HUD FAQs Concerning HUD's Notice of Proposed Rulemaking: "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"

On June 16, 2016 HUD published a Notice of Proposed Rulemaking (Proposed 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 proposes repealing the 50th Percentile FMR regulation as a tool for helping PHAs deconcentrate voucher tenants and replacing it with a regulation based on Small Area FMRs.

Based on HUD and external research, and using the comment responses on an Advance Notice of Proposed Rulemaking on the same topic published in 2015, HUD has crafted a Proposed Rule.

The following is a high level summary of the contents of the Proposed Rule:
- HUD proposes to amend the regulations governing FMRs and HCV Operations to repeal the 50th percentile FMR rule and replace it with a SAFMR-based rule
- The rule sets certain parameters (size of area, dispersion of rents within the area, concentration of voucher holders within High Poverty/Lower Income areas) to identify areas within which PHAs would operate their voucher programs using SAFMRs
- The rule allows PHAs in areas not identified as using SAFMRs as being able to opt into SAFMR use

These questions and answers are intended to increase the awareness of the Proposed Rule, provide more detail concerning what HUD aims to accomplish, and provide background on the regulation designated for repeal and its replacement.

1. **What are SAFMRs and how do they differ from FMRs?**

   Currently, HUD calculates FMRs for 535 metropolitan areas and approximately 2,037 non-metropolitan counties. The FMR in a metropolitan area is the same value regardless of the rent variation within the FMR area. For example, think of the Washington, DC metropolitan area. The current FMR is the same value in Frederick County, MD, Spotsylvania County, VA, Calvert County, MD, Loudoun County, VA and most areas in between including the District of Columbia and Arlington, VA.

   SAFMRs would set different FMRs by zip code within each metropolitan area. Due to data availability, HUD is unable to calculate SAFMRs for non-metropolitan counties; however, approximately 90 percent of Housing Choice Voucher tenants reside within metropolitan areas.

2. **What Programs are impacted by changes in the Proposed Rule?**

   SAFMRs are targeted to assisted families in the **Housing Choice Voucher (HCV) Program**. HUD proposes to implement Small Area FMRs in metropolitan areas where voucher holders are more likely than renters in general to be highly concentrated in areas of high poverty or relatively low income, and in which there is significant variability in rents (to ensure that SAFMRs are likely to be effective in providing choice). The primary beneficiaries of implementing SAFMRs are <u>tenant based voucher</u> holders, who have the choice of selecting a rental unit in the private

marketplace. HUD is also asking for comment through the Proposed Rule on how SAFMRs should also be applied to *future* Project Based Voucher Units.

The Proposed Rule couples the implementation of Small Area FMRs with a repeal of the 50th Percentile FMR rule. PD&R will still be calculating metropolitan wide FMRs for other uses than in the voucher program, and the Proposed Rule does not transition the entire voucher program to SAFMRs. Based on the parameters selected, approximately 565,000 vouchers are in areas where SAFMRs would be required. HUD's office of Policy Development and Research (PD&R) will maintain the ability to calculate 50th percentile FMRs (e.g., to fulfill the Success Rate Payment Standard regulation within the voucher program).

3. Why is HUD undertaking this proposed rulemaking?

PHAs operating the Housing Choice Voucher (HCV) program use FMRs to establish maximum allowable rent payment standards. HUD sets FMRs to assure that a sufficient supply of rental housing is available to program participants. To accomplish this objective, FMRs must be both high enough to permit a selection of units and neighborhoods and low enough to serve as many low-income families as possible. The level at which FMRs are set is expressed as a percentile point within the rent distribution of standard-quality rental housing units. The current definition used is the 40th percentile rent, the dollar amount below which 40 percent of the standard-quality rental housing units are rented. Because FMRs are currently calculated for entire metropolitan areas, in housing markets with highly varying rents, few units are available to HCV holders in high-cost portions of these metropolitan areas. As a result, many of the units available to voucher holders end up clustered in higher-poverty areas. In high-poverty areas, metropolitan-wide FMRs are often higher than average neighborhood rents and may artificially drive up rents in those areas for people without vouchers.

Currently, HUD sets FMRs at the 50th percentile in a limited number of areas in which voucher households are particularly highly concentrated. Research indicates that 50th percentile FMRs are not an effective tool in providing voucher holders with more choices in accessing opportunity neighborhoods. Additionally, the 50th percentile regulations were drafted before the voucher program was budget based. To manage the greater cost to the federal budget, areas are disqualified from using 50th percentile rents if voucher tenants do not deconcentrate or if voucher holders deconcentrate below the threshold for program eligibility, creating disruptive and burdensome churning in and out of the program.

HUD believes that SAFMRs provide more access to opportunity neighborhoods without increasing subsidies (and rents) in high poverty neighborhoods. Application of SAFMRs will be targeted to areas where voucher holders are concentrated in high poverty portions of metropolitan areas and sufficient numbers of units are available in higher-rent opportunity areas. Therefore, HUD proposes to repeal a regulation that does not provide the opportunities as originally intended and replace it with a new one that is likely to provide the additional opportunities.

4. Why do you believe that a SAFMR-based rule will be more effective than the current 50th percentile rule?

Currently, rent payment standards are set around Metropolitan-wide Fair Market Rents. In those metropolitan areas where rents vary substantially by neighborhood quality, metropolitan FMRs may be insufficient for accessing low poverty neighborhoods and rather, may contribute to concentrating voucher households in high poverty areas. Small Area Fair Market Rents (SAFMRs), which are FMRs set at the zip code level, would represent a fundamentally different way of operating the Housing Choice Voucher program in such metro areas, by allowing the subsidy to actually work in the more desirable neighborhoods.

Evidence from Dallas where SAFMRs have been in effect since 2010 is quite promising – suggesting de-concentration to lower poverty, lower crime neighborhoods at essentially the same total cost per voucher as using the 40th percentile metropolitan FMR. Research and results from Dallas suggest SAFMRs could be both *more effective* and *less costly* than the 50th percentile FMR policy.

5. **How did HUD determine what areas would be required to use SAFMRs?**

   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. HUD also sought to apply the program in areas where the concentration of voucher tenants in high-poverty/low-income neighborhoods exceeded national averages, *and* 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 (i.e., more than 110 percent of the metro FMR) so that SAFMRs could be a workable solution for alleviating voucher tenant concentration in high-poverty areas.

6. **The Proposed Rule says HUD started looking into this in 2010. What made you think a change was needed?**

   Former HUD Secretary (now OMB Director) Shaun Donovan often spoke about how it was wrong that a child's ZIP Code, could be such a good predictor of their life outcomes—that poverty and social conditions in a child's neighborhood determined so much of a child's life chances. Our housing programs are meant to provide affordable, stable housing as the foundation to improving those outcomes, yet in many metropolitan areas, voucher tenants are concentrated in high-poverty neighborhoods, and HUD's existing policies to encourage deconcentration are not working – including the existing 50th percentile policy that we are proposing to change.

7. **What kind of budget impact do you anticipate from a change? (i.e. – would the amount needed for subsidy increase if more tenants found units in higher rent areas? Or would this primarily mean paying less in bulk to landlords in lower rent areas?)**

   It is difficult to fully predict the cost impact of a switch to SAFMRs on the voucher program as a whole, or in any particular market. However, we do have evidence suggesting SAFMRs could generally be cost effective relative to the existing 50th percentile policy.

   In the Dallas MSA, which has been using SAFMRs since 2010, the average cost per voucher has not increased relative to using the 40th percentile. Yet movers in the Dallas voucher program

are improving their neighborhoods, they are moving to significantly better neighborhoods in terms of safety and poverty; they are just not doing so by large numbers moving to the most expensive ZIP Codes. There is a mixture of some movement toward higher rent areas as well as savings from tenants that remain in lower rent neighborhoods and receive lower subsidies. Given SAFMRs did not increase the average cost of vouchers relative to the 40th Percentile, it was clearly less costly than the 50th percentile would have been, at least in Dallas.

Indeed, there is recent research by Rob Collinson (NYU) and Peter Ganong (Harvard) showing that most of the transfers created by our existing 50th percentile policy accrue to landlords through higher rents rather than improvements in housing and neighborhood quality for tenants. This suggests that removing those unnecessary subsidies might be accomplished without lowering housing quality for tenants that don't move.

8. **The cost neutrality of the SAFMR program is rooted in cutting voucher payment standards in low-rent neighborhoods while tenants choose to remain there with lower subsidies. What tenant protections are contemplated for tenants that cannot move and may face greater rent burdens under the lower payment standards imposed by SAFMRs?**

The Proposed Rule maintains the existing requirement that payments standards for tenants that do not move cannot decrease until the second annual recertification after the payment standard is decreased. Additionally, exception payments standards as reasonable accommodation for disabled tenants are not removed by the Proposed Rule. While no specific tenant protections are included in the Proposed Rule, HUD has asked for public comment on whether additional tenant protections are necessary. For example, one possibility included in the propose rule is to increase the amount of time that the family is held harmless from a decrease in the payment standard. For instance, instead of the lower payment standard going into effect on the second reexamination following the effective date of the decrease in the payment standard, the final rule could provide that the lower payment standard would not go into effect for a family under HAP contract until a later re-examination (e.g., third, fourth, or fifth reexamination).

9. **My understanding is this is focused on the tenant based voucher program, and potentially project based. How would it work for project based? How would this affect LIHTC projects? How would this interact with RAD?**

To be clear, the <u>primary intent of the Proposed Rule is on the application of SAFMRs to the voucher program.</u> For other programs, metro FMR estimates would remain available.

While the focus is on tenant based vouchers, project-based voucher (where public housing authorities contract with an owner of multifamily housing to maintain vouchers in particular units) raises interesting questions. The Proposed Rule would base payment standards in currently contracted project-based vouchers on the metropolitan FMR in order to maintain project viability, but would apply SAFMRs to future project-based vouchers in order to encourage their placement in higher-rent opportunity areas.

Rents in LIHTC projects are governed <u>by HUD's Income Limits</u>, not FMRs, so any effects would come through the presence of voucher tenants in LIHTC projects.

10. **Are there other effects that you anticipate?**

Recent research released by Raj Chetty of Stanford finds a substantial impact on the long-term earnings of young children in voucher tenant families that moved to low poverty neighborhoods in HUD's Moving to Opportunity demonstration (which notably did not use SAFMRs or other enhancements to the subsidy amounts to help families find and stay in units in low poverty neighborhoods). We hope to see voucher families with young children taking advantage of the new subsidy structure under SAFMRs to move to lower poverty, safer neighborhoods. This should improve our ability to use housing subsidies to increase economic and social mobility of the families we serve.

11. **What is the timeline for the Proposed Rule?**

The federal rulemaking process is complex and seeking public input takes time. Hence, timing is not easy to predict. HUD's hope would be to issue a final rule in 2016. The Proposed Rule is currently open for public comment.

12. **Is the list of 31 areas published within the Proposed Rule, the final list of FMR areas that will be converted to Small Area FMR usage?**

No. The list of 31 areas included in the Proposed Rule would be the areas that would use Small Area FMRs to run their Housing Choice Voucher program if the final rule were put into effect at this time. This list is based on the parameter values within the proposed rule and the location data (Census tract level poverty rate data, Small Area FMR values, HUD HCV Tenant location data, and Qualified Census tract data) available at the time the Proposed Rule was crafted. Should HUD continue to Final Rulemaking, the list of areas will be re-evaluated based on the most current location data available plus any changes to the selection criteria within the Proposed Rule based on public comments received. Additionally, the Proposed Rule contains a provision for PHAs operating in areas not designated for Small Area FMR usage to "opt-in" to using Small Area FMRs. These "opt-in" PHAs will also contribute to the list of FMRs areas where Small Area FMRs are utilized.

13. **Where can I find more information about HUD's Small Area and metropolitan area FMR calculations?**

HUD publishes the methodology for calculating standard FMRs and Small Area FMRs annually in our Proposed FMR Federal Register notices. These notices are available at:
http://www.huduser.gov/portal/datasets/fmr.html.

14. **Are Moving-To-Work (MTW) PHAs operating in Small Area FMR designated metropolitan areas exempted from using Small Area FMRs?**

There are no exemptions for MTW PHAs within the text of the Proposed Rule. If the Proposed Rule were to be made Final now, MTW PHAs operating in designated areas would be required to use Small Area FMRs; however, HUD also notes in the Proposed Rule that MTW PHAs have the ability to submit "alternative rent policies" to the Department for approval. Nothing within the Proposed Rule removes this ability from MTW PHAs, so with HUD approval, MTW PHAs

within Small Area FMR designated areas can implement an "alternative rent policy" to the standard Small Area FMRs.

15. **What is the HUD justification for choosing "155 percent (or 1.55)" formula as a measure of poverty or income concentration?**

The voucher weighted average of the concentration measure across all metropolitan areas is 1.548. This can be calculated using the data contained in the SAFMR-HMFA-Selection-Tool-Proposed-Rule.xlsx available at: https://www.huduser.gov/portal/datasets/fmr/fmr2016p/SAFMR-HMFA-Selection-Tool-Proposed-Rule.xlsx.

In order to calculate this voucher weighted average, please multiply the value in column C by column D in each row of the "All BR" worksheet. Please sum the results of this multiplication and divide the sum by the sum of the values in column "C". In excel formulas, this can be accomplished with the following formula: SUMPRODUCT(C3:C625,D3:D625)/SUM(C3:C625)

16. **What is the data and what are the calculations that were used to adopt the "155 percent (or 1.55)" formula for the poverty concentration requirement.**

As stated in the proposed rule, HUD used its administrative data on voucher locations by census tract to determine the percentage of current voucher holders living in concentrated low income areas. Similarly, HUD used 2013 5-year ACS data at the Census Tract level to determine the percentage of renter occupied units in Concentrated Low Income Areas. The concentration measure for the purposed of the proposed rule is the percentage of voucher holders in units in Concentrated Low Income Areas divided by the percentage of renter units in Concentrated Low Income Areas.

17. **Is there a citation to the available HUD or academic studies or reports that use the "155 percent (or 1.55)" formula as a measure of poverty or income concentration.**

This measure of voucher concentration was developed for this Proposed Rule. It was developed to identify metropolitan areas where voucher tenants are more likely than renters in general to live in concentrated low income areas.

18. **What are the voucher concentrations and the all renter occupied unit concentrations for the areas included in the SAFMR-HMFA-Selection-Tool-Proposed-Rule provided for the proposed rule?**

   In the updated SAFMR-HMFA Selection Tool workbook, updated on July 22, 2016, HUD has included the voucher concentrations and all renter unit concentrations in the workbook tab "underlying data". These concentrations are available in columns G & H respectively.

19. **Does the proposed definition of concentrated low income areas include tracts that are less than 25% poverty but meet the eligibility requirements for QCT status but have not been designated as QCTs by HUD? If the answer is yes, what are those tracts?**

   No, as stated in the summary of the preamble of the proposed rule (on page 39219 of the Federal Register publication and elsewhere as well) "''concentrated low-income areas'' means those census tracts in the metropolitan FMR area with a poverty rate of 25 percent or more; or any tract in the metropolitan FMR area where more than 50 percent of the households earn incomes at less than 60 percent of the area median income (AMI)*__and are designated as Qualified Census Tracts__* in accordance with section 42 of the Internal Revenue Code (26 U.S.C. 42)." (emphasis added).

20. **What is the source of ACS data used to determine the SAFMRs for the U.S. Postal Zip code areas? Is it the ACS Zip Code Tabulation Area (ZCTA) data?**

   HUD uses special tabulations of Zip Code Tabulation Area (ZCTA) and County-level data from the American Community Survey to calculate Small Area FMRs. However, while ZCTAs and Zip Codes generally have similar boundaries, there are cases where there is no corresponding ZCTA data for postal service ZIP Codes. In publishing Small Area FMRs, HUD attempts to ensure that we assign a small area FMR for each ZIP Code. To accomplish this, HUD uses its US Postal Service Vacancy Data (https://www.huduser.gov/portal/datasets/usps.html) to glean any 5 digit ZIP Code which has a non-zero number of Residential Addresses that doesn't have a corresponding ZCTA. Lastly, HUD uses its administrative data on current voucher holders addresses to further augment the list of ZIPs for which HUD publishes a Small Area FMR. The ZIP codes with statistically reliable matching ZCTAs receive Small Area FMRs based on the ZCTA level information, and those ZIP codes without statistically reliable ZCTA information receive Small Area FMRs based on county-level information.