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DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

[Docket No. FR-5413-N-01]

**Section 8 Housing Choice Voucher Program –
Demonstration Project of Small Area Fair Market Rents
In Certain Metropolitan Areas for Fiscal Year 2011**

AGENCY: Office of the Assistant Secretary for Policy Development and Research, HUD.

ACTION: Notice of Demonstration Project of Small Area Fair Market Rents (FMRs) in Selected Metropolitan Areas for Fiscal Year (FY) 2011.

SUMMARY: Section 8(c)(1) of the United States Housing Act of 1937 (USHA) requires the Secretary to publish FMRs periodically, but not less than annually, adjusted to be effective on October 1 of each year. The primary uses of FMRs are to determine payment standard amounts for the Housing Choice Voucher (HCV) program, to determine initial renewal rents for some expiring project-based Section 8 contracts, to determine initial rents for housing assistance payment (HAP) contracts in the Moderate Rehabilitation Single Room Occupancy program (Mod Rehab), and to serve as a rent ceiling in the HOME rental assistance program. Today's notice announces a demonstration project that will set small area FMRs for the HCV program within certain metropolitan areas, and requests comments on several topics related to small area FMRs, including how these small areas should be defined. Small area FMRs calculated for the Demonstration projects will be used only in the Section 8 HCV program and will not affect rents in any other HUD or other federal program. HUD expects that small area FMRs will provide Section 8 tenants with greater ability to move into opportunity areas where jobs, transportation, and educational opportunities exist, and prevent undue subsidy in lower-rent areas.

DATES: *Comments Due Date: 60 Days after Publication in the Federal Register*

ADDRESSES: Interested persons are invited to submit comments regarding HUD's small area FMR demonstration, as announced in this notice, to the Office of General Counsel, Rules Docket Clerk, Department of Housing and Urban Development, 451 Seventh Street, SW, Room 10276, Washington, DC 20410-0001. Communications should refer to the above docket number and title and should contain the information specified in the "Request for Comments" of this notice.

Submission of Hard Copy Comments. To ensure that the information is fully considered by all of the reviewers, each commenter submitting hard copy comments, by mail or hand delivery, should submit comments or requests to the address above, addressed to the attention of the Rules Docket Clerk. Due to security measures at all federal agencies, submission of comments or requests by mail often result in delayed delivery. To ensure timely receipt of comments, HUD recommends that any comments submitted by mail be submitted at least 2 weeks in advance of the public comment deadline.

Electronic Submission of Comments. Interested persons may submit comments electronically through the Federal eRulemaking Portal at <http://www.regulations.gov>. HUD strongly encourages commenters to submit comments electronically. Electronic submission of comments allows the commenter maximum time to prepare and submit a comment, ensures timely receipt by HUD, and enables HUD to make them immediately available to the public. Comments submitted electronically through the <http://www.regulations.gov> website can be viewed by interested members of the public. Commenters should follow instructions provided on that site to submit comments electronically.

No Facsimile Comments. Facsimile (FAX) comments are not acceptable.

Public Inspection of Comments. All comments submitted to HUD regarding this notice will be available, without charge, for public inspection and copying between 8 a.m. and 5 p.m.

weekdays at the above address. Due to security measures at the HUD Headquarters building, an advance appointment to review the documents must be scheduled by calling the Regulations Division at 202-708-3055 (this is not a toll-free number). Copies of all documents submitted are available for inspection and downloading at <http://www.regulations.gov>.

FOR FURTHER INFORMATION CONTACT: For technical information on the methodology used to develop small area FMRs, please contact Peter B. Kahn or Marie L. Lihn, Economic and Market Analysis Division, Office of Economic Affairs, Office of Policy Development and Research, telephone number 202-708-0590 (this is not a toll-free number). Persons with hearing or speech impairments may access this number through TTY by calling the toll-free Federal Information Relay Service at 800-877-8339. (Other than the HUD USER information line and TTY numbers, telephone numbers are not toll free.)

SUPPLEMENTARY INFORMATION

I. Background

Section 8 of the USHA (42 U.S.C. 1437f) authorizes housing assistance to aid lower-income families in renting safe and decent housing. Housing assistance payments are limited by FMRs established by HUD for different areas. In the HCV program, the FMR is the basis for determining the “payment standard amount” used to calculate the maximum monthly subsidy for an assisted family (see 24 CFR 982.503). In general, the FMR for an area is the amount that would be needed to pay the gross rent (shelter rent plus utilities) of privately owned, decent, and safe rental housing of a modest (nonluxury) nature with suitable amenities. In addition, all rents subsidized under the HCV program must meet reasonable rent standards.

Currently FMRs are calculated for all nonmetropolitan counties and metropolitan areas. The same FMR is available throughout a nonmetropolitan county or a metropolitan area, which

is generally comprised of several metropolitan counties. FMRs in a metropolitan area represent the 40th-percentile (or in special circumstances the 50th-percentile) gross rent of the entire HUD-defined metropolitan area. Public housing agencies (PHAs) may set a payment standard within 90 percent to 110 percent of the FMR. PHAs may determine that payment standards that are higher than 110 percent, or lower than 90 percent, are needed to make the voucher program work in subareas of their market; in this instance, a PHA would request HUD approval for payment standards below 90 percent or exception payment standards above 110 percent. These requests cannot represent more than 50 percent of the population of the area (see 24 CFR 982.503).

In the past, HUD has not had the means to maintain and update a small area FMR system. In late 2010, the Census Bureau will make publicly available the data it collected over the first 5 years of the American Community Survey (ACS) in 5-year aggregations for the areas with population of less than 20,000. With these data, HUD will be able to update FMR estimates in smaller geographic areas than is currently possible using ACS data at one-year or 3-year aggregations. HUD intends to use this data to establish a program of smaller area FMRs for metropolitan areas. To determine how best to implement a comprehensive small area FMR program, HUD will operate small area FMR demonstration projects for the HCV program using 2000 Census data to determine FMRs for smaller areas. HUD expects that small area FMRs will provide Section 8 tenants with greater ability to move into opportunity areas, where jobs, transportation and educational opportunities exist, and prevent undue subsidy in lower-rent areas. Small area FMRs will alter some administrative responsibilities of PHAs that administer housing voucher programs, but it is unclear what the net effect will be. For example, small area FMRs are likely to reduce the time needed to determine whether rents are reasonable. (Rent reasonableness tests reflect the conditions and characteristics of units relative to others in the

area, as well as market rents in the immediate area of the units.) While the requirement to determine rent reasonableness based on the condition and characteristics of individual units will remain, less comparative data may be needed, since local area baseline rents will largely be embedded in the small area FMR. Small area FMRs will also increase the number of payment standards used in a metropolitan area. The small area FMR demonstration projects will provide HUD with insight into the administration of small area FMRs before implementing such a program nationwide.

The first demonstration projects will begin October 1, 2010 (the beginning of FY2011), with others being added prior to the beginning of Calendar Year 2011. Small area FMRs would be rolled out to all metropolitan areas at a later date, provided that the small area FMR demonstration project shows that voucher program operation using small area FMRs is feasible.

For illustrative purposes, the following website provides hypothetical Small Area FMRs that are based on the current FY2010 FMRs: <http://www.huduser.org/portal/datasets/fmr.html>. Comments may be provided on these FMRs.

Electronic Data Availability: This Federal Register notice is available electronically from the HUD website at <http://www.hudclips.org>. Federal Register notices also are available electronically from the U.S. Government Printing Office website, <http://www.gpoaccess.gov/fr/index.html>.

II. Methodology for Small Area FMRs

Currently, FMRs are determined based on Office of Management and Budget (OMB) Core Based Statistical Areas (CBSAs), with some modifications based on pre-FY2006 FMR area definitions for metropolitan areas. For nonmetropolitan areas, the basic unit of geography is at

the county level.¹ The standards for definition of CBSAs are based on a review of journey-to-work data, or commuting patterns, as the basis for grouping counties together to form CBSAs.²

Use of metropolitan area-wide FMRs allows HUD's Section 8 Voucher tenants access to different parts of a metropolitan area; however, because FMRs generally are set at the 40th percentile of the metropolitan rent distribution, certain neighborhoods may not have many units available in the FMR range. That is why HUD has an exception payment standard policy that allows payments standards to be set much higher than the FMR, but the policy is dependent on a showing of program need in terms of whether or not suitable housing is available. To make a broader range of neighborhoods accessible to its clients, HUD is researching ways to set FMRs at a more localized level. Currently, HUD is focusing on a methodology that would use small areas, defined by U.S. Postal Service ZIP codes, as the basis for FMRs in metropolitan areas. For nonmetropolitan areas, counties would continue to be used as the basis for FMRs.

The most recent data regarding rents, incomes, and other socio-economic information collected by the U.S. Census Bureau comes from the ACS. At this time, only one-year and 3-year ACS tables are available. ACS 5-year data are expected to have sufficient data at the small area level available to permit the calculation of statistically reliable FMRs for many ZIP codes in metropolitan areas. However, the first publication of 5-year ACS data does not begin until after October 1, 2010, so for the FY2011 small area FMR demonstration projects, HUD will have to use a different data source; HUD will use data from the 2000 Decennial Census to estimate the rent relationship (rental rate ratio) between the OMB-defined CBSA and each ZIP code within

¹ In some sparsely populated counties where statistically reliable information was not available from the 2000 Decennial Census, county groups are used instead.

² OMB published a Federal Register notice (65 FR 82228), available at <http://www.whitehouse.gov/omb/fedreg/metroareas122700.pdf>, that outlined its decisions for how to create CBSAs and responses to public comments concerning the formation of CBSAs.

the given metropolitan area.³ The individual ZIP code-level 2-bedroom FMR for each part of the FMR area is the product of the rental rate ratio and the 2-bedroom FMR for that area's CBSA as calculated using methods employed for past metropolitan area FMR estimates.

Before a rent relationship can be determined, HUD first eliminates any records where there were no units with occupants paying cash rent. HUD then aggregates these rental distribution data for each CBSA and calculates a median (50th-percentile) gross rent across all bedroom sizes. These CBSA median gross rents serve as the denominator in the rent relationship calculation. HUD then aggregates the rental distributions for each ZIP code within a given CBSA (ZIP codes can cross county boundaries; therefore, there may be multiple records for each ZIP code within a single CBSA, and HUD aggregates these multiple records). A median gross rent is calculated for each ZIP code (or ZIP code part for ZIP codes spanning CBSA boundaries). HUD restricts the use of ZIP code level median gross rents to those areas that have at least 1,000 cash rental unit observations. HUD anticipates that the set of ZIP codes with at least 1,000 cash renter-occupied units in the 2000 Decennial Census will be representative of the set of ZIP codes with statistically valid 5-year ACS data that can be used to set small area FMRs.

The rent relationship is calculated in the following manner for those ZIP codes within the metropolitan area that have 1,000 or more cash rental units:

$$\text{Rental Rate Ratio} = \text{Median Gross Rent for ZIP Code Area} / \text{Median Gross Rent for CBSA}$$

³ Note that some ZIP codes span metropolitan area boundaries so that a ZIP code may contain parts of a metropolitan area and one (or more) nonmetropolitan county (counties), or part of another metropolitan CBSA. As in current FMR policy, nonmetropolitan counties would not be broken along ZIP code or any other lines under the small area FMR policy. ZIP codes that span more than one metropolitan CBSA would have different FMRs in each CBSA as they do under current metropolitan FMR policy.

The rent relationship is capped at 150 percent for areas that would otherwise be greater. If the ZIP code within the CBSA does not have 1,000 cash rental units, then the rent relationship is calculated as:

$$\text{Rental Rate Ratio} = \text{Median Gross Rent STCO} / \text{Median Gross Rent of the CBSA}$$

where STCO is the county within the state containing the ZIP code.⁴ For metropolitan areas, FMRs will be calculated and published for each small area. ZIP codes were chosen because they localize rental rates and a unit's ZIP code is easily identified both by PHAs and by tenants.

As previously stated, the individual ZIP code level 2-bedroom FMR for each part of the FMR area is the product of the rental rate ratio and the 2-bedroom FMR for that area's CBSA, as calculated using methods employed for past metropolitan area FMR estimates. To set the floor for small area FMRs in a metropolitan area, this product is then compared to the state nonmetropolitan minimum 2-bedroom rent for the state the area is located in and, if the ZIP code rent determined using the rental rate ratio is less than the minimum, the ZIP code rent is set at the nonmetropolitan minimum for that state. The relationship between 2-bedroom units and other bedroom sizes has been estimated from Decennial Census data and then held constant until superseded by more recent data. Small area FMRs for other bedroom sizes will be calculated based on the bedroom-size relationships estimated for the large area of geography. HUD anticipates updating the bedroom rental rate ratios with the release of 5-year ACS data (covering 2005 through 2009), and then once every 5 years when the 5-year ACS sample is completely replaced.⁵ The final calculated rents are then rounded to the nearest \$25.

⁴ For ZIP codes with fewer than 1000 cash rental units that cross county boundaries, the median gross rent in the numerator is calculated as the rental unit weighted average of the median gross rents for each county containing the ZIP code.

⁵ The current decennial data is not robust enough to lead HUD to believe that updating bedroom ratios on a more frequent basis would provide many changes. The current bedroom ratios are constrained by ranges that reflect the

Small area FMRs for all metropolitan areas are available for viewing and download on the Internet at <http://www.huduser.org/portal/datasets/fmr.html>. These will be updated using FY2011 FMRs and posted on the website when the proposed FY2011 FMR notice is published. Small area FMRs calculated for the demonstration projects will be used only in the Section 8 HCV program and will not affect rents in any other HUD or other federal program. PHAs in small area FMR demonstration sites will be empowered to renew pre-existing HAP contracts based on payment standards outside the new basic range (90 to 110 percent of the small area FMR) for tenants who wish to remain in their existing units and whose existing payment standards would otherwise fall outside the new basic range due to the implementation of the small area FMR demonstration project.

III. Requirements for Participation in the Small Area FMR Demonstration Project

The small area FMR demonstration project is intended to cover a limited set of FMR areas so that HUD can provide adequate technical assistance to the participating PHAs and monitor the effects and effectiveness of the policy. At the same time, HUD seeks to have all PHAs in small area FMR demonstration project areas firmly committed to implementing the program to achieve its stated goals. HUD will apply three principles for selecting participating FMR areas if participation needs to be limited because too many areas volunteer: (1) the participant area is large enough that small area FMRs will result in substantial variation in rents, (2) the greatest possible proportion of voucher tenants are served by PHAs that are willing participants in the demonstration, and (3) the PHAs in the area have demonstrated previous commitment, within the flexibilities available in the voucher program, to set voucher payment standards at varying and appropriate levels.

average relationship of a given bedroom size to the 2-bedroom rent, and, for the 3-bedroom and 4-bedroom rents, bonuses have been added to assist with the operation of the Section 8 program.

Larger FMR areas provide the greatest potential benefit from the small area FMR proposal in that they are likelier to have a wider array of market rents that can be captured by the proposed methodology. HUD may therefore limit participation in the small area FMR demonstration project to FMR areas meeting the size (100 or more census tracts) and affordable housing concentration (in less than 70 percent of their census tracts containing 10 or more rental units, at least 30 percent of rental units rent for the 40th-percentile two-bedroom FMR or less) criteria for eligibility for the 50th-percentile FMR at 24 CFR 888.113.

The small area FMR demonstration project will not be effective unless the PHAs that operate voucher programs covering the vast majority of voucher tenants in a metropolitan area agree to participate and abide by the small area rents. Therefore, HUD is requiring that PHAs requesting participation in the small area FMR demonstration project must account for at least 80 percent of the voucher tenants in that metropolitan area. If the PHAs represent a smaller percentage of the voucher tenant population, they will not be able to participate. HUD will consider as evidence a joint letter requesting participation in the small area FMR demonstration project, signed by the Executive Director and/or Board Chair of each PHA in the metropolitan area jointly making the request. HUD will verify, using data for Calendar Year 2009, that the signatories represent at least 80 percent of the voucher tenants residing in each nominated metropolitan area. HUD will notify the PHAs if they are found to represent fewer than 80 percent of voucher tenants in the metropolitan area, so that they may enlist participation by additional PHAs in the metropolitan area.

Applicants who provide evidence that they are using multiple payment standards or that use exception payment standards may be given priority for participating in the demonstration project. Through their current operating procedures, these applicants are already showing the

ability and willingness to administer the project using multiple rent structures and are likely able to provide HUD with valuable feedback on the small area FMRs HUD calculates and provides.

IV. Request for Public Comment on Small Area FMRs and Demonstration Eligibility

Criteria

Before HUD institutes the small area FMR demonstration project, HUD would like to solicit comments on the implementation of small area FMRs. The following is a list of issues that maybe addressed in comments:

- Should HUD institute caps and floors on small area FMRs? As proposed, the current cap is 150 percent of the metropolitan FMR, and the current floor is the state nonmetropolitan minimum FMR. Are these appropriate, or should they be changed or eliminated? What is an appropriate amount or percentage for caps and floors?
- The use of small area FMRs in metropolitan areas will result in no areas being big enough to qualify for 50th-percentile FMRs. (The goal of the 50th-percentile FMR policy should be more efficiently addressed through the use of small area FMRs.) Should HUD revise the 50th-percentile FMR policy or eliminate it, and why?
- The exception payment standard policy, which is based on a relationship like that used to set the small area FMRs, will generally be redundant and could therefore be eliminated if the small area FMR policy is adopted. Are there any instances where an exception payment standard policy might still be useful? Such instances could include, for example, areas where rents have changed so rapidly due to extraordinary circumstances (such as natural

disasters, or rapid economic change) that existing statistical methods cannot determine accurate rents, but PHAs can show that their voucher program operations have been impacted. If the exception payment standard policy remains in effect, should the exceptions be continued for nonmetropolitan counties only, or for larger areas within a metropolitan area?

- Do small area FMRs increase the administrative burden of PHAs, and if so, how can this be reduced?
- Is the proposed rounding protocol of \$25 appropriate, or should small area FMRs be rounded to a larger or smaller amount?
- Should state minimums be rounded both up and down? Should they be rounded before comparison with a ZIP code rent?

In addition, comments may discuss the proposed HUD methodology for the small area FMRs that would be used for the demonstration project, including the use of 2000 Census data for the demonstration projects and the anomalies created by that data; using 5-year ACS data and implementing small area FMRs in metropolitan areas only; addressing the need, if it exists, for small area FMRs in nonmetropolitan counties; and addressing the general need for and implementation of a small area FMR demonstration project.

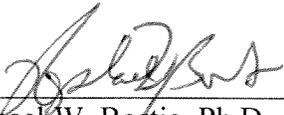
HUD also seeks comments on the eligibility criteria for the small area FMR demonstration project. Should the demonstration be open to smaller metropolitan areas than those meeting the size criterion for 50th-percentile FMR eligibility? Should, or should not, the affordable housing concentration criterion be a consideration in selecting participating areas? Is the 80 percent-of-voucher-tenants standard appropriate? Is there a better way for PHAs to

demonstrate commitment to the demonstration project than a joint letter to HUD? Is demonstrated past use of multiple payment standards an appropriate criterion for participation?

V. Implementation of the Small Area FMR Demonstration Program

The first small area FMR demonstration projects for the HCV program are expected to be put in place on October 1, 2010, after a review of all comments, when FY2011 FMRs become effective. Other demonstration areas may be added between this date and the beginning of Calendar Year 2011. For illustrative purposes, hypothetical small area FMRs that are based on the current FY2010 FMRs are available for review on the HUD USER website at <http://www.huduser.org/portal/datasets/fmr.html>. The Federal Register notice on proposed FY2011 FMRs will include an update of these potential small area FMRs and the selection criteria for areas interested in being a part of the demonstration project. The demonstration project will operate for approximately one year before a complete national implementation of small area FMRs will be proposed. The timing of full implementation will be determined based on the outcomes of the demonstrations.

Dated: May 12, 2010



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