# Key Aspects of HUD's Final Rule on Small Area Fair Market Rents

On November 16, 2016, HUD published a Final Rule titled "Establishing a More Effective Fair Market Rent (FMR) System; Using Small Area Fair Market Rents (SAFMRs) in Housing Choice Voucher Program Instead of the Current 50th Percentile FMRs (FR-5855-P-02)" which repeals the $50^{th}$ Percentile FMR regulation as a tool to help Public Housing Authorities (PHAs) deconcentrate voucher tenants and replaces it with a regulation based on SAFMRs.

## 1.) **KEY CHANGES MADE AT THE FINAL RULE STAGE**: PROPOSED VS. FINAL RULE

**Tenant Protections.**

- Proposed Rule: While the Proposed Rule contained no payment standard reduction protections, HUD explicitly requested comments on specific policies or requirements HUD should adopt to address concerns raised in public comments.

- Final Rule: The final rule includes three protections recommended by commenters:

    1. *Provide PHAs with Option to Hold Tenants under HAP Contract Harmless*. Consistent with the Housing Opportunity Through Modernization Act (HOTMA), provides PHAs with the option to hold families under a housing assistance payment (HAP) contract harmless from payment standard reductions that are currently required at the family's 2nd annual recertification *if* the family's payment standard falls outside of the basic range as the result of a decrease in FMRs (including a decrease in FMR attributable to the implementation of Small Area FMRs).

    2. *Providing Flexibility in Payment Standard Reduction*. Should a PHA choose not to hold the payment standard at its current level for families under HAP contract in an area experiencing a payment standard reduction, the PHA may set the payment standard for families that remain under HAP contract at any amount between the current payment standard and new normally applicable payment standard amount, and may further reduce the payment standard for families under HAP contract over time to gradually bring the payment standard in an area down to payment standard that is normally applicable to the area for the PHA's program or reduce the gap between the two payment standards. These same flexibilities are extended to a PHA in cases where the payment standard decrease is not the result of a FMR decrease.

    3. *Ensuring Sufficient Available Units in Transition to Small Area FMRs*. Limits the annual decrease in Small Area FMRs to no more than 10 percent of the area's FMR in the prior fiscal year to ensure that a suitable amount of units remain available during the transition to Small Area FMRs. That is, the current FMR may be no less than 90 percent of the area's FMR in the previous fiscal year. This provision applies to ordinary FMRs as well as Small Area FMRs to mitigate large swings in FMRs due to ACS sampling issues.

**Criteria by which Small Area FMR Areas were selected.**

- Proposed Rule: HUD proposed the following criteria during the Proposed Rule stage:

    1. Recognizing that a SAFMR policy will involve some increase in the complexity of administering the voucher program, HUD sought to exclude many small PHAs by only applying SAFMRs in metropolitan areas with at least 2,500 vouchers.

    2. HUD also sought to apply the program in areas where the concentration of voucher tenants in high-poverty/low-income neighborhoods exceeded national averages. (i.e., Voucher holders 55%+ more likely to live in Concentrated Areas of Low Income (LIHTC Qualified Census Tracts) relative to all renters within the metro area.)

3. Finally, HUD sought to apply SAFMRs where there are sufficient numbers of rental units available in neighborhoods with rents higher than the top of the payment standard "basic range" around the metro FMR so that SAFMRs could be a workable solution for alleviating voucher tenant concentration in high-poverty areas. (i.e., 20%+ of area's rental units are in ZIPs with SAFMRs greater than 110% of Metro FMR).

- Final Rule: HUD retained those criteria and added the following at the Final Rule stage:
  1. Vacancy rates: While SAFMRs can be a useful tool for expanding choice and providing voucher holders with access to more units in areas experiencing low vacancy rates, public comments on the proposed rule raised concerns with HUD's knowledge of how well SAFMRs will work in these areas. HUD agrees that areas with extremely low vacancy rates are indicative of rental markets in disequilibrium. In order for the rental housing market to function in an orderly manner, there needs to be an ample supply of available vacant units. Once the vacancy rate falls below a certain percentage, typically when the quantity of units demanded exceeds the quantity of units supplied, this places upward pressure on rental prices. The solution is typically the creation of additional supply; however, in the short run, a market clearing price is harder to achieve and the rental market ceases to function normally. Therefore, the final rule includes vacancy rate as an additional selection criterion to those provided in the proposed rule. Vacancy rate is calculated from the 3 most current American Community Survey (ACS) 1 year datasets available and average the 3 values.[1] Initially, this threshold is set at 4 percent, meaning Small Area FMR areas must have vacancy rates higher than 4 percent. Most public comments on the proposed rule suggested that areas with a rental vacancy rate of 5 percent or less be exempt from selection as Small Area FMR areas. Given analysis of potential downward bias in nationally available data on metropolitan-level vacancy rates, HUD chose a rate of 4 percent or less be exempt. [2]
  2. Voucher Concentration: As suggested in comments, to better target where voucher concentration is most severe, the Final Rule includes an additional requirement to the voucher concentration ratio provided in Proposed Rule. In addition to requiring the ratio of the proportion of voucher tenants in concentrated low-income areas (CLIAs) to the proportion of renter occupied units in CLIAs to exceed a minimum threshold (initially 155 percent), the final rule requires that the numerator of the ratio (the proportion of voucher tenants in CLIAs) meet or exceed a minimum threshold. Initially, this threshold is set at 25 percent.

**Treatment of Project-Based Vouchers (PBVs)**

- Proposed Rule: HUD proposed to make Small Area FMRs applicable to PBV projects where the PHA notice of owner selection was made after the effective date of an area being designated as a Small Area FMR area; moreover, HUD sought comment in the Proposed Rule about whether PBVs in the pipeline and newly proposed should be required to use SAFMRs.

- Final Rule: Exempts Project-Based Vouchers (PBVs) but allows PHAs to apply Small Area FMRs subject to certain conditions.
  1. Given the range and variation among public comments, and the range of uses of PBV within HUD's rental assistance programs, HUD is choosing to exempt all current and future PBVs from

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[1] Vacancy rate is the number of Vacant for Rent Units divided by sum of the number of Vacant for Rent Units, the number of Renter Occupied Units, and the number of Rented, not occupied units.

[2] The choice of 4 percent arises from the nature of the data source HUD uses to measure the rental vacancy rate, the American Community Survey (ACS), and the method by which the ACS determines vacancy status of units in the survey. As noted in the Regulatory Impact Analysis accompanying the rule, HUD opted to use 4 percent rental vacancy rates as measured by the ACS as the tight-market cut-off for requiring the use of Small Area FMRs to account for the potential underestimation of the rental vacancy rate.

Small Area FMRs at this time. However, if a PHA is operating its tenant-based program under the Small Area FMRs, the PHA may apply Small Area FMRs to all future PBV projects if it establishes such a policy in its PHA administrative plan. In such a case, the PHA may also choose to also establish a policy that allows the PHA to apply the Small Area FMRs to current PBV projects, provided the owner is willing to mutually agree to do so. The application of the Small Area FMR to the PBV project must be prospective. The PHA and the PBV project owner operating under the Small Area FMRs may not subsequently choose to revert back to the metropolitan-wide FMR, regardless of whether the PHA subsequently changes its administrative policy to no longer apply Small Area FMRs to PBV projects. HUD believes this approach offers maximum flexibility for varied circumstances and HUD will closely monitor the results of the policy including for any fair housing or civil rights concerns.

Addressing Burden.

- Proposed Rule: HUD specifically sought comment on how to reduce the administrative burden on PHAs and simplify the transition to Small Area FMRs.

- Final Rule: To address burden, HUD made the following changes at the Final Rule stage:

    1. *Changes to Exception Payment Standard Requirements*: Makes two changes to simplify Exception Payment Standard requirements in response to public comments: (1) PHAs not operating in Small Area FMR designated areas may establish Exception Payment Standards for a ZIP code area of up to 110 percent of the relevant Small Area FMR by notifying HUD; and (2) the existing 50 percent population cap is not applicable to Exception Payment Standards in Small Area FMR areas.

    2. *Timing of Transition to New FMRs*. Provides PHAs with up to 3 months from the date when the new FMRs go into effect in which to update their payment standards if a change is necessary to fall within the basic range of new FMRs. For example, if the new FMR went into effect on October 1, 2017, the PHA would need to update its payment standard if necessary to fall within the basic range of the new FMRs no later than January 1, 2018.

    3. *Rent Reasonableness*: Amends the FMR decrease percentage triggering an automatic rent reasonableness review of their entire voucher portfolio to 10 percent for all PHAs. Previously, the standard that triggered the rent reasonableness review was a 5 percent decrease.

**2.) FORTHCOMING RESOURCES**

To support implementation, HUD is pursuing the following resources:

- HUD expects to issue implementation guidance in FY2017 to provide additional information and support to PHAs implementing SAFMRs.
- HUD will seek to produce webinars in FY2017 to share lessons learned and best practices from PHAs already implementing SAFMRs.
- HUD will explore whether there is interest among implementing PHAs in providing HUD with payment standard data to inform the development of a mobile application (within HUD's Resource Locator) that will enable tenants to confirm a unit's payment standard by entering the address.

**3.) IMPACTED AREAS**

The following areas are required to implement SAFMRs; other PHAs may decide to opt-in.

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| Atlanta-Sandy Springs-Marietta, GA HUD Metro FMR Area |
| Bergen-Passaic, NJ HUD Metro FMR Area |
| Charlotte-Gastonia-Rock Hill, NC-SC HUD Metro FMR Area |

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| Chicago-Joliet-Naperville, IL HUD Metro FMR Area |
| Colorado Springs, CO HUD Metro FMR Area |
| Dallas-Plano-Irving, TX Metro Division |
| Fort Lauderdale-Pompano Beach-Deerfield Beach, FL Metro Division |
| Fort Worth-Arlington, TX HUD Metro FMR Area |
| Gary, IN HUD Metro FMR Area |
| Hartford-West Hartford-East Hartford, CT HUD Metro FMR Area |
| Jackson, MS HUD Metro FMR Area |
| Jacksonville, FL HUD Metro FMR Area |
| Monmouth-Ocean, NJ HUD Metro FMR Area |
| North Port-Bradenton-Sarasota, FL MSA |
| Palm Bay-Melbourne-Titusville, FL MSA |
| Philadelphia-Camden-Wilmington, PA-NJ-DE-MD MSA |
| Pittsburgh, PA HUD Metro FMR Area |
| Sacramento--Arden-Arcade--Roseville, CA HUD Metro FMR Area |
| San Antonio-New Braunfels, TX HUD Metro FMR Area |
| San Diego-Carlsbad-San Marcos, CA MSA |
| Tampa-St. Petersburg-Clearwater, FL MSA |
| Urban Honolulu, HI MSA |
| Washington-Arlington-Alexandria, DC-VA-MD HUD Metro FMR Area |
| West Palm Beach-Boca Raton-Delray Beach, FL Metro Division |