

Use of CDBG Funds in Support of Housing

February 17, 1989

U.S. Department of Housing and Urban Development

Community Planning and Development

Special Attention of

All Regional Administrators Notice

All Regional CPD Directors

All Category A Field Office Managers Issued: February 17, 1989

All CPD Division Directors

CDBG Entitlement Grantees Expires: February 17, 1990

CDBG State Grantees

Cross References

SUBJECT: Use of Community Development Block Grant Funds in Support of Housing

This notice describes ways in which the Community Development Block Grant (CDBG) program may contribute to affordable housing initiatives and to expanding housing opportunities in communities. It updates information provided in CPD notice 80-18.

While this notice contains no new policy interpretations, it brings together some ideas for using CDBG funds for housing which are contained in various sections of the Block Grant regulations. The list contains all those which come to mind; but it is, undoubtedly, not exhaustive. You are encouraged to inform us of other ideas, so that those can also be shared.

The notice focuses on eligible activities in support of affordable housing. In all instances, a CDBG-funded activity must meet a national objective -- either benefiting low and moderate income persons, eliminating conditions of slums or blight, or meeting a particularly urgent community development need. Applicable criteria for meeting a national objective are given in section 570.208 of the CDBG regulations. The Guide to CDBG Eligible Activities gives descriptions of national objectives requirements for individual activities.

Grantees may contact their field office CPD representative to discuss this notice.

Field Office actions: Field offices should make this notice available to their staff and CDBG entitlement grantees and States. Staff should be prepared to advise grantees on how housing activities may meet a national objective since that topic, although not a subject of this notice, is integral to determining fundability. For inquiries relating to entitlement grantees, contact the Entitlement Cities Division at FTS 755-5977; for those relating to States, contact the States and Small Cities Division at FTS 755-6322.

New Housing Construction

Using CDBG funds for new housing construction may substantially lower the purchase price of homes and apartments. The savings may be passed on to buyers and renters in the form of lower monthly mortgage and rent payments. The result is more affordable housing in the community.

Grantees may use CDBG funds in four ways for new housing construction, provided a national objective is met:

1. Construction by eligible subrecipients. The regulations at section 570.204(a) allow for certain "eligible subrecipients" to receive CDBG funds for constructing housing. The eligible subrecipients are described in section 570.204(c) as neighborhood-based nonprofit organizations (NBOs), section 301(d) Small Business Investment Companies (SBICs), and local development corporations (LDCs).
2. Two further requirements are imposed by section 570.204(a). To receive funding, eligible subrecipients must be undertaking a neighborhood revitalization, community economic development, or energy conservation project with the CDBG funds. And, the grantee must determine that the project is necessary or appropriate to achieve its community development objectives.
3. Eligible subrecipients must carry out the project in name and in deed. Although inexperienced eligible subrecipients may need technical assistance from the grantee, the eligible subrecipient must actually be implementing the activity.
4. Last resort housing. Under 24 CFR Part 42, Subpart I, grantees may construct housing of last resort. Grantees are limited to constructing housing for displacees of a CDBG project, subject to the Uniform Act, when the project is prevented from proceeding because comparable replacement housing is not available otherwise. [section 570.207(b)(3)(i)]

Limited new construction after failed rehabilitation. Grantees may substantially reconstruct, on the same site, housing which is owned and occupied by low and moderate income persons where the need for the reconstruction was not determinable until after CDBG-assisted rehabilitation began. [section 510 of the Housing and Community Development Act of 1987]

Limited new construction with neighborhood rehabilitation efforts. When a final rule is published defining criteria relating to such activities, grantees may reconstruct housing as part of a neighborhood rehabilitation effort where the grantee has determined beforehand that the house is not suitable for rehabilitation. The grantee must demonstrate to the satisfaction of the Secretary of HUD that the cost of substantial reconstruction is significantly less than the cost of new construction and less than the fair market value of the property after substantial reconstruction. [section 510 of the Housing and Community Development Act of 1987]

It should be noted that, except as provided for above, grantees are prohibited under section 570.207(b)(3) from constructing new housing using Block Grant funds. These regulations prevent grantees from acting as developers, themselves, with CDBG financing and from directly financing new housing. Grantees are also prohibited from acquiring newly constructed housing with CDBG funds. In addition, new housing construction by private developers is not eligible for CDBG assistance under section 570.203(b), because such projects are not deemed economic development projects under the

requirements of that section.

Activities Aimed At Reducing Costs For Private Development

Using CDBG funds to lower the cost of private development is another way of making housing affordable. Lower land costs and improved sites may reduce the ultimate sale price for homes or monthly rent for apartments.

Grantees may, alone and in combination with constructing housing as described above, use CDBG funds in support of housing construction under the following circumstances, provided a national objective is met:

Acquisition of sites. Grantees may acquire property to be used for housing and resell it at a lower price to developers. [section 570.201(a) and (b)].

Clearance of sites. Grantees may clear a site to be used for housing. [section 570.201(d)]

Site improvements. Grantees may improve publicly-owned sites for housing. [section 570.201(c)] Using CDBG funds for improvements to a site after disposition to a private developer is eligible only if carried out by an eligible subrecipient, in which case the activity must be for neighborhood revitalization, community economic development, or energy conservation and the grantee must determine that it is necessary or appropriate to achieve community development objectives. [section 570.204(a)]

Payment of soft costs. Entitlement grantees may pay certain "soft costs" associated with developing new housing identified in their Housing Assistance Plans (HAPs). For HUD-administered small cities recipients, payment of soft costs is limited to those associated with the construction of units where at least 20 percent of the units in each project will be occupied at affordable rents/costs by low and moderate income persons. [section 570.206(g)]

These pre-construction costs are eligible if they are necessary to construction and if they occur prior to construction start. Some examples of pre-construction activities are: Preliminary surveys and analyses of market need, site and utility plans, preliminary cost estimates, sketch drawings, and application processing fees.

Activities Aimed at Facilitating Private Development

Grantees may be able to encourage private developers to construct housing and in some cases, to increase housing affordability by carrying out public improvements in the area. These costs may be borne by CDBG funds. Moreover, grantees may use CDBG for certain planning activities which have the aim of increasing private housing development.

Grantees may use CDBG funds to facilitate housing construction in the following circumstances, provided a national objective is met:

Construction or reconstruction of utilities. Grantees may provide water, sewer, and utility lines on public property in support of housing as public facilities and improvements activities. [section 570.201(c)]

However, the lines and connections on private property which are normally the responsibility of the owner are ineligible, except when undertaken as part of a rehabilitation activity. [section 570.202(b)(6)]

Street improvements. The construction or reconstruction of publicly-owned streets, bridges, and alleys is eligible as a public facilities and improvements activity. [section 570.201(c)]

Parks, neighborhood facilities, and recreation centers. Construction of and improvements to publicly-owned facilities are eligible for CDBG funding as public facilities and improvements activities. [section 570.201(c)]

Development of codes and ordinances. Grantees may, as a planning activity, develop or revise codes, ordinances, and regulations and streamline processing of permits that facilitate the provision of housing. [section 570.205(a)(4)(v)] As planning, these activities are subject to the 20 percent funding limitation on planning and administrative costs, but exempt from national objectives requirements.

Conversion and Acquisition of Existing Structures for Housing

A community may increase its supply of housing by converting buildings to housing units. Existing housing units may become more affordable when grantees acquire those units and sell or lease them at reduced prices.

Grantees may use CDBG funds to finance conversions and acquisitions in the following ways, provided a national objective is met:

Conversion. The costs of converting an existing non-residential structure to residential use is eligible as a rehabilitation activity. [section 570.202(e)]

Acquisition for rehabilitation. CDBG funds may be provided to private individuals and private for-profit entities to acquire property for the purpose of its being rehabilitated. The property may then be rehabilitated and used or sold for residential purposes. [section 570.202(b)(1)]

Acquisition for housing. Grantees may acquire housing units, as long as the units are not newly constructed, and either lease or sell them for residential purposes. [section 570.201(a) and (b)] CDBG regulations do not limit the amount of write-down to the buyer. The property may even be donated to purchasers. Of course, grantees will want to analyze the situation to avoid giving windfall profits to purchasers. [section 570.505]

Grantees may use CDBG funds to finance or to supplement the financing of acquisition of properties in their Urban Homesteading programs.

Initiatives to increase private participation. The supply of affordable rental units may be increased when grantees use CDBG funds to undertake special outreach activities which result in greater landlord participation in Section 8 Housing Assistance Payments Program-Existing Housing, the Rental Rehabilitation Program, or similar programs for low and moderate income persons. These activities are eligible, as administrative costs, when linked with housing identified in the HAP. [section 570.206(g)] As

administration, these activities are subject to the 20 percent funding limitation on planning and administrative costs, but exempt from national objectives requirements.

Rehabilitation

CDBG funds may be used in a variety of ways to rehabilitate publicly- and privately-owned housing, including manufactured housing that is part of the community's permanent housing stock. With CDBG funds providing a grant or a low interest loan for rehabilitation, housing can be improved without appreciably increasing an owner's or renter's housing costs.

The following are among the ways CDBG funds may be used for housing rehabilitation, provided a national objective is met:

Direct loans and grants. Grantees may provide loans and/or grants to property owners for rehabilitation. [section 570.202(b)]

Loan guarantees. Grantees may use CDBG funds as a loan guarantee in order to encourage lending institutions to make loans available to homeowners for rehabilitation, to encourage them to lend in neighborhoods where they are not currently doing so, and to induce them to lend at more favorable rates. [section 570.202(b)]

In guaranteeing the loans, grantees may not deposit CDBG funds in the lending institution (unless it can be determined that without such a deposit the loans will not be made), but merely be prepared to pay in the event of loan default. If needed, deposits must be limited to expected losses, which should equal only a small percent of the amount lent.

Subsidies and reductions. CDBG funds may be used in combination with funds from lending institutions to reduce monthly interest or principal payments. [section 570.202(b)]

Bonding. Grantees may pay, as part of rehabilitation services, the cost of a rehabilitation contractor's performance and payment bonding, as needed to carry out CDBG-funded rehabilitation activities. [section 570.202(b)(9)]

Use of lump sum accounts. Grantees may draw funds from the letter of credit in a lump sum to establish a rehabilitation fund in one or more lending institutions for the purpose of financing rehabilitation of privately-owned properties. The fund may be used along with various financing mechanisms. Funds may be used as a grant only with the purpose of leveraging non-CDBG funds for rehabilitation of the same property.

The lump sum account requirements limit the size of the drawdown and set times during which lending must take place. The requirements state that the lump sum deposit must result in appropriate benefits in support of the grantee's rehabilitation program. See section 570.513 for details.

Section 312 Rehabilitation Loan Program, Urban Homesteading, and Rental Rehabilitation Program. CDBG funds may be used in combination with the Section 312 program, Urban Homesteading, and

Rental Rehabilitation Program (RRP) for rehabilitation activities themselves and/or for costs of administering the program, provided a national objective is met. [section 570.202(b)(9) and (10)]

Costs associated with HAP implementation. CDBG funds may be used for necessary administrative expenses in planning or obtaining financing for housing units identified in the HAP. [section 570.206(g)] As administration, these activities are subject to the 20 percent funding limitation on planning and administrative costs, but exempt from national objectives requirements.

Housing Payments for Owners and Renters

Grantees are prohibited by section 570.207(b)(4) from making payments to persons for acquisition, construction, or rental of housing unless the activity qualifies under section 570.204(a). The regulations at section 570.204(a) allow eligible subrecipients to receive CDBG funds for making such housing payments to persons, as long as it is part of, or it qualifies as, a neighborhood revitalization, community economic development, or energy conservation project and the grantee determines that the project is necessary or appropriate to achieve community development objectives.

The following are some ways eligible subrecipients may use income payments to reduce housing costs for families and individuals, provided a national objective is met:

Down payments. CDBG funds may be used for a down payment on a new or existing home.

Closing costs. CDBG funds may pay the closing costs of a home purchase.

Monthly housing payment. CDBG funds may pay all or part of monthly mortgage or rent payments.

Housing Counseling

A community may effectively utilize its housing resources by operating a housing counseling program. Such a program provides information, advice, and assistance to homebuyers, homeowners, and renters with the goal of preventing loan defaults, foreclosures, non-payment of rents, and assisting home buyers. These programs often complement local "bricks and mortar" programs. As public services, these activities are subject to the 15 percent (for most grantees) funding limitation on public service obligations.

The following are examples of housing counseling activities that may be funded with CDBG, provided a national objective is met:

Pre-purchase counseling. Grantees may fund, as a public service activity, counseling programs for those interested in purchasing a home. The counseling generally consists of information on financial responsibilities, budgeting, housing needs, housing quality, maintenance requirements, and costs associated with home purchase. [section 570.201(e)]

Homeownership counseling. In a similar way, grantees may carry out homeownership counseling. Here, the emphasis is on financial management, debt management, and maintenance needs. Included are

default counseling, counseling under HUD's assignment program, foreclosure prevention counseling, and relocation counseling. [section 570.201(e)]

Renter counseling. Grantees may provide counseling for delinquent renters, those facing eviction, and for landlords and tenants on responsibilities, repair and maintenance, and availability of rental assistance.

Emergency housing counseling. Housing counseling may be provided for all residents affected, or to be affected, by plant closings and acquisitions. [section 570.201(e)]

Shared housing opportunities. Grantees may fund counseling or other informational programs for elderly to learn about sharing their dwelling with others and, thereby, reducing their cost of housing. [section 570.201(e)]

Fair Housing Activities

Communities may undertake fair housing activities with CDBG funds, including actions to affirmatively further fair housing. These activities are directed toward increasing housing choice and informing the community about fair housing rights. Fair housing activities are eligible as administrative activities, subject to the 20 percent funding limitation but exempt from national objectives requirements.

The CDBG regulations in section 570.904(c) set out review criteria for assessing a grantee's performance against its affirmatively furthering fair housing responsibilities. The regulation also contains a definition of the term fair housing choice.

The following are some examples of fair housing activities and of actions to affirmatively further fair housing which may be supported by CDBG funds:

Outreach, counseling, referral. CDBG may pay the costs of outreach, counseling, or referral services to assist persons seeking housing outside areas containing a high proportion of lower income persons. [section 570.206(c)]

Fair housing counseling. Grantees may fund fair housing counseling programs in the community. The programs provide information on fair housing rights and on the availability of housing in a wide variety of locations, emphasizing housing choice. [section 570.206(c)]

Fair housing counseling may also be funded as a public service activity, provided a national objective is met. Then, the activity would be subject to the public service funding limitation. [section 570.201(e)]

Modification of ordinances. CDBG funds may be used to pay the administrative costs of modifying local ordinances and land use measures in pursuit of housing opportunity. [section 570.206(c)]

Information programs. Grantees may support training and education programs for real estate agents, housing managers, city officials, and others to increase knowledge of techniques for promoting economically and racially integrated housing. They may also carry out promotional activities to initiate

housing proposals in areas outside those with a high proportion of lower income persons. [section 570.206(c)]

Enforcement. Grantees may undertake improvements in enforcement of fair housing laws and ordinances and in complaint resolution mechanisms. [section 570.206(c)]

Co-operation. As an administrative activity, grantees may enlist the participation of local real estate brokers and mortgage lenders in promoting open housing and in reviewing mortgage credit analysis and underwriting criteria to determine whether they may have an adverse impact on housing opportunities for minorities and women. [section 570.206(c)]