDAG administrators had a short list of rules which were simple but "terribly important." Instead of a suffocating set of regulations, there was a small set of unbreakable rules that everyone could remember. For example, one rule was "we put our money in last." This contributed to a low project failure rate because the program would fail before the program was completely involved.

30. Opportunities for Innovation Are Exploited. The political support that emerges from a politically urgent issue creates unique opportunities for learning that should not be missed. For example, UDAG projects created fertile ground for investigation into new public/private partnership models. Unique as a government program designed to influence private investment during the Reagan Administration, it was the subject of numerous research efforts and critiques that provided a wealth of useful real-world information relevant to redevelopment efforts.

Conclusion

Exploring the issues involved in deciding when and how to implement experimentation creates many more questions than answers, including the following:

What Are the Reasons Behind Experimentation in Practice? Experimental projects can be created in order to achieve a variety of goals:

- Test a new approach in the real world
- Keep a policy idea in the political process
- Get a policy alternative off the table for the short term

- Provide data on market behavior
- Create a temporary solution to a pressing problem

Since many pilot and demonstration programs occur every year and this paper examined only a few of them, it would be useful to investigate the motivations behind a much larger set of projects. What are the reasons behind experimentation most often in practice? Do these reasons change over the course of a project? Have these reasons changed over time?

Is There a "Best Size" for an Experiment? In determining how large to make an experimental project, a policymaker faces a complex set of tradeoffs. Some of these might include the following:

- Administrative complexity versus variety of treatments
- Cost versus sample size
- Risking political support versus understanding longer-term interactions

A better understanding of the issues involved in each of these tradeoffs and how they should be judged when determining the scale of an experimental project would be very useful.

Can Piloting be Anticipatory? By the time a pilot project creates meaningful results, the political urgency of the problem it was created to address is likely to be significantly diminished, and its impact on policy might therefore be similarly diminished. Since some housing issues might be anticipated early in the political process before they gain public attention, would the advance creation of pilot projects be feasible? Would it be possible to create sufficient political support before widespread public awareness of a problem exists? Would the results lose applicability anyway?

How Do Other Countries Handle Experimentation? This paper examined experimentation solely from the perspective of the United States. How do other countries handle policy experimentation? How does governmental structure interact with experimental effectiveness? How do public and private institutions interact? Are the motivations behind experimentation different?

An experimental approach to housing policy development is useful because no amount of knowledge-based analysis can replicate the practical insights gained from interacting with real customers in a real marketplace. Experimentation is often approached haphazardly, however, and some systematic thought might make it an even more effective tool.

NOTES

[1] There exists a vast body of work describing effective social research methods. See Bennet, Carl A. & Lumsdaine, Arthur A. (Eds.) *Evaluation and Experiment : Some Critical Issues in Asessing Social Programs* (1975) and Singleton, Royce A., Straits, Bruce C. & Straits, Margaret Miller. *Approaches to Social Research* (1993).

[2] Nehemiah Homes is not represented at the bottom of the spectrum in Figure 2, however, because it developed into a federal program as opposed to remaining a set of similar local programs.

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[17] United States Department of Housing and Urban Development. "Summary Report of Current Findings from the Experimental Housing Allowance Program." Office of Policy Development and Research, 1978.

[18] Frieden, Bernard J. "Housing Allowances: An Experiment that Worked." In *Federal Housing Policy and Programs: Past and Present*. Mitchell, J. Paul (Ed.)

[19] Housing allowances are notably useful for ameliorating "gentrification" whereby rising property values are forcing many poor families out of their homes.

[20] United States Department of Housing and Urban Development. "Housing Choice Vouchers." <http://www.hud.gov/offices/pih/programs/hcv/index.cfm>

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[30] United States Department of Housing and Urban Development. Office of Affordable Housing Preservation. <http://www.hud.gov/offices/hsg/omhar/>

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[53] This section draws heavily from "Affordable Homeownership in New York City: Nehemiah Plan Homes and the New York City Housing Partnership (A)." Kennedy School of Government Case Program. Case C16-94-1252.0

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