

Eligibility Determination on an Amended Project

August 23, 1990

MEMORANDUM FOR: David P. Forsberg, Regional Administrator
Regional Housing Commissioner, 1S

ATTENTION: Frank V. Del Vecchio, Director,
Community Planning and Development, 1C

FROM: Anna Kondratas, Assistant Secretary for Community
Planning and Development, C

**SUBJECT: Request for Eligibility Determination - India Point Marina Project CDBG Program
Providence, Rhode Island**

We are in receipt of a memorandum dated January 18, 1990, from Robert Pacquin, requesting an eligibility determination of a \$2.5 million CDBG loan provided by the City of Providence, Rhode Island to a developer for construction of a project. The City considers the project eligible as an economic development activity pursuant to 24 CFR 570.203(b) since the originally planned condominium complex was never constructed and the project was purportedly revised to include just a marina and a restaurant. We apologize for the delay in responding to your request, however, the issues presented were complex and raised policy issues without precedent.

Background

It is our understanding, from reviewing the documentation attached to the memorandum, that a private lender, Fleet National Bank, agreed to provide interim financing to a developer for the India Point Marina Project which was to consist of a marina and condominium housing complex. The bank was willing to provide construction financing in the amount of \$39.6 million, provided it was able to obtain the participation of other lenders for a minimum of \$24.6 million of the total. However, the bank was unable to obtain the required participation and thus withdrew the commitment.

At that point, the developer had an outstanding debt of approximately \$5 million to the bank, there was no financing in place for this debt, and no income revenue from the project. The bank agreed not to foreclose on the outstanding loan of \$5 million as long as the City provided an interim, low interest loan for \$2.5 million and applied for assistance under the Section 108 Loan Guarantee program in the amount of \$6 million. The City agreed to step in and provided \$2.5 million in CDBG funds in the form of interim financing to the developer to partially repay the outstanding debt to Fleet National Bank. The Section 108 loan application that has been submitted to HUD, if approved, was excepted to be used to repay the \$2.5 million to the CDBG program, \$2.5 million to the bank for the balance of its outstanding \$5 million loan, and the remainder to begin construction of the marina (which was expected to generate profit from the sale of marina slips. As a point of information, however, Section 108 funds cannot be used to reimburse

the grantee's program account for the \$2.5 million loan to the developer, according to the requirements of 570.701.

Issues

The CDBG funds were provided in the form of interim financing. An activity financed using this method is treated as any other CDBG-assisted activity. This means that it is subject to all pertinent laws, regulations, and rules such as national objectives, eligibility, citizen participation, Davis-Bacon, environmental requirements, etc.

The City contends that the activity was carried out under 24 CFR 570.203(b) which permits assistance in a variety of forms to for profit entities to carry out economic development projects. In determining whether the use of \$2.5 million in CDBG funds to repay the bank for an outstanding debt was an eligible activity, two pertinent issues have been raised: whether the assisted activity was, or was part of, an economic development project, and whether the grantee otherwise complied with program requirements.

Assistance provided to for-profits under 570.203(b) must be for an economic development project. The provision further requires the grantee to conduct a "necessary or appropriate" analysis to determine that the "amount of any financial assistance to be provided is not excessive, taking into account the actual needs of the business in making the project financially feasible and the extent of public benefit expected to be derived from the economic development project." To demonstrate compliance with this provision, therefore, the grantee must delineate what the economic development project is to consist of and, within the context of this description, show what the CDBG funds will be expended for. The process of clearly defining the CDBG- assisted portion of the project is important because certain activities carry with them other requirements, e.g., a CDBG- assisted construction activity generally requires the payment of Davis-Bacon wages.

The City stated on page two of its August 8, 1989, letter to your office that, in carrying out its necessary or appropriate analysis, it relied, in part, "on the professional review of Fleet National Bank as to the reasonableness of the project costs." It is our understanding, however, that the bank's loan to the developer was for the construction of the condominium with the marina to be built at a later point in time. Therefore, we find inconsistent the City's statement, in its November 15, 1989, correspondence to your office, that "the project which the City partially funded through the Float mechanism at no time included or even contemplated housing." Since the original project financed by the bank was to consist of the condominium complex and a marina, it is unlikely that the bank had project costs related to a restaurant. HUD has not been shown any documentary evidence to demonstrate that, at the time CDBG assistance was provided, the project had, in fact, been restructured as an economic development project consisting solely of a marina and a restaurant. In fact, a July 19, 1989, amendment to The Foundry Urban Development Action Grant (UDAG) sought to amend an existing UDAG to permit the construction of 60 residential condominium units along with a 250 room all-suite hotel on the India Point site. This amendment was filed several months subsequent to the CDBG float loan which had been provided to the developer in April, 1989. The insufficient and inconsistent information does not permit us to conclude that the assisted activity met the requirements of 570.203(b) as assistance to a for-profit business for an "economic development" project.

We therefore support your conclusion that the activity is ineligible. In the absence of an adequate necessary or appropriate analysis based upon a clearly defined, reconfigured project, it appears that the loan was used simply to replace financing provided by the bank to support the construction of the new housing (condominiums). As you stated, 570.203 specifically prohibits the use of CDBG funds under special economic development activities to assist the construction of new housing. It is further prohibited under 570.207(b)(3).

Notwithstanding the eligibility issue, we believe the City failed to comply with the presubmission requirements specified at 570.301. Discussion with Field Office staff indicates that the activity was not described in sufficient detail prior to the City's amendment of the final statement to allow citizens to determine the degree to which they may be affected. This is particularly important for activities funded using interim financing techniques wherein activities already described in a final statement may be delayed or otherwise adversely impacted if the loan is not repaid in a timely manner.

It further appears that the grantee failed to comply with HUD's required environmental review procedures. Page five of the grantee's August 3, 1989, letter to your office states that ". . .once the City agreed to commit funds to this project, an environmental review in accordance with 24 CFR 58 was conducted." However, an environmental monitoring review conducted by HUD Field staff on August 3, 1989, found no evidence that the City complied with the provisions of 24 CFR Part 58 or with requirements regarding the release of funds.

Conclusion

We do not see the need to comment on the issue of national objectives since your memorandum indicates that it is unclear as to which objective would ultimately be claimed. This point is moot, however, given that we support your determination of ineligibility of the \$2.5 million loan for the following reasons: (1) no evidence that the loan was made for an economic development project; (2) inadequate documentation of a necessary or appropriate determination; (3) the prohibition against the use of CDBG funds under 570.207 for construction of new housing; and (4) failure to comply with applicable rules and regulations concerning citizen participation and environmental review requirements. We therefore support your efforts to require the grantee to undertake appropriate corrective actions.