Does HUD Overpay for Voucher Units, and Will SAFMRs Reduce the Overpayment?

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Abstract

One argument for Small Area Fair Market Rents (SAFMRs) is that they would reduce overpayment for voucher units in low-rent neighborhoods. This leads to the belief that the benefits of SAFMRs can be funded largely by reductions in landlord profits rather than by losses to voucher recipients who remain in low-rent areas. The usual theoretical argument that has led many to believe that voucher units are overpriced focuses on one implication of one feature of the Housing Choice Voucher program. This article provides a more comprehensive theoretical analysis that leads to the conclusion that the worst voucher units and those in the worst neighborhoods will usually rent for more than the mean market rent of identical units, and the best units in the best neighborhoods will rent for less than this amount. The debate over this matter has ignored the bulk of the available evidence. This article summarizes and assesses the data, methods, and results of the major studies. The evidence is consistent with the general pattern predicted by the comprehensive theoretical analysis but also with an alternative explanation that challenges its interpretation of overpayments and underpayments for voucher units. The mix of units with estimated overpayments and underpayments varies across studies, but the weight of the evidence is that the aggregate differences are modest. Finally, the evidence available indicates that SAFMRs will decrease the rents paid for voucher units with any specified set of characteristics in the worst neighborhoods and will increase the rents of such units in the best neighborhoods.

Introduction

Convincing evidence indicates that children in low-income households will have better outcomes as adults if they grow up in better neighborhoods (Chetty, Hendren, and Katz, 2016; Chyn, 2018). Evidence also indicates that Small Area Fair Market Rents (SAFMRs) will induce more voucher recipients with children to move to better neighborhoods without any significant increase in

taxpayer cost (Collinson and Ganong, 2018; Dastrup et al., 2018). If the decision makers in these families undervalue the benefits of a better neighborhood for themselves or their children, or if they fail to devote a sufficient share of the family's resources to their children in the eyes of others who care about them, this evidence provides a strong argument for SAFMRs.[1]

Another argument in the debate over the desirability of SAFMRs is on shakier ground. At several points in the Federal Register entries for the proposed SAFMR rule (81 FR 39218) and final rule (81 FR 80567), it is argued that another benefit of SAFMRs is that they would reduce overpayment of rent in areas where median neighborhood rent is below the average for the metropolitan area. The belief that the voucher program overpays for units in these areas is widespread among housing policy analysts and others involved in housing policy debates. This leads to the belief that the benefits of SAFMRs can be funded largely by reductions in landlord profits rather than losses to voucher recipients who remain in low-rent areas. If market rents are paid for voucher units in these areas, reduced payment standards would force these recipients to pay higher rents or move to less desirable units.

The usual theoretical argument that has led many to believe that voucher units are overpriced focuses on one feature of the Housing Choice Voucher (HCV) program and ignores other features that affect this outcome. The Federal Register entries for the proposed and final SAFMR rule are not specific about the nature of the evidence on this matter. They cite an early version of a recently published paper (Collinson and Ganong, 2015), however, that contained some evidence about the extent of overpayment for voucher units. Desmond and Perkins (2016) provide recent results for one county, but neither Collinson and Ganong nor Desmond and Perkins provide a good account of the major studies funded by the U.S. Department of Housing and Urban Development (HUD) that shed considerable light on this matter.

The purposes of this article are to explain the theoretical reasons for rents of voucher units to be greater or less than the mean rents of similar units occupied by unsubsidized households and to summarize and assess the data, methods, and results of the major empirical studies of this matter. Because the voucher program has changed over time and voucher programs with different features should be expected to have different outcomes, this assessment will account for the nature of the voucher program at the time of the data underlying the results of each study. This article will provide a comprehensive account of the state of the evidence on this matter.

Theory

The HCV program has features that lead to the expectation that HUD will pay more than the mean market rent of identical units for some units in some locations and less than the mean market rent of identical units for other units in other locations. This section analyzes the expected effect of these features.

The argument that has led many to expect that voucher units would be overpriced is based on a simplified version of the program. It assumes that a voucher recipient is allowed to occupy any

[1] Otherwise, the evidence provides no rationale for incentivizing families with children to live in a better neighborhood at the expense of worse housing.

unit that meets the program's minimum housing standards and rents for less than a program parameter called the payment standard, the voucher recipient can agree to pay the landlord any rent up to the payment standard, and the recipient will contribute a fixed amount toward its rent, usually 30 percent of their countable income. Under these assumptions, if the market rent of a unit occupied by a voucher recipient is less than the payment standard, its tenant would have no reason to resist paying the landlord a rent equal to the payment standard. This leads to the conclusion that all landlords who serve voucher recipients will charge rents equal to this amount. Therefore, all voucher units with market rents less than the payment standard would be overpriced, and the worst units in the worst neighborhoods would be overpriced to the greatest extent.

The conclusion that all landlords who serve voucher recipients will set their rents equal to the payment standard is counterfactual. Collinson and Ganong (2018, Online Appendix, Figure B.5) reveal that this is true for only 12 percent of voucher recipients.[2] About 52 percent have rents less than the payment standard and, in many cases, substantially less. Their results also indicate HUD pays more for better units (Online Appendix, Figure B.1). The Freestanding Housing Voucher Demonstration produced similar results for the predecessor to the current HCV program.[3]

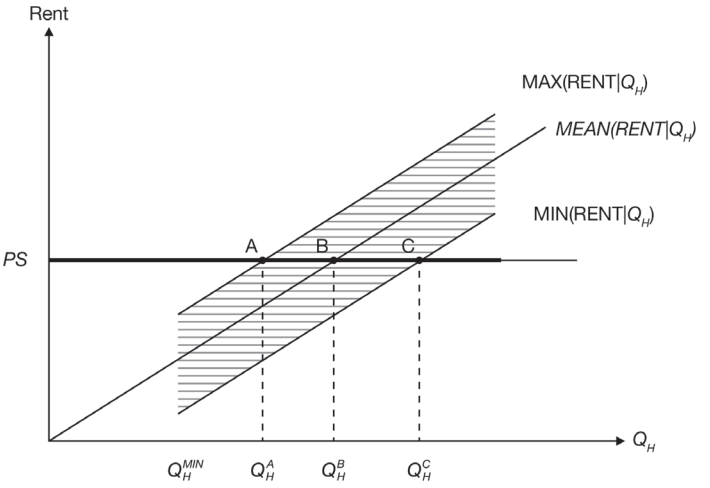
The argument that leads to the expectation that voucher units will be overpriced ignores an important aspect of reality and an important incentive in the simplified version of the program. Exhibit 1 illustrates their combined effect. The exhibit describes the relationship between the desirability and rents of the units in a given neighborhood. The units in the neighborhood differ in their desirability Q_H. Due to search cost, identical units in the neighborhood do not have the same rent. The points in the shaded area represent combinations of unit desirability and asking rents to unsubsidized tenants for units that meet the voucher program's minimum housing standards Q_H^{MIN}. PS is the program's ceiling rent. The units available to voucher recipients are the units in the shaded area to the right of Q_H^{MIN} and below PS. Landlords with asking rents above PS will not agree to rent to voucher recipients. Based on the assumptions of the usual argument, landlords with asking rents less than or equal to PS will agree to rent to voucher recipients for a rent equal to PS because they realize that voucher recipients have no reason to resist this rent for their unit.

[2] https://assets.aeaweb.org/asset-server/files/6861.pdf

[3] Leger and Kennedy (1990b, Table G.17) at https://www.huduser.gov/portal/Publications/pdf/HUD-005555.pdf and Leger and Kennedy (1990c, Table E.25C) at https://www.huduser.gov/portal/Publications/pdf/HUD-005597.pdf

Exhibit 1

Units of Different Quality Potentially Available to Voucher Recipients in a Neighborhood



Like unsubsidized tenants, voucher recipients looking for a unit will contact a number of landlords and visit a number of units. Asking rent and a few rudimentary characteristics are nearly always stated in advertisements, but it is necessary to visit units to determine their desirability. Voucher recipients will limit their search to units in the shaded area to the right of Q_H^{MIN} and below PS, but due to search costs, they will not contact all landlords with vacant units. Because the rent that they pay does not depend on the desirability of the unit, they will occupy the best unit that they find during their search. This is a largely unrecognized implication of the assumptions of the usual argument. Recognizing that units with the higher asking rent usually have more desirable characteristics would motivate voucher recipients to search among units with asking rents slightly below PS.

On the usual argument, if the best unit found in a search has desirability between Q_H^B and Q_H^C, the recipient's combination of unit desirability and landlord rent would be on the line segment BC. Except for units with an initial asking rent equal to PS, these landlords would receive rents greater than their initial asking rents. In that sense, they would be overpriced. They would also, however, have rents less than the mean rent of identical units. In this sense, they would be underpriced. All empirical work on this topic is based on the second concept of underpayment and overpayment. It compares the actual rent of voucher units with an estimate of the mean market rent of units with the same characteristics.

Therefore, the fact that the tenant contribution to rent does not vary with the rent paid to the landlord does not imply that HUD pays rents greater than the mean market rent of identical units for units occupied by voucher recipients. Under the assumptions of the usual argument, two offsetting forces are at work—no incentive to avoid overpayment for units and an incentive to occupy the best possible unit. This leads to the expectation that the worst units occupied by voucher recipients in a neighborhood would be overpriced and the best units underpriced.

By reinterpreting Q_H, it is possible to get similar results for the pricing of identical units in neighborhoods of different quality or the pricing of a composite of unit and neighborhood quality across the entire housing market. Among units of identical quality, those in the worst neighborhoods will be overpriced and those in the best neighborhoods underpriced. Among all units, those with the lowest market rent will be overpriced and those with the highest, underpriced.

In assessing the likelihood of underpricing and overpricing in exhibit 1, it is important to realize that many landlords are unwilling to serve voucher recipients and the fraction willing to serve them is lower for landlords with higher asking rents (Phillips, 2017).[4] This will probably induce voucher recipients to modify their search in terms of neighborhoods and asking rent. As a result, the best option that results from their search are less likely to be between Q_H^B and Q_H^C in exhibit 1. This would lead to fewer underpriced and more overpriced units.

The simplified description of the voucher program ignores two important features of the HCV program. First, the housing agency rather than the tenant decides on the rent that will be paid for a voucher unit. HUD regulations require public housing agencies (PHAs) to conduct a rent reasonableness determination before units are leased and before rent increases are granted to owners. They use a variety of methods to comply with this requirement. The most common is based on the rents of unsubsidized units in the same building or nearby, adjusted for differences in their characteristics (ICF International, 2014, Exhibit IV-25).[5] Presumably, the PHA sets an upper limit on the amount it is willing to pay for each unit. Landlords who understand the program's operation might reasonably propose rents equal to the payment standard even for units with market rents well below these levels, but the housing agency will not agree to rent above its upper limit. Therefore, for the lowest quality units and units in the worst neighborhoods, the payment standard is not the effective upper limit on the rents paid to landlords. The effective upper limit is what the housing agency is willing to pay. In terms of exhibit 1, it varies with Q_H and is probably somewhere between MAX (RENT|Q_H) and MEAN (RENT|Q_H). Enforcement of the rent reasonableness test would reduce and possibly prevent overpayment for the worst units in the worst neighborhoods. If housing agencies were able to determine completely accurately the mean market rent of identical units and established it as an upper limit on a reasonable rent, no voucher units would be overpriced.

The HCV program differs from the simplified version in another important respect. A voucher recipient is allowed to occupy a unit renting for more than the payment standard but must pay the entire additional cost. On the initial lease, the maximum rent is the payment standard plus 10 percent of countable income. This ensures that the household will not devote more than 40 percent of its countable income to rent. This restriction does not apply beyond the initial lease. A household with a voucher might choose to occupy a unit renting for more than the payment standard if it places a particularly high value on better housing or a more desirable neighborhood, or if it is not worth the effort to find a unit renting for less. In 2018, the program's mean payment

[4] In an online appendix at https://assets.aeaweb.org/asset-server/files/6861.pdf, Collinson and Ganong (2018) develop a model that focuses on this aspect of reality.

[5] https://www.huduser.gov/portal/publications/pubasst/QCinc_fy13.html

standard and mean countable income were about $1,100 a month. Therefore, the rent ceiling exceeded the payment standard by about 10 percent.

This feature affects many HCV recipients. In 2009, 36 percent of voucher units had rents greater than the applicable payment standard.[6] Because voucher recipients would bear the full cost of better housing over this range of asking rents, they face the same incentives as unsubsidized tenants. We would not expect the mean rent paid for voucher units in this range to differ from the mean market rent for identical unsubsidized units. Therefore, some voucher recipients living in the best units and neighborhoods are in this group. Others may live in units that are underpriced.

Taking account of incentives and features of the HCV program that are ignored in the usual argument suggests that the worst voucher units, and those in the worst neighborhoods, will usually rent for more than the mean market rent of identical units, and the best units in the best neighborhoods will rent for less than this amount. The following evidence supports that general pattern. It also sheds light on the mix of units in the two categories and the magnitudes of the differences.

Evidence

The best evidence about voucher rents relative to market rents comes from three major HUD-funded studies and one recent journal article. The HUD-funded studies use random sampling to estimate patterns for the country as a whole. The journal article produces results for one county. Most studies predict the market rent of voucher units based on estimated hedonic equations, but one used real estate appraisers.

Because there is no reason to believe that the HCV program has about the same effect in all localities, it is important to consider the evidence from the best older studies. However, since these studies produced results for different times in the history of the Section 8 Existing Housing Program (1979, 1987, 2000), it is also important to consider how the versions of the program that existed at the earlier times differed from the current program and how these differences are likely to affect the outcomes of interest. We are primarily interested in the performance of the current program, and the Section 8 program has undergone significant changes on several occasions (Olsen, 2003).

The earliest studies produced results for the rent certificate program. The only significant difference between the rent certificate program and the HCV program is that the certificate program's payment standard was its ceiling rent.[7] Unlike current recipients, certificate holders were not allowed to occupy a more expensive unit by paying the incremental cost. It is reasonable to believe that the recipients who would have chosen this option under the HCV program would have lived in the best units and neighborhoods under the certificate program. The earlier analysis suggests that these households would typically have paid below-market rents for their units under the certificate

[6] Rob Collinson provided this number based on the data underlying Figure B.5 in the online appendix to Collinson and Ganong (2018).

[7] For most certificate holders, the payment standard was the applicable Fair Market Rent (FMR) that applied everywhere in a metropolitan area. Housing agencies were allowed to have payment standards called exception FMRs up to 10 percent greater than the applicable FMR for up to 20 percent of recipients, however.

program. Under the HCV program, they have the same incentive to avoid overpriced units as unsubsidized households. Therefore, they would, on average, pay market rents for their units, and we expect aggregate overpayment to be larger in the HCV program than in the certificate program. This is consistent with evidence from the only study that compared the two programs (ORC/Macro, 2001, Exhibit V-10).[8]

Participation and Benefits in the Urban Section 8 Program

Abt Associates (1981) provides the first evidence on the rents paid for voucher units relative to the mean market rent of similar units in similar neighborhoods.[9] This study is based on 1979 data for 276 randomly selected participants in the original housing certificate program from 16 randomly selected metropolitan areas. The authors predict the market rents of voucher units using hedonic equations estimated with detailed information on the characteristics of unsubsidized dwelling units and their neighborhoods from the Annual Housing Survey (AHS) and even better information collected by the contractor for the study. The AHS data contained information on 40,560 rental units; the latter information on 1,365 apartments in 13 metropolitan areas. With the smaller sample, the authors estimated separate hedonics for four regions with dummy variables for the standard metropolitan statistical areas (SMSAs) in those regions. For the larger sample, they estimated separate hedonics for each SMSA. The results indicate that the program's gross rent exceeded predicted rent by 4 to 5 percent.[10] Under standard assumptions, the premium was estimated with considerable precision. The authors did not estimate how the premium varied with the desirability of the unit or neighborhood.

Freestanding Housing Voucher Demonstration

The second major HUD-funded study that sheds light on the rents paid for units under voucher programs is the Freestanding Housing Voucher Demonstration, a random assignment experiment that compared selected outcomes of the old certificate and voucher programs.[11] The 1998 Housing Act created the HCV program as a hybrid of these two programs. With minor exceptions, the old voucher program provided a fixed subsidy to each household and placed no upper limit on the rent of the unit occupied. Every additional dollar paid in rent reduced the recipient's spending on other goods by that amount. Unlike the certificate program, the old housing voucher program did not have a rent reasonableness test.

The results of the experiment are based on data collected between 1985 and 1987 on recipients served by 17 randomly selected large urban PHAs and two statewide voucher agencies. The experiment assigned new recipients randomly to receive one of the two types of housing assistance. Many outcomes were studied, including the rents paid for certificate and voucher units with the same characteristics. Recipient housing is the subject of a lengthy report (Leger and Kennedy,

[8] https://www.huduser.gov/portal/Publications/pdf/qualitycontrol.pdf

[9] This report is not available on HUD's website. A scanned version can be found at http://eoolsen.weebly.com/housing-policy-info.html.

[10] See tables 6-25 and 6-26 at http://eoolsen.weebly.com/housing-policy-info.html.

[11] The experiment generated reports totaling more than a thousand pages. The two final reports that contain the detailed results (Leger and Kennedy, 1990b; 1990c) are posted on HUD's website. Oddly, the summary report (Leger and Kennedy, 1990a) is not posted.

1990c). Its authors used data on households in the old housing voucher program to estimate a hedonic equation that was used to predict the market rents of units occupied by households with rent certificates. Because voucher recipients faced the full marginal cost of their housing, the authors assumed that they paid market rents for their units. The analysis is based on data from the 10 urban PHAs that had a specified minimum number of recipients in each program. The contractor assembled detailed information about the housing and its neighborhood for about 100 certificate and 100 voucher recipients in each site.

The study found that the mean rent paid for units in the certificate program was about 4 percent less than the mean of the market rents of its units.[12] Detailed results indicated a pattern of overpayment and underpayment consistent with the implications of the theoretical model in the preceding section. Certificate recipients paid higher than market rents for low-quality housing (broadly conceived) and the opposite for high-quality housing.[13] Specifically, the authors provide estimates of the mean actual and predicted rent for 15 ranges of predicted market rent relative to FMR to account for different rent levels in different localities.[14] For the 28 percent of certificate units that had predicted market rents less than 75 percent of the applicable local FMR, the mean actual rent exceeded the mean predicted market rent. With a trivial exception, the percentage difference was greater for units with the lower predicted market rent. The largest percentage difference (15 percent) was for units with predicted market rents less than 55 percent of the FMR. For units with predicted market rents between 75 and 85 percent of the FMR, there was essentially no difference between mean actual and market rents. For the 55 percent of certificate units with predicted market rents in excess of 85 percent of the FMR, the mean predicted market rent exceeded the mean rent paid for the units. The percentage difference tended to be greatest for units with the highest predicted market rent; the largest percentage difference (17 percent) was for units with predicted market rents greater than 140 percent of the FMR. Therefore, in most cases, the incentive of certificate recipients to find the best units renting for less than the payment standard outweighed the absence of an incentive to resist overpaying for the unit.

Quality Control for Rental Assistance Subsidies Determination

For many years, HUD has funded studies to assess the performance of PHAs in administering its rental assistance programs. To determine their effectiveness in enforcing the rent reasonableness test, one of these studies compared the rents paid for voucher units with their estimated market rents (ORC/Macro, 2001). Unlike other studies discussed in this paper, the contractor hired real estate appraisers to estimate market rents. Appraisers attempt to find comparable units that are nearby and account for differences in the characteristics of the units that significantly affect market rent. Whether appraisers or hedonics are more effective in predicting market rents is an open question.

[12] Leger and Kennedy (1990b, Table D.21A, D.21B) at https://www.huduser.gov/portal/Publications/pdf/HUD-005555.pdf.

[13] The authors did not distinguish between unit and neighborhood quality. They used market rent as an index that captures both.

[14] Leger and Kennedy (1990b, Table D.22C) at https://www.huduser.gov/portal/Publications/pdf/HUD-005555.pdf and Leger and Kennedy (1990c, Table E.25C) at https://www.huduser.gov/portal/Publications/pdf/HUD-005597.pdf provide similar results based on ranges of predicted rent alone. The qualitative conclusions are the same.

This study is based on data for 752 recipients served by 107 randomly selected housing authorities in 2000. Different recipients were served by different voucher programs. In October 1999, HUD began the transition from the rent certificate and old voucher program to the current HCV program. At the time of the study, some units were under each of the three programs. The report does not contain information on the percentage served by each program. The results reported in exhibit V-10, however, imply that the rent certificate program served 53 percent of the total.[15] The study does not report results separately for the three programs, and the one result reported for different programs does not distinguish between the old and new voucher programs. Because the old voucher program was quite small relative to the certificate program, it seems likely that the current voucher program served many voucher recipients in the study.

ORC/Macro (2001) found that in aggregate the three programs paid 10 percent less than market rents for their units. Exhibit V-10 indicates that, on average, program units rent for less than predicted market rents for all types of households, dwelling units, and program parameters studied. Consistent with the implications of the model in the preceding section, the discount is greater in the certificate program than in the voucher programs ($120 versus $66 a month) and greater in high- than in low-cost submarkets ($244 versus $14 a month). Because each unit is classified as living in a high- or low-cost submarket based on whether its estimated market rent is greater or less than the FMR in the locality, the latter result is more accurately described as reflecting the overall desirability of the unit rather than only neighborhood desirability.

Milwaukee Study

In a recent study based on a random sample of rental units in Milwaukee County, WI, Desmond and Perkins (2016) estimated the difference between the rents of unsubsidized and voucher units based on excellent information about the housing, neighborhood, and tenant characteristics of 1,046 renters in 2010. They found that landlords received rents about $51 to $68 a month more than market rents for their units. The mean rent paid for voucher units was about $765 a month, so this amounted to 7 to 10 percent higher than market rents. The authors also present results for different quartiles of the distribution of an index of neighborhood disadvantage (Desmond and Perkins, 2016: Figure 3). They find that the excess cost in dollar terms is greatest and about equal for neighborhoods in the two quartiles with the greatest disadvantage. In the most advantaged neighborhoods, voucher recipients paid slightly less than market rents. If the results had been expressed as percentages, they undoubtedly would have indicated a monotonic relationship.

This study has several important virtues. All recipients participated in the current HCV program and hence the results apply directly to this program. Furthermore, its estimated hedonic equation is the equal of the best previous hedonics used to estimate differences between the rents of unsubsidized and voucher units.

Two disadvantages of this study compared with the other studies concern the generalizability of the results and the small sample of voucher recipients. The magnitudes of interest surely vary

[15] The exhibit at https://www.huduser.gov/portal/Publications/pdf/qualitycontrol.pdf reports the mean difference between actual and market rent for all units and separately for certificate and voucher units. The percentage served by the certificate program can be calculated from these numbers.

from time to time and place to place. For example, some PHAs surely do a better job than others in enforcing the program's rent reasonableness test. The variance in outcomes could be large, and Milwaukee County could be far from average in its outcomes. The best previous studies produced estimates for a random sample of locations in an attempt to produce national average results. Furthermore, these studies base their estimates on much larger samples of voucher units ranging from 276 to about 1,000, as opposed to 57 in the Milwaukee study.

Another problem with this study is that some households identified as unassisted probably live in privately owned subsidized housing projects. Because they pay below-market rents, their inclusion in the analysis as unassisted households would bias the results in the direction of overstating the excess rent of voucher units. Despite the authors' efforts to avoid it, there are good reasons to believe that this inclusion is a problem. The sample is a stratified random sample of households in the county. About 57 of the 1,045 households used in the analysis were identified as voucher recipients. According to HUD's Picture of Subsidized Households, twice as many households in Milwaukee County live in privately owned subsidized housing projects as have housing vouchers. Therefore, the sample should be expected to contain about 114 households living in subsidized projects. Using address matching, Desmond and Perkins were able to identify only four households in their sample who lived in such projects. It is very unlikely that such a large difference resulted from random sampling. It is more likely to have resulted from the difficulties of address matching. The list of addresses of privately owned subsidized housing projects may have been incomplete. The address listed for a project may have been the address of a business office rather than the residences at the project. Only one address is listed for each project, and projects often contain multiple buildings with addresses that differ beyond differences in apartment numbers. Despite substantial efforts, HUD has been unable to identify most of the tax credit units in the American Housing Survey, and identifying units served by HUD's programs was no mean feat. This testifies to the challenges involved. It seems likely that about 10 percent of households identified as unassisted paid below-market rents. For this reason, the Desmond and Perkins (2016) results should be regarded as an upper bound on the overpayment for voucher units.

How Do Changes in Housing Voucher Design Affect Rent and Neighborhood Quality?

As suggested by its title, the most important contribution of Collinson and Ganong's published paper is its estimates of the effects of replacing uniform metro-wide FMRs with SAFMRs on the neighborhood choices of voucher recipients. Their results indicate that SAFMRs will induce voucher recipients to live in significantly better neighborhoods with minimal effect on the taxpayer cost per recipient and hence the number of recipients who can be served with a fixed budget. This contrasts sharply in both respects with the effect of uniform increases in FMRs across the entire metropolitan area. The paper also contains evidence, however, about whether HUD overpays for voucher units in the worst neighborhoods and whether SAFMR will reduce these overpayments.

The paper's evidence on the pattern of overpayment and underpayment for voucher units appears in Figure B.1 in their online appendix.[16] The figure displays the relationship between the actual

[16] https://assets.aeaweb.org/asset-server/files/6861.pdf

rents and predicted market rents of voucher units in one of their event studies. It indicates that the mean of the actual rents exceeded the mean of the predicted market rents for nearly all levels of predicted market rent, and the difference is largest for units with the lowest predicted market rent. For units with a predicted market rent of about $450 a month in 2010, the estimated overpayment was about 90 percent. These large differences are well outside the range of other estimates. The most plausible explanation is that Collinson and Ganong's predicted market rents for this analysis are based on a hedonic equation with only a few unit and neighborhood characteristics, namely, number of bedrooms, structure age, structure type, and the unit's Public Use Microdata Area (PUMA). The other studies had much better information on housing and neighborhood characteristics.

The paper devotes considerable effort to estimating effects of changes in payment standards on (1) the rents paid for housing units, (2) indicators of neighborhood desirability, and (3) indices of unit desirability and combined unit and neighborhood desirability. These results are directly relevant to the effect of SAFMRs on the degree of overpayment and underpayment. The authors find that exogenous increases in payment standards will lead to much greater percentage increases in the rents of voucher units than in indices of the overall desirability of these units and their neighborhoods. Similarly, exogenous decreases in payment standards will lead to much greater percentage decreases in the rents of voucher units than in indices of the overall desirability of these units and their neighborhoods. If true, replacing current FMR with SAFMR would decrease net overpayment for voucher units in areas with less than average median rents and increase it in other areas.

Although the authors studied the effects of three events that created exogenous variation in payment standards, assembled the best available data for studying these events, and used it well, some uncertainty remains about this conclusion. Because the information on the desirability of the dwelling unit and its neighborhood available for studying two of the three events was meager, it is entirely possible that the increased payment standards led to a much larger percentage increase in the actual as opposed to the measured desirability of the unit and its neighborhood. A sensitivity analysis that attempted to hold constant unit characteristics by using unit fixed effects suggested a much smaller increase in voucher rent relative to housing desirability (Collinson and Ganong, 2018: 74–75). In the one event where detailed information about unit desirability was available, the circumstances arguably did not permit estimation of the long run effect of the increased payment standards. Increases in the payment standard were modest (about 5 percent on average in the first year), the time period studied was short (3 years), and most observations involved sitting tenants. It would not be surprising if few sitting voucher recipients found it in their interest to search for the very slightly better unit made available by the slightly higher payment standard. The effect of the increased payment standards on the desirability of the unit and neighborhood occupied might have been much larger after most recipients had moved from their initial units.

Caveat

It is important to realize that there is an alternative explanation for the preceding empirical results that challenges their interpretation as overpayments and underpayments for voucher units. All of

the empirical literature on this topic is based on the implicit assumption that, among all units that are the same with respect to the observed housing and neighborhood characteristics used to predict the market rents of voucher units, voucher units are neither better nor worse than unsubsidized units with respect to unobserved characteristics. It is reasonable to expect that this assumption is violated in a way that gives the appearance of overpayment in the worst, and underpayment in the best, neighborhoods. The voucher subsidy gives its recipients the resources and incentive to demand much better housing in their current low-rent neighborhoods. Some landlords in these neighborhoods substantially renovate their units to attract and retain voucher recipients (Rosen, 2014). The observed housing characteristics used in empirical studies will capture some of these improvements, but it is reasonable to believe that, among units that are equally good with respect to observed characteristics in these neighborhoods, units occupied by voucher recipients are better in unobserved respects. In the best neighborhoods, voucher recipients live in units that are the worst with respect to observed and unobserved characteristics in order to occupy a unit renting for less than the payment standard. To some extent, the apparent overpayments and underpayments reflect differences in unit quality. Empirical studies with the best data on the characteristics of the dwelling units and their neighborhoods should be expected to have the smallest bias in estimating overpayment and underpayment for voucher units.

Conclusion

The evidence available suggests that HUD overpays for voucher units in the worst neighborhoods. More generally, the current HCV program pays rents to landlords that are usually greater than the mean rents of similar unsubsidized units for the least desirable units and units in the worst neighborhoods. The opposite is true for the most desirable voucher units and units in the best neighborhoods. The mix of units in these categories varies across studies. Some find an aggregate overpayment and others an aggregate underpayment. The weight of the evidence is that these aggregate differences are modest.

These outcomes are the net result of several program features. Ignoring the program's rent reasonableness test and the possibility that tenants can occupy a unit renting for more than the payment standard by paying the entire extra cost, the tenant's rent does not depend on the total rent paid to the landlord for the unit. If the best unit resulting from the tenant's search has an initial asking rent less than the payment standard, the voucher recipient has no incentive to resist a rent increase up to the payment standard. The tenant, however, does have an incentive to find the best possible unit renting for no more than the payment standard. If the tenant's limited search leads to one of these units, the landlord's initial asking rent will be only slightly less than the payment standard and below the mean rents of similar units occupied by unsubsidized households. If the landlord is paid the payment standard for these units, these units would still be underpriced. The rent reasonableness test limits the extent to which HUD overpays for voucher units, especially for the worst units and units in the worst neighborhoods. The possibility that tenants can occupy a unit renting for more than the payment standard by paying the entire extra cost provides a significant fraction of voucher recipients with a strong incentive to avoid overpriced units.

Finally, Collinson and Ganong's results indicate that replacing current FMR with SAFMR would decrease net overpayment for voucher units in areas with less than average median rents and increase it in other areas. They also imply that lowering FMR across-the-board would have modest effects on the desirability of the units and neighborhoods occupied by voucher recipients. If these results are accurate, lowering the FMR would enable us to serve many more households with the same budget without significant negative effects on existing recipients. Since only about one-third of households with extremely low incomes receive any housing assistance, this reform would have considerable merit. It could be achieved gradually by freezing Fair Market Rent at current levels. Alternatively, current recipients could be grandfathered and the new schedule applied only to new voucher recipients. This reduction in base FMR could be combined with a tilting of the schedule using Small Area Fair Market Rent methodology to incentivize families, especially with children, to move to better neighborhoods.

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