



# The Economic Development Toolkit

## A Practical Guide to Constructing Your Economic Development Programs

*Spring 2010*



# Welcome

- HUD's Office of Community Planning and Development
- Training conducted by Training & Development Associates and Lockheed Martin
- Trainers
  - Peg Barringer
  - Rocky Wade



# Participant Introductions

- Name
- Agency/Organization
- Typical ED activities at your organization
- The most important question/issue to you



# Learning Objectives

- Be familiar with types of ED strategies/activities
- Be able to determine eligibility and appropriateness of ED projects or programs for CDBG
- Understand how ED meets CDBG national objectives
- Comprehend Revitalization Strategies
- Recognize options for financing ED
- Grasp basics of financial underwriting
- Know requirements & process for Section 108



# Agenda

- Day 1
  - Economic development strategies
  - CDBG overview – history, activities, national objectives, public benefits, program caps
- Day 2
  - Administration
  - Financing ED projects
  - Underwriting
  - Section 108 and brownfields
  - Large-scale development



# Agenda (cont)

- Day 3
  - Infrastructure
  - Small business development
  - Revitalization strategies – NRSA, CRSA
  - Job training and other public services



# Logistics

- Ask questions!
- Case study activities
- Breaks & lunch
- Facilities
- Please turn cell phones off or to vibrate



# ECONOMIC DEVELOPMENT STRATEGIES (TOOLKIT CH 1)



# Topics

- Benefits of an economic development strategy
- Steps in developing a strategy
- Integration with other plans



# Overview of Economic Development

- ED = process, policies, & activities by which a jurisdiction improves the long-term economic & social well-being of its people
- ED strategy = a framework for making programmatic & project choices to improve the local economy
  - Scale: neighborhood, municipal, regional, or statewide

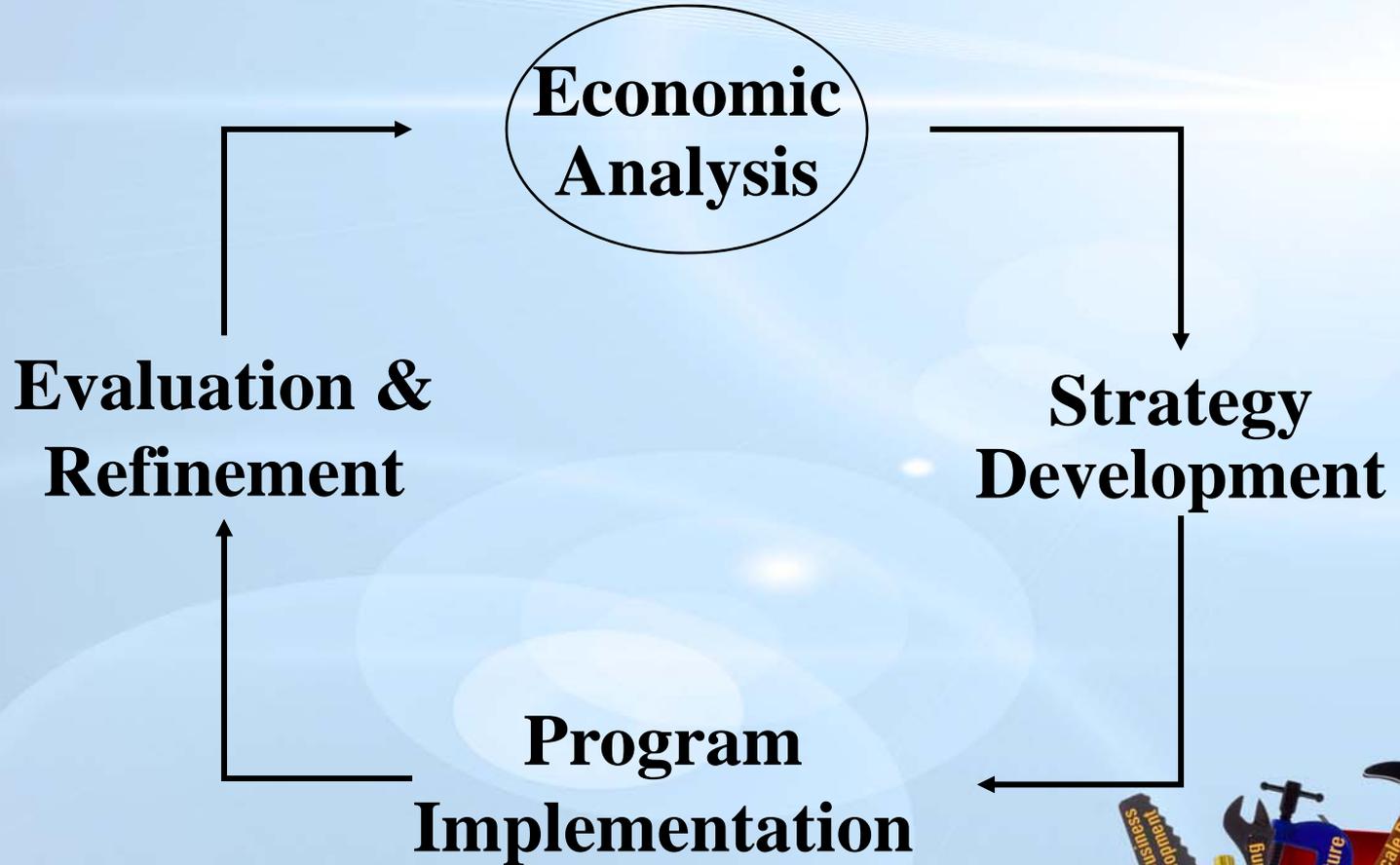


# Benefits

- Strategy is proactive & preventive: making good choices, avoiding bad investments
  - Poorly focused programs
    - ex. Loan program available to all; used by none
  - Program with no market
    - ex. High-tech incubator in low-tech area
  - Wasted resources
    - ex. Two microenterprise funds with same clients



# The Process



# Steps in the Process

1. Assess existing conditions
2. Assess local resources
3. Select desired outcome(s) or goal(s)
4. Select market sector to target
5. Select general approach
6. Identify appropriate techniques
7. Develop a mission statement
8. Prepare a written strategy
9. Develop an implementation action plan
10. Assess, evaluate, and modify



# Economic Analysis

- Assess qualitative and quantitative conditions
- Evaluate business and social environment
- Assess monetary, human, and physical resources & obstacles



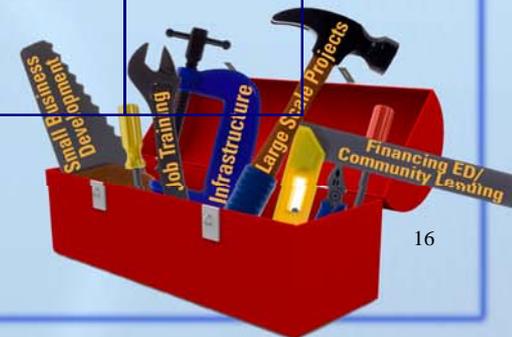
# Strategy Development

- Choose priority outcomes and market sectors
- Determine how to direct your assistance:
  - Locational approach
  - Minority/disadvantaged business
  - Sectoral approach
- Choose activities to match intended outcomes



# Strategy Options

	<b>CDBG</b>	<b>108</b>	<b>Other Fed – CDFI, SBA, Ag</b>	<b>State</b>	<b>Private lender</b>	<b>Other agency</b>
<b>TA</b>						
<b>Job training</b>						
<b>Micro Business</b>						
<b>Incubators</b>						
<b>Small Business</b>						
<b>Infrastructure</b>						
<b>Large scale (real estate, large businesses)</b>						



# Coordination w/ Other Plans

- Consolidated Plan
- Plans by other organizations & agencies
- Revitalization Strategy Areas (more on this later)



# Implementation

- Describe goals
- Written strategy summarizes plans & needs
- Action Plan implements the strategy
  - Tie to method of distribution & application process
- Plan is iterative and refined based on monitoring and evaluation



# Evaluation & Refinement

- Periodically review and assess progress toward strategy
- Establish measurable benchmarks to assess outcomes
- Update strategy based on assessment



# Summary: ED Strategies

- Economic development focuses on improving economic/social well-being
- Strategy is framework for making good investment decisions
- 10-step process for developing strategy
- Strategy evaluation/refinement is ongoing



# ED & CDBG FOUNDATION (TOOLKIT CH 2)



# Topics

- CDBG history background
- Eligible & ineligible CDBG ED activities
- National objectives
- Public benefits & program caps



# CDBG History

Authorized under Title I of the Housing and Community Development Act of 1974



# Primary Purpose

- Develop viable urban communities thru:
  - Provision of decent housing
  - Expanding economic opportunities
  - Principally for LMI persons
- National objectives and eligible activities: the two sides of the CDBG “coin”
- Consolidated Plan: the third side



# Administered at 2 Levels

- Federal level – HUD
- Local Level – one of 2 programs
  - CDBG Entitlement Program
    - Large cities & urban counties – City/County administrators
    - Automatic annual allocation based on demographics
  - CDBG Small Cities Program
    - Smaller communities – State administrators



# “Companion” Programs to CDBG

- Section 108 Loan Guarantee Program
  - Designed to provide financing for large economic development projects
- Economic Development Initiative (EDI) & Brownfield Economic Development Initiative (BEDI)



# CDBG Regulations

- 24 CFR 570
- Key changes related to ED
  - ED edits published 1/5/95
  - Consolidated Plan 11/9/95
  - Expenditure documentation 7/19/99
  - Job relocation limitation 12/23/05
  - Performance measurement 2/9/06
  - Brownfields 5/24/06

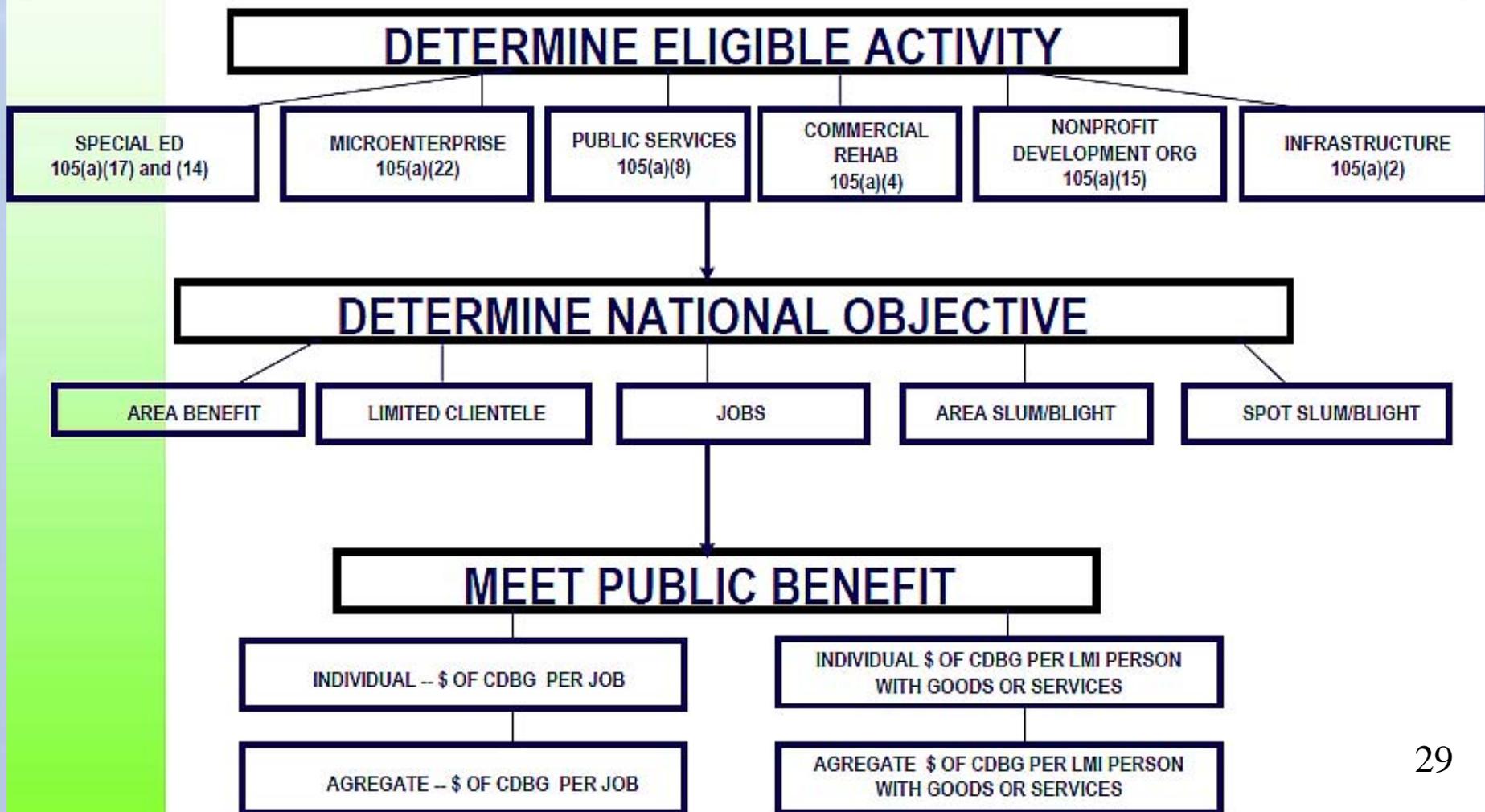


# CDBG ED Project Decision Process

1. Determine eligibility
  2. Check that it is not ineligible
  3. Make sure a national objective will be met
  4. Ensure compliance with other specific requirements
- Examples . . .
    - Public benefit test (Special ED & some infrastructure)
    - Project Underwriting (assistance to a for-profit)



# Qualifying ED Activities



# Typical CDBG-Funded ED Activities

- Loans for Businesses and Commercial Real Estate Development Project (Individual project loan or creation of loan program)
- Business Incubators
- Façade Improvement Programs
- Microenterprise Assistance Activities
- Economic Development Infrastructure Projects
- Job readiness, skills training, and job placement programs



# ELIGIBLE & INELIGIBLE CDBG ED ACTIVITIES



# Eligible Activities

- Wide variety possible
  - Housing & other real property activities
  - Public facilities
  - Public services
  - Nonprofit development organizations
  - Other activities
  - Planning and administration
- Statutory cites at Section 105



# Eligible Activity Categories

- CDBG Regulations 24 CFR Part 570, Subpart C
  - 570.201 Basic Eligible Activities
  - 570.202 Rehabilitation
  - 570.203 Special Economic Development
  - 570.204 Activities by CBDOs
  - 570.205 Planning
  - 570.206 Program Administration



# Eligible Activities – ED Projects Typically Qualify Under

- 201 Basic Eligible Activities
  - (c) public facilities and improvements
  - (e) public services
  - (o) microenterprise assistance
- 202 Rehabilitation
  - (a)(1) Privately owned residences that contain a business
  - (a)(3) Privately owned commercial buildings – exterior rehab and code correction only
  - (a)(4) Nonprofit-owned nonresidential buildings
- 203 Special Economic Development
- 204 Special Activities by CBDs
- 205 Planning



# Some Categories Trigger Other Requirements & Have Spending Caps

- Require Public Benefit Test and Underwriting
  - 570.203 Special Economic Development
  - 570.204 Activities by CBDOs (that would otherwise qualify under 203)
- Spending Caps
  - 570.205 Planning
  - 570.206 Program Administration
  - 570.201 (e) Public Services



# Special Econ. Development

- Commercial/industrial improvement (recipient/subrecipient)
- Assistance to for-profit business
- Economic development services in conjunction with above activities (including job training)



# Microenterprise Assistance

- Microenterprise
  - Commercial enterprise with  $\leq 5$  employees (one of whom is the owner)
  - Owners/persons developing a business
- Financial and/or Technical Assistance
  - Loans
  - Training
  - Business Plan Assistance
- General support (child care, transportation)



# Commercial Rehab

- Limited types of rehab on commercial structures
  - Privately owned residence with a business
  - If for-profit owned, only exterior improvements or correction of code violations
  - Nonprofit owned



# Public Facilities & Services

- Often done in support of other economic development efforts:
  - For example, infrastructure in support of business
  - For example, job training as a part of economic revitalization efforts



# Special Activities by CBDOs

- Types of Activities:
  - Neighborhood revitalization
  - Community economic development
  - Energy conservation
- Activities not subject to 15% public services cap
  - Services that increase economic opportunities thru job training, placement, and employment support
  - Any services carried out by a CBDO as part of NRSA



# What is a CBDO?

- Community-Based Development Organization
- CBDO major criteria:
  - Organized under State or local law to carry out CD
  - $\geq 51\%$  of Board is LMI residents, organizations serving the area, or reps of LMI neigh. organizations
  - Board nominated by general membership
  - Primary purpose community improvement, emphasis on LMI
  - Not an agency of the municipality, not more than 1/3 Board appointed by public officials



# Planning and Capacity Building

- Studies, analysis, data gathering, preparation of plans
- Together with program admin., costs cannot exceed 20% in a program year



# Ineligible Activities

- Buildings for conduct of government
- General government expenses
- Political or religious activities
- New housing construction
- Income payments
- Purchase of equipment
- Operations and maintenance
  - Except for public services & CDBG program staff office



# ACTIVITY: DETERMINING PROJECT ELIGIBILITY



# CDBG NATIONAL OBJECTIVES



# National Objectives 570.208

All CDBG activities must either:

(a) Benefit low- and moderate-income persons

(1) Area Benefit

(2) Limited Clientele

(3) Housing

(4) Job Creation and Retention

(b) Prevent slums or blight

(1) Area

(2) Spot

(c) Meeting urgent community need



# Remember: All National Objectives Are Not Equal

- LMI Priority
  - Grantees must spend  $\geq 70\%$  of CDBG funds to benefit LMI (primary CDBG objective – develop viable communities for benefit of LMI persons)
  - So, only 30% can be spent on (b) Preventing Slums and Blight and (c) Urgent Need
- Documentation
  - Different National Objectives Require Different Documentation



# LMI: Area Benefit

- Activity that benefits all residents of area
  - That is primarily residential
  - Where 51% of residents are LMI (or highest quartile of area in jurisdiction)
  - That meets the needs of the residents
    - Streetscape improvements
    - Water/sewer lines
    - Loan to a neighborhood-serving business
    - Commercial façade programs



# Job Creation/Retention can only qualify as Area Benefit, if:

- Carried out by CDFI, investment area 51% LMI and primarily residential
- Activities part of HUD–approved Neighborhood Revitalization Strategy



# Documenting Area Benefit

- Boundaries of the service area
- Income characteristics of service area and data used for determining % of LMI
- Proof area is primarily residential



# LMI: Limited Clientele

- Activity that benefits specific population
  - E.g., services for seniors, homeless shelters
- Options for meeting limited clientele
  - Presumed clientele
  - Eligibility requirements limit participation to LMI
  - Documentation that 51% participants are LMI
  - Nature and location indicate LMI
- Some activities are unique:
  - Removal of architectural barriers (some activities);
  - Microenterprise activities with LMI owners; or
  - Certain types of job training efforts.



# Job Training, Placement, or Support Services

- Can still be eligible for CDBG even if less than 51% beneficiaries are LMI if:
  - only CDBG assistance to a business
  - CDBG is proportionate to % LMI persons



# Documenting Limited Clientele

- Income limits and timeframe
- Documentation showing that facility is designed for exclusive use by eligible “special needs” group; OR
- Documentation showing nature and location is such that LMI can be presumed; OR
- Data showing size & annual income of family of all persons receiving benefit



# LMI: Housing Activities

- Permanent housing where 51% of occupants are LMI
  - Single-unit structure: LMI occupied
  - 2 units: at least 1 occupied by LMI
  - 3 + units: 51% or more LMI
  - New, MF, non-elderly: 20% or more
- Ownership or rental w/ affordable rents



# LMI: Housing (cont)

- Can treat units as single structure if:
  - Rentals are under common ownership; and on the same or contiguous parcels; OR
  - All units in an approved NRS area; OR
  - All units assisted by a CDFI in an investment area of 51% or more LMI
- Documented based on actual income of HHs



# LMI: Job Creation & Retention

- Activities related to economic development
  - Typical activities: business loans, commercial rehabilitation, infrastructure to a business
- To meet this:
  - Activities must create or retain jobs AND
  - 51% of jobs must be held by or available to LMI persons (FTE basis)



# Job Creation with LMI Benefit

- Job must be “available to” LMI person
  - No special skill/train or educ. beyond H.S.
  - Employer agrees to give first consideration LMI
  - Written agreement with employer
  - Reasonable application process, pool of applicants, no logistic barriers
- Jobs must be “held by” or “taken by” LMI
  - Documentation that employee was LMI at time of hiring
    - Self certification of income information from individuals
    - Qualification/referral through qualifying program/agency
    - Evidence can presume LMI
  - Must have a written agreement with business



# Job Retention with LMI Benefit

- Document that jobs would be lost without CDBG
- Job is currently held by LMI person; or job expected to turn over in 2 years and will be filled by or available to LMI person



# LMI Presumption

- Job can be presumed LMI if either:
  - Job holder resides in
    - Census tract with 20% poverty & general distress
    - Census tract with 30% poverty, CBD, & general distress
    - EZ/RC area OR
    - Census tract/block group with 70% LMI
  - Business and job located in
    - Census tract with 20% poverty and general distress
    - Census tract with 30% poverty, CBD, and general distress OR
    - EZ/EC area



# Counting Jobs

- Each business tracked individually; for each business: 51% of jobs must be held by or available to LMI persons
- Permanent FTE basis: convert part-time jobs, no temporary jobs
- Can aggregate jobs if:
  - Property development only (incubator)
  - CDBG paying RLF staff & overhead only
  - Activities carried out by a CDFI
  - Technical assistance
  - Other important national interests (activities exempt from aggregate public benefit standard)



# Special Requirement for Public Facilities and Improvements

- If  $>1$  job/\$10,000 CDBG – aggregate only the jobs of businesses principally being assisted
- If  $\leq 1$  job/\$10,000 will be created – all jobs created by all businesses in service area



# Counting Jobs

- Count all jobs created as direct result of CDBG \$\$\$
- Cannot stop counting at specified time or planned number of jobs
- Count first person to take position, not turn-over
- LMI based on current income not salary of created job



# Documenting Job Creation

- When “available to” LMI Individuals
  - Written agreement with business with listing of job titles, descriptions, FTE status and prerequisites/skills required
  - Description of actions taken, how first consideration given to LMI, hiring process, names of persons interviewed, income status of persons interviewed



# Documenting Job Creation

- When “taken by” LMI Individuals
  - Written agreement with business listing of job titles and FTE status
  - Listing of job titles filled
  - Name and Income status for each person hired



# Documenting Job Retention

- Evidence that jobs would be lost w/out CDBG
- For retained jobs held by LMI persons
  - Job title, FTE status, household size and income of each LMI person
- For retained jobs expected to turn over to LMI
  - Job titles expected to turn over and basis for turnover assumption,
  - Actual turn over date, income status of person taking job
  - If not taken by LMI, records that jobs were available to LMI interviewee name, date, income status, and income status of person hired



# Determining Income Status

- Written self-certification of income and household size prior to job application/hiring
- Referral from qualifying program/agency
- Evidence that person is homeless
- Address and qualifying demographic data for “presumption of LMI” status



# Documenting LMI Presumption

- Person's address, Census tract, % LMI, data source (must be  $\geq 70\%$  LMI or 20% poverty, 30% poverty if includes CBD or EZ/EC)

OR

- Business address, Census tract, % poverty (must be  $\geq 20\%$ , 30% if CBD) and data source, or other evidence of pervasive poverty and general distress



# Slum & Blight: Area Basis

- Activities to address dilapidated physical environment
  - Not based on income of residents
  - Typical activities: code enforcement, infrastructure, commercial rehabilitation
- Area must meet state/local definition of S&B, and:
  - 25%+ properties deteriorated/abandoned, declining values or know environmental contamination or
  - Public infrastructure in disrepair



# Documenting Area Slum & Blight

- Boundaries of area
- Description of conditions that demonstrate blight
- If residential rehabilitation:
  - Local definition of substandard
  - Pre-rehab inspection
  - Scope of CDBG rehab



# Slum & Blight: Spot Basis

- Activities that address specific condition
- Activities limited: acquisition, clearance, relocation, historic preservation, environmental remediation, building rehab (limited to public health and safety)
- May rarely use for ED given limited eligible activities



# Documenting Spot Slum & Blight

- Document activity was one of six possible
- Describe condition of blight or decay
- For rehab
  - Description of specific conditions detrimental to health and safety
  - Details of CDBG-funded rehab



# Urgent Need

- Activities that alleviate emergency conditions
  - Serious/immediate threat to health/welfare of the community
  - Recently became urgent (generally 18 months)
  - Inability of recipient to finance the activity on their own
  - No other means of funding
- Typical activities: infrastructure, interim assistance, rehab of community facilities



# Documenting Urgent Need

- Documentation on nature and degree of condition
- Evidence that CDBG addresses this condition
- Information on timing of problem
- Evidence that other financial resources not available



# ACTIVITY: MEETING NATIONAL OBJECTIVES



# PROGRAM LIMITATIONS, CAPS & PUBLIC BENEFIT STANDARDS



# Limitations on Job Relocation

- Job pirating is prohibited
  - If assist in relocation of plant, facility, or operation  
AND
  - Relocation will result in significant loss of jobs in another geographic area of U.S.
- Significant loss defined as:
  - Number of lost jobs is equal or greater than  $1/10^{\text{th}}$  of 1% of jobs in labor market area OR
  - Loss of 500 jobs



# Limitations on Eminent Domain

- FY2006 and subsequent appropriations
- CDBG not used for eminent domain except for public use
  - Public use does not include ED primarily benefiting private entities
  - Transit, utility, public facilities, & brownfields are public uses



# Faith-Based Organizations

- Final rule 10/30/03
- FBOs are eligible on equal footing
- May not support worship/religious instruction
- Must serve without regard to religion



# Program Caps

- 70% of \$ for LMI benefit over 1-3 years
- 20% cap on Planning & Administration
- 15% cap on Public Services



# 570.209 Public Benefit Standards

- Applies to:
  - Special Economic Development (570.203)
  - Activities by CBDOs (570.204), otherwise eligible under SED
  - Public improvements carried out for ED, creating  $<1$  job/\$10,000



# Examining Public Benefit

- Determine if proposed activity is subject to the Public Benefit Test?
- Calculate the minimum public benefit that must be achieved based on:
  - Number jobs that will be created/retained, or
  - Number of LMI persons that will be assisted (whichever is appropriate)
- Determine the number of jobs that will be created/retained or LMI persons assisted as a result of the proposed activity. Compare to minimum standards.



# Test at Two levels

- Individual Standard – every project
- Aggregate Standard – average of all projects grantee funds in a program year



# Individual Standards

- Create/retain 1 Job per \$50,000 CDBG funds

OR

- Goods and services to 1 LMI person per \$1,000 CDBG



# Aggregate Standards

- Create/retain 1 Job per \$35,000 CDBG funds

OR

- Goods and services to 1 LMI person per \$350 CDBG



# Applying Individual Standards

- If activity creates jobs and provides goods/services, qualifies as long as it passes at least one criterion
- Applied at time of obligation
- If limited to job training/placement or employment services, the jobs assisted are considered jobs created/retained for purposes of the public benefit standard



# Projects Automatically Fail Individual Public Benefit Test

- Community promotion
- Professional sports teams
- Recreation facilities for higher income
- Acquisition of land, no use specified
- Assist business w/ unresolved CDBG noncompliance findings



# Applying Aggregate Standards

- All activities obligated during program year
- Categorize each activity as either jobs or goods/services! But meet both criteria!
- Some job activities may be excluded 570.209 (b)(2)(v):
  - Unemployed
  - Homeless
  - Low-skill, LMI w/ clear advancement
  - Businesses in CT with  $\geq 20\%$  poverty
  - Neighborhood  $\geq 70\%$  LMI
  - CDFI serving predominantly LMI . . .



# Summary: CDBG Foundation

- Three foundational elements of CDBG:
  - Eligible & ineligible ED activities
  - National objectives relating to ED & the documentation required
  - Program limits, caps & the public benefit standards pertaining to ED



# ACTIVITY: APPLYING THE PUBLIC BENEFIT TEST



# REVITALIZATION STRATEGY AREAS (TOOLKIT CH 3)



# Topics

- Benefits
- Elements of strategy
- Review & approval



# Revitalization Strategies

- Written economic development plan
  - Entitlement: Neighborhood Revitalization Strategy (NRS)
  - State: Community Revitalization Strategy (CRS)
- Submitted with Consolidated Plan
- Addresses community/economic development approach in designated area



# Benefits of RS

- Job creation/retention activities meet LMI Area Benefit requirements
- Can track scattered site housing as single structure
- Economic development activities in area may be exempt from aggregate public benefit standards
- Any public service by CBDO is exempt from public services cap



# Strategy Area

- Area must be:
  - Contiguous
  - Primarily residential
  - High LMI %
    - 70% LMI if upper quartile  $> 70\%$  (use upper quartile % if quartile 51 – 70%; 51% LMI if upper quartile  $< 51\%$ )
    - EZ/RC; or
    - 20% poverty rate in Census tracts/block groups and 90% have 25% poverty



# Consultation

- Must be developed in consultation with community/stakeholders
- Describe community outreach efforts
- Coordinate revitalization efforts
- Describe how community needs and concerns are addressed



# Assessment

- Describe economic conditions
- Describe economic opportunities
- Highlight problems likely to encounter



# Economic Empowerment

- Activities that will be undertaken
- How will create jobs
- How will promote revitalization



# Benchmarks

- Must describe measurable goals and outcomes
- Examples:
  - Reduced unemployment
  - Lower crime rate
  - New businesses created
  - Public assistance roles smaller



# Funding

- Need not commit future funds BUT
- Must describe benchmarks & resources in each annual action plan



# Review & Approval

- Submitted with the Consolidated Plan
- Approved with the Consolidated Plan
  - Careful! Need specific approval for NRS
  - EZ/RC target area is automatic
- Amending the Strategy



# Summary: Revitalization Strategies

- NRSAs/CRSAs make strategic sense & offer some regulatory advantages
- Must meet area definition & consultation requirements
- Submit as part of Con Plan



# SMALL BUSINESS DEVELOPMENT (TOOLKIT CH 4)



# Topics

- Small business development
- Microenterprise assistance
- Business incubators



# SMALL BUSINESS DEVELOPMENT



# Benefits of Small Business Development

- New/improved job opportunities
- Increased income for residents
- Expanded goods & services
- Increased tax revenue



# What Is a Small Business?

- Not universal standard definition
- SBA defines thresholds for small businesses by NAICS code
  - Number of employees, or
  - Sales
- Most ED projects – businesses much smaller than SBA definition



# Typical Small Business Assistance

- Technical Assistance & Training
- Financing Assistance
- Business Incubators
- Infrastructure Development



# Technical Assistance

- Business consultation services
  - Often focused on business plan development, legal, and accounting issues
  - Often offered in conjunction with financial assistance
- Helps reduce risk
- Critical to programs directed to startups



# Training

- Single workshops on specific topics (e.g., social media marketing, e-commerce, “going green,” merchandising)
- Multi-week courses/more comprehensive (e.g., how to prepare a business plan)



# Typical Training & TA Providers

- Local nonprofit agencies and Community Development Corporations (CDCs)
- Small Business Development Centers (SBDCs)
- Service Corps of Retired Executives (SCORE)



# Providing TA & Training with CDBG

- 570.203 Special Economic Development
  - 51% jobs must be LMI (unless NRS or CDFI), can aggregate jobs created by all assisted businesses in a year
  - Must meet public benefit test
- 570.201 Public Service
  - 51% of trainees must be LMI
- 570.204 Activities by CBDOs
  - 51% jobs must be LMI (unless NRS or CDFI), can aggregate jobs created by all assisted businesses in a year
  - Must meet public benefit test
  - Won't count toward public service cap



# Financial Assistance

- Types of Assistance
  - Grants/Rebates
  - Loans
  - Loan Guarantees
- Grantees expected to establish policies compatible with CDBG regulations and address how applications will be reviewed, approved, & serviced



# Providing Business Financing with CDBG

- 570.203 Special Economic Development
- 570.202 (a)(3) Commercial rehab (exterior & code only)
- 570.204 (a)(2) Activities by CBDOs
- National Objectives
  - Area benefit if business serves all residents in LMI area or if NRSA or CDFI
  - LMI job creation/retention
- 203 & 204 trigger Public Benefit Test



# MICROENTERPRISE ASSISTANCE



# What is a Microenterprise?

- Commercial enterprise with  $\leq 5$  employees (one or more of whom is the owner)
- Owners or persons who are working toward developing a business



# Microenterprise Assistance

- Financial assistance
- Technical assistance
- Training
- General support (childcare, transportation)



# Using CDBG for Microenterprise

- Microenterprise assistance is eligible under 570.201(o)
- Can do TA and training to increase capacity of recipient/subrecipient to do microenterprise programs
- No limit on amount or type of CDBG loan/grant to microenterprise
- Not subject to public benefit test if separate program
- Some programs require microenterprises to receive TA and/or training before financial assistance



# National Objective

- Limited Clientele if the owner is LMI
  - Each client's income eligibility must be documented based on household size and income
  - Remains income-qualified for 3 yrs
- Job Creation/Retention
- Area Benefit if business serves LMI neighborhood



# Documenting Income

- CDBG eligible definitions
- Documentation of income typically done under two approaches:
  - Self certification
  - third-party verification



# Key Steps In Setting Up Program

- Define program objectives
  - What do you want to achieve?
- Know your target market
  - Geographic area
  - Characteristics of target businesses/entrepreneurs



# Key Steps (cont)

- Determine technical and credit needs
  - Other sources of financing
  - Types of credit needed
- Develop lending program
  - Underwriting criteria
  - Administrative procedures
  - Loan criteria and fees



# Key Steps

- Design TA and training
  - Offer in conjunction with financing
- Ensure program has funding and implement
- Monitor and evaluate progress



# Summary: Micro/Small Business

- TA is an important element
- Labor intensive & high transaction costs
- Micro Loan Program should be separate from other ED revolving loan funds
- Beware of closing costs
- Many prospects for one funded deal
- Ensure the venture has a reasonable chance of success



# BUSINESS INCUBATORS



# What Are Business Incubators?

- Reasonable rent, flexible space for businesses
- Access to shared services, equipment, & expertise
  - Services depend on types of businesses
- Networking, peer reinforcement
- Technical assistance
- Adaptation
  - Incubators without walls
- Info resource: [NBIA.org](http://NBIA.org)



# Benefits of Incubators

- Help reduce risk for businesses/increase chance of success
  - Lower costs, TA, peer support
- Supports business growth & job creation
- Can promote industry cluster growth



# Cluster Incubators

- Focus on a particular industry sector/cluster
- Fosters information sharing, alliances, promoting identity
- Examples: software, food, health care, advanced technology



# Financial Burden

- Incubator is a specialized real estate transaction
- Cash flow must fund operating expenses, capital expenditures and debt service
- Successful incubators balance real estate realities with enhancing survival of fledgling businesses
  - Important to keep capital costs low as possible



# Use of CDBG

- Fund construction/development
- Provide assistance to businesses locating within incubator



# Funding Incubator Construction

- Eligibility
  - 203 Special Economic Development, 204 CBDOs
    - Public benefit test applies
  - 201 (o) Microenterprise
    - If tenants are restricted to microenterprises
- National Objective
  - Job creation/retention - 51% LMI jobs
    - Can aggregate jobs
  - Area Benefit – If NRSA



# Funding Businesses in Incubators

- Eligibility
  - Microenterprise 570.201(o)
    - $\geq 5$  employees
  - Special ED (570.203)
- National Objective
  - Job creation/retention – 51% LMI jobs
  - Area Benefit – if NRSA



# Evaluating Incubator Applications

- Evidence of demand for incubator services
- Qualified management
- Ability to leverage resources
- Plan for self-sufficiency
- Financial feasibility – accurate projections for rents & expenses, ability to pay debt service



# Incubator Development

- Prepare a feasibility analysis
- Locate site
- Assemble development team
- Prepare financials and marketing plan
- Identify resources
- Finalize construction contract & develop
- Market & lease



# Summary: Incubators

- TA is important
- Businesses in incubator may need financing assistance
- Ultimately, an incubator is a real estate deal
  - Facility may need operating subsidies
  - Complete total analysis before funding acquisition



# ACTIVITY: DESIGNING SMALL BUSINESS DEVELOPMENT PROGRAMS



# **JOB TRAINING & OTHER PUBLIC SERVICES (TOOLKIT CH 5)**



# Topics

- Eligible activities
- National objectives
- Key steps



# What Is Job Training?

- Help unemployed or underemployed gain skills in demand in the labor market
- Frequently linked to job placement
- TA and entrepreneurial training to owner of microenterprise



# Eligibility Under CDBG

- Public service – 570.201(e)
- As part of special economic development project – 570.203 (c)
- By CBDO – 570.204
- As part of microenterprise efforts – 570.201(o)



# Other ED Public Services

- To support economic development, may wish to consider other services such as:
  - Child care
  - Transportation
  - Crime prevention



# Statutory Flexibility

- TA, training, support to microenterprises (570.201(o))
- Special economic development (570.203 (c)) – Services in connection with eligible special ED activities, including training for persons filling jobs
- CBDO *job training/placement/support activities* that increase economic opportunities (570.204(b))
- *Any* CBDO service under a Neighborhood Revitalization Strategy (570.204(b))



# Who Can Undertake Training?

- Grantee
- Other government agencies
- Subrecipients
- Businesses
- CBDOs



# Types of Training Programs

- Job search assistance
- Short-term classroom training
- Long-term classroom training
- Subsidized employment



# National Objective

- Training as a Public Service
- Qualify under LMI limited clientele:
  - Document household size and income & ensure that 51% are LMI persons;
  - Limit to only LMI persons;
  - Serve only a presumed group; or
  - Document based on location (very difficult)



# National Objective (cont)

- Training Under Special ED
- Qualify under EITHER:
  - LMI Jobs, if clear connection to jobs being created or retained; OR
  - LMI Limited Clientele, if CDBG is provided to business to pay only for training & the % of total project costs paid with CDBG is  $\leq$  % of LMI persons trained;



# Key Steps

- Conduct a needs assessment
- Identify employment opportunities
- Form partnerships
- Address barriers



# Key Steps (cont)

- Develop “soft skills” training
- Create a flexible program
- Define performance measures
- Consider other funding sources



# Summary: Job Training

- Job training is CDBG-eligible under several scenarios
  - Sometimes other public services that support employment
- Assess needs & opportunities & design a flexible program



# ACTIVITY: JOB TRAINING



# LARGE-SCALE COMMERCIAL DEVELOPMENTS (TOOLKIT CH 6)



# Topics

- Eligible activities
- National objectives
- Key steps



# What Are Large-Scale Commercial Developments?

- Activities such as:
  - Retail centers
  - Office buildings and other commercial manufacturing/industrial facilities
  - Public commercial development



# Typical Characteristics

- Large financial investment
- Large impact
- Real estate development
- Multiple financing sources
- Might be appropriate for Section 108 activity



# CDBG Roles

- Financing to business to build/expand facility
- Ground lease
- Ancillary facilities for public use
- Assist with equipment or working capital
- Services
- Development costs
- Infrastructure



# CDBG & Large Scale Projects

- Eligibility
  - Special Economic Development (570.203)
  - Community-Based Development Organizations (570.204)
  - Commercial Rehab (570.202)
  - Infrastructure (public facilities) 570.201(c)



# Special ED Activities

- Acquisition, construction, reconstruction, rehabilitation, or installation by recipient or subrecipient
- Assistance to for-profit
- Economic development services
- Remember the public benefit test!



# Other Eligible Activities

- CBDOs can undertake under certain circumstances
  - But capacity & financial limitations of nonprofits as developers of large-scale projects
- Commercial rehab may be possible under limited conditions



# National Objective

- Job creation/retention
- Area benefit
- Area slum blight
- Spot blight – rare



# Section 108 can be used for Large-Scale Activities

- Eligible activities
  - ED activities eligible under CDBG
  - Acquisition of real property
  - Public facilities
- Must meet national objective
- Sample projects
  - Neighborhood shopping center
  - Grocery store
  - Mixed-use retail and housing rehab
  - Industrial expansion



# Key Steps in Design

- Determine if want to target neighborhood for concentrated impact
- Ensure project meets HUD criteria
- Choose projects that are job generators
- Screen early
- Assess & control lending risks
- Make early decision about best way to conduct the project & develop a timeline



# Summary: Large-Scale Commercial Development

- Large investment & risk, but substantial economic impact
- Usually real estate based; careful underwriting required
- Often tied to 108
- Need to monitor carefully



# INFRASTRUCTURE (TOOLKIT CH 7)



# Topics

- Eligible & ineligible activities
- National objectives
- Key steps



# What Is Infrastructure?

- Non-housing activities
- Public works
  - Transportation facilities
  - Water, sewer, drainage
- Community facilities
  - Parks, recreational facilities, senior centers
  - Neighborhood service centers
  - Social services buildings



# Typical Infrastructure Activities

- Roads, streets, sewers that are:
  - Leading to business location
  - Within an industrial park
  - On a business site



# Privately Owned Utilities

- Covers utilities owned by private company not public agency
  - Utilities includes: electricity, telephone, water, sewer, natural gas, television cable
- Must meet a national objective:
  - Area LMI
  - Possibly LMI job creation
  - Slum/blight area
  - Possibly urgent need



# Privately Owned Utilities (cont)

- Must be publicly regulated and provided through distribution lines to private property
- Activities include:
  - Acquisition
  - Construction
  - Reconstruction
  - Rehabilitation
  - Installation



# Ineligible Infrastructure Activities

- Maintenance and repair of public facilities
  - Exception for handicapped accessibility
- Operating costs
  - Exception for costs related to operating a CDBG public service activity
- Buildings for general conduct of government (e.g., city hall)
  - Some exceptions



# Special Assessments

- Special assessments are used to recover capital costs through a fee or charge
- Under CDBG, two ways think about special assessments:
  - To recover costs of CDBG-assisted public improvements
  - To pay private assessments for low/mod owner occupants



# Special Assessments (cont)

- If all costs of public improvement paid w/ CDBG, special assessment may recover CDBG funds
  - Only made against properties owned & occupied by non-LMI persons
  - Special assessment payments considered program income



# Special Assessments

- If CDBG used to pay part of public improvement, assessments may recover non-CDBG-assisted portion
  - CDBG must be used to pay assessment on behalf of properties owned & occupied by LMI persons
- If not initially funded with CDBG, use CDBG to pay assessments to recover the cost makes improvement CDBG assisted



# Special Assessments Are Not

- Not taxes
- Not periodic charges based on use (e.g., water or sewer)



# National Objective

- Typically, Low/Mod Job Creation/Retention:
  - Must aggregate all FTE jobs created by affected businesses if cost/job less than \$10,000
  - If \$10,000+ must aggregate all FTE jobs created in service area within 1 year after construction completed



# National Objective (cont)

- Low/Mod Area Benefit
  - Surveys common for small service areas within Census Tracts (must have approved survey methodology)
- Some improvements may fit Slum/Blight Area Basis national objective



# Public Benefit

- Public improvements carried out for ED that create  $<1$  job/\$10,000 are subject to public benefit test



# Key Steps

- Decide if want to target neighborhoods
- Ensure potential projects meet HUD criteria
- Choose projects that are generators
- Assess and control lending risks
  - Screen early



# Cost Benefit Analysis

- Assess risk
- Determine amount of public participation – all costs
- Calculate benefit stream
  - Jobs
  - Tax increments
  - Payments
- Relate risk and cost to benefits over time



# Summary: Infrastructure

- Public & private (with limitations) infrastructure is CDBG eligible
  - Capital cost, but not maintenance and operation
  - Special assessments if not infrastructure is CDBG funded (assessments may also be used to recover CDBG capital investment)



# FINANCING ECONOMIC DEVELOPMENT (TOOLKIT CH 8)



# Topics

- Financing options
- Revolving loan funds
- CDFIs



# FINANCING OPTIONS



# Methods of Financing

- Grants
- Equity investment
- Sale/lease of assets
- Debt financing
- Loan guarantees



# Grants

- Cash contribution or principal reduction
- Plusses
  - Easy to administer
  - May be only available \$\$ source
- Minuses
  - Resources not replenished
  - Business commitment?
- Examples:
  - Interest subsidy, Principal reduction, Rehabilitation rebate



# Equity

- Contribution of cash or property in exchange for share of ownership
- Plus
  - Share in success
- Minuses
  - Exit strategy
  - Risk, lack of recourse



# Purchase & Sale or Lease

- Entity purchases asset and sells or leases asset to borrower at a negotiated price
- Plusses
  - Can target economic development
  - Increase feasibility of projects
- Minuses
  - Requires specific skills in acquisition & leasing



# Debt Options

- Direct loans
  - Subordinated loans
  - Tandem loans
- Repayment structure
  - Self amortizing
  - Contingent payment
  - Partial or full forgiveness



# Amortizing Direct Loans

- Loans that are paid back over time
- Pluses:
  - Ensures business commitment
  - Extends resource
  - Interest can multiply impact
- Minuses:
  - Need loan processing/servicing skills
  - Must have default procedures
  - May not be financially feasible



# Contingent Payment Loans

- “Deferred Payment” – part or all depends on future events
  - (e.g., sale of property, profit level, # of years)
  - Tip: Use simple, quantifiable measures
- Plus – permits loan to function as grant in short term, with option of eventual payment
- Minus – repayment might not happen
- Can mix contingent payment & amortizing loan
  - e.g. Forgivable deferred payment loan – facade improvement program



# Loan Guarantee

- Make it easier for business to borrow from private lender
- Pledge loan repayment in event of default (100% or portion)
- Plus – leverage, lower CDBG investment
- Minus – Can be difficult to structure, must have very clear agreement on what guarantee covers and when will be paid



# REVOLVING LOAN FUNDS



# What is a RLF?

- Fund: Source of money
- Loan: Used to make loans usually to small and medium size businesses
- Revolving: Loans are repaid and reloaned. With interest, the fund can increase and become an endowment.



# Typical Borrowers

- Existing businesses
- Startup ventures
- Developers
- Nonprofits
- Microenterprises



# CDBG Rules for RLF

- Projects must comply with CDBG requirements
- Must be separate, interest-bearing fund
- Interest earned by RLF loans is program income



# Steps: Market & Client Scan

- Confer with professionals & borrowers to identify market
  - Bankers
  - Realtors
  - Economic development personnel
  - Trade associations
  - Local officials
  - Small business groups or associations
- What gap in funding exists?
  - Understand existing efforts
  - Who will the effort serve?



# Step: Program Design Focus

- Requirements/eligibility
  - Borrowers
  - Minimum/maximum loan amounts
  - Minimum leverage
  - Cost per job
  - Minimum equity requirements
- Establish loan rates & terms
- Seek funds to capitalize RLF



# Step: Select Administrative Entity

- Who will administer the program?
  - City
  - Existing nonprofit
  - New organization
- Does staff have the necessary skills to implement?
- Develop organizational structure
  - Loan committee, staffing, budget



# Step: Design Operational Procedures

- Establish systems for delivery
  - Marketing
  - Screening
  - Application
  - Approval
  - Closing
  - Disbursement
  - Portfolio Management



# CDFIs



# Community Development Finance Institution Fund

- Subsidiary of Department of Treasury
- Expands availability of credit, investment capital, & financial services in distressed and underserved communities
- Does not lend or grant money to individuals
- Provides capital to local intermediaries that, in turn, lend and invest the funds – CDFIs



# Definition of a CDFI

- Specialized financial institutions that work in distressed communities underserved by traditional financial institutions.
- May provide a wide array of financial products and services (e.g., first-time homebuyers, community facilities, start or expand small businesses)
- Might also offer technical assistance to small businesses or credit counseling



# Certification Criteria for CDFIs

- Primary mission = econ & com dev in distressed communities
- Must be a financing entity
- Serve a specific target market or area where  $\geq 60\%$  of total activities are directed
- Development services offered in conjunction with financial services
- Accountability thru Board members or staff from organizations that serve target market
- Not government entity or controlled by gov



# CDFIs & CDBG

- Job creation/retention activities meet Area Benefit
- Housing units treated as a single structure
- ED activities exempt from aggregate public services test
- May aggregate jobs



# Summary: Financing

- CDBG permits full range of financing options: grants, loans of various types, loan guarantees, equity, etc.
  - Each option has pluses and minuses
  - Appropriate under different circumstances
- Revolving loan funds permitted, but require structure/administration
- CDFIs can support ED and are compatible with CDBG



# UNDERWRITING (TOOLKIT CH 9)



# Topics

- CDBG underwriting guidelines & public benefit test
- Underwriting business loans
- Underwriting real estate loans



# Underwriting Defined

- Underwriting is the process for determining project risk and evaluating rewards
- Public underwriting differs from private
- Within CDBG, portions of this analysis are known as “appropriateness evaluation”



# Purposes of Underwriting

- Ensure project meets public benefit
- Ensure project has reasonable chance of success
- Ensure that public subsidy is needed



# HUD Appropriateness Criteria

- Two types:
  - Voluntary underwriting criteria
  - Mandatory public benefit test (for certain types of ED projects)



# CDBG ED Underwriting Criteria

- Recommended, not mandatory
- Criteria
  - Reasonable costs
  - Commitment of other financing sources
  - Necessity of assistance (non-substitution)
  - Feasibility of project
  - Reasonable financial terms/return
  - CDBG funds disbursed pro rata



# Reasonable Costs

## Risks:

Inflated costs

Understated costs

Excessive fees



## Contribution:

Independent quotes

Scrutiny of budget

Cost certification

Retainage



# Commitment of Other Sources

- Before CDBG disbursed, all debt and equity committed to project
  - Letter from source/copy of agreements
- Issue is whether have sufficient funds to complete project
- CDBG funds at application may be contingent upon other financing



# Necessity of Public Funding

- Should not substitute CDBG for other available funds
- Look at “gaps”
  - Financing gap: uses exceed sources
  - Rate of return gap: reasonable return
  - Locational gap: higher costs associated with specific site/project



# Project Feasibility

- Project is financially feasible with assistance
- Project is viable for the term of assistance or regulatory restrictions
- Terms of CDBG loan:
  - Reflect the ability to repay without threatening the success of project



# Reasonable Return & Terms

- Loan terms can be subsidized so long as not result in excess return to borrower
  - Don't over-subsidize private participation (undue enrichment)
- Compare to market: Is developer/owner making more/less than conventional?
  - Take risk & incentives into account



# Pro Rata Disbursement of CDBG

- Borrowers often want CDBG money spent first
  - CDBG usually costs less than other funds
- May result in CDBG investment in uncompleted projects = ineligible costs
- CDBG should be drawn in same proportion to other funds
  - Exception if CDBG for acquisition but need other safeguards



# Public Benefit Test

- Applies to special ED activities, some 105(a)(15) activities, and some infrastructure undertaken as jobs activity
  - Grant or loan, does not matter
- Measures \$ cost in CDBG funds against benefits derived
- # Jobs or LMI persons served used as “benefit” criteria



# Public Benefits: Individual Transactions

- Individual transactions:
  - 1 job per \$50,000 CDBG, OR
  - 1 LMI person per \$1,000 CDBG (goods & services)
- If activity creates jobs and provides goods/services, qualifies as long as it passes at least one criteria
  - Activities with insufficient benefit (e.g., general promotion, professional sports teams, privately owned recreational facilities in high income areas, land without purpose (land banking), owner with unresolved findings)



# Public Benefits: Aggregate Portfolio

- All activities obligated during program year:
  - 1 job per \$35,000 CDBG, OR
  - 1 LMI person per \$350 CDBG (goods and services)
- Categorize each activity as either jobs or goods/services
  - But meet both criteria!
- Some job activities may be excluded (e.g., unemployed, homeless, low-skill, LMI w/ clear advancement, public housing residents)



# Documenting Appropriateness

- Maintain files of analysis
- Show research and copies of financial statements
- Explain calculation of gaps or returns
- Justify infusion of public funds
- Respond to each of the appropriateness criteria
- Use a checklist



# Two Primary Types of ED Lending

- Business loans
- Real estate loans



# UNDERWRITING BUSINESS LOANS



# Underwriting Business Loans

- Ability to repay
- Collateral
- Commitment to project
- Balance sheet analysis
- Management experience
- Credit history



# Ability to Repay

$$\text{DCR} = \frac{\text{CASH FLOW}}{\text{DEBT SERVICE}}$$

$$1.25 = \frac{\$100,000}{\$80,000}$$



# Debt Coverage Ratio Guidelines

- The higher the better
- Use known cash flow or a conservative estimate
- Generally private lenders want a DCR between 1.2 and 1.3
- Limit the number of deals with DCR  $< 1.1$
- Avoid deals with DCR  $< 1$



# Collateral

$$\text{Loan to value} = \frac{\text{Loan amount}}{\text{Value/Cost of assets securing the loan}}$$

$$.80 = \frac{\$1,000,000}{\$1,250,000}$$



# What Is Value?

Fair market value

Liquidation value

Value in use

Replacement value

Investment cost

Cost

Salvage value



# Loan-to-Value Ratio Guidelines

- HUD has no requirement but generally 80%
- Loan-to-value is matter of judgment
- No definite standards
- Do not exceed 100% loan-to-value



# General Guidelines: LTV

- Commercial buildings (80%)
- Home mortgage (80%)
- Machinery and equipment (50-70%)
- SBA 504 (90%)
- Inventory (50-80%)
- Receivables (80%)



# LTV Guidelines

- The lower the better
- Loan portfolios should have only a few loans with a loan-to-value more than 90%
- Cash flow is more important than collateral
- Lenders avoid projects with a loan-to-value over 100%



# Commitment

- Commitment by owners is critical!
- Owner guarantee may be proportional to interest



# Balance Sheet

- Look at soundness:
  - Collection of receivables?
  - Payment of bills?
  - Management of inventory?
  - Owner bleeding the company?
  - Cash relative to needs?



# Management

- Must be experienced in all areas of business
- Should have direct or transferable skills



# Credit History

- Favorable credit history
- Good & fair reputation
- No recent bankruptcy
- Clean criminal report



# Small Startups

- Likely to have a higher default rate
- Look for:
  - Business plan
  - Borrower commitment
  - Personality
  - Niche



# UNDERWRITING REAL ESTATE LOANS



# Underwriting Real Estate Loans

- Real Estate
  - Ability to repay
  - Collateral
  - Commitment to project
  - Experience of development team
  - Credit history



# Ability to Repay

$$\text{DCR} = \frac{\text{NOI}}{\text{Debt Service}}$$

- Usually conventional lenders look at 1.25 - 1.3
- Usually public lenders look at 1.1 - 1.15



# Collateral

- Use Loan-to-Value Ratio
- Appraiser normally determines value
- Be certain to carefully review appraisal
- Generally LTV ranges from 75% to 90%



# Commitment to Project

- Ways to show commitment
  - Completion guarantee
  - Recourse
  - Deferral of development fee
  - Guarantee cash flow shortfalls
  - Equity



# Experience

- Be certain development team has significant similar experience
- Developer should have good credit and be reputable



# HUD Appropriateness Criteria

- Two types:
  - Voluntary underwriting criteria
  - Mandatory public benefit test (for certain types of projects)



# Summary of Appropriateness

- Good approach to projects that need public assistance
- Local flexibility in analysis
- Provides a checklist for analysis



# Purpose of Appropriateness

- Ensure project meets public benefit
- Ensure project has reasonable chance of success
- Ensure that subsidy is needed



# History of Appropriateness Criteria

- Amendment allowing assistance to for-profit businesses (1981)
- Stokvis Memorandum (1987)
- National Affordable Housing Act (1990)
- Kondratas memorandum (1992)
- Housing and Community Development Act (1992)
- Publishing of new regulations (1995)



# Financial Analysis (Underwriting)

- Recommended, not mandatory
- Reasonable costs
- Commitment of other financing sources
- Necessity of assistance (non-substitution)
- Feasibility of project
- Reasonable financial terms/return
- CDBG funds disbursed pro rata



# Cost Reasonableness

## Risks:

Inflated costs

Understated costs

Excessive fees



## Contribution:

Independent quotes

Scrutiny of budget

Cost certification

Retainage



# CDBG Commitment Terms

- CDBG funds may be contingent upon other financing
- No substitution of private funds with CDBG
- CDBG funds should be disbursed at a rate no greater than other sources of funds



# Gap Analysis

- Financing gap
- Rate of return gap
- Locational gap



# Financing Gap

- + Reasonable cost
- Conventional debt
- Other debt
- Conventional equity

---

= Financing gap



# Rate of Return

$$\begin{array}{r} + \text{ Reasonable cost} \\ - \text{ Conventional debt} \\ \hline \text{Equity needed} \end{array}$$

Market rate  
of return

gap? →

$$\begin{array}{r} + \text{ Benefits to investors} \\ + \text{ Equity Invested} \\ \hline = \text{ Project rate} \\ \text{of return} \end{array}$$



# Locational Gap

$$\begin{array}{r} + \quad \text{Cost of project in location X} \\ - \quad \text{Cost of project in location Y} \\ \hline = \quad \text{“Locational” gap} \end{array}$$



# Project Feasibility & Return

- Terms of CDBG loan reflect the ability to repay without threatening the success of project
- Project is financially feasible with assistance
- Terms don't over-subsidize private participation (undue enrichment)
- Terms of CDBG loan affect conventional debt & equity



# Subsidizing Participation

- Use public funds to balance interest of those participating
- Example of participants in investor deals:
  - developer
  - lender
  - investors
- Repayment terms of public funds are structured such that each receives a market (but not above) yield/fee



# Summary: Underwriting

- CDBG has:
  - Voluntary underwriting guidelines
  - Required public benefit standards
- Two types of ED underwriting: business loans and real estate loans
  - Each requires a different underwriting approach
  - But both focus on reasonable and necessary public investment in the venture



# ACTIVITY: UNDERWRITING



# SECTION 108 (TOOLKIT CH 10)



# Topics

- Section 108 Overview
- Implementation
- Other Initiatives Tied to Section 108



# SECTION 108 OVERVIEW



# What is Section 108?

- Loan not a grant
- Community borrows money from private investors
- Communities either use the loan to carryout activities or re-loans the funds to a third party
- HUD provides a 100% guarantee to the investors who purchase the notes at public offering



# How much can communities borrow?

- Communities or States (small cities program) can receive authority to borrow up to 5 times annual CDBG allocation
- Maximum loan term is 20 years



# How is the loan secured?

- Communities or States must pledge their future CDBG funds to HUD
- HUD cannot rely only on the CDBG pledge
- Project must meet prudent underwriting standards or
- Community must pledge other assets/additional security (e.g., parking revenue, land)



# Advantages of 108

- Leverage
  - Access funds = 5 X CDBG while retaining use of CDBG \$
- Avoid referendum
  - Not a general obligation
- Accelerate CDBG activities
- Avoid private benefit restrictions
- Access to funds at AAA rate



# Potential Obstacles

- No administration \$
- Commercial grade lending not like CDBG
- Timing to get cash
- Fees (paid by borrower)
- Expertise needed to package 108 application
- CDBG regulations apply to 108



# Eligible Activities

- Acquisition, clearance, demolition, site prep
- Rehabilitation of publicly-owned property
- Economic development activities
- Housing rehabilitation and preservation
- Issuance and finance costs – 108 loans
- Infrastructure



# Ineligible Activities

- Operation of community centers, recreation facilities, parks (construction/rehab is okay)
- Nonfederal share of other Federal grant programs
- Long-term planning



# Program Requirements

- National objectives
- Other Federal requirements (relocation, Davis Bacon, environmental, etc.)
- Public benefit test for economic development
- 70% rule
- Certifications

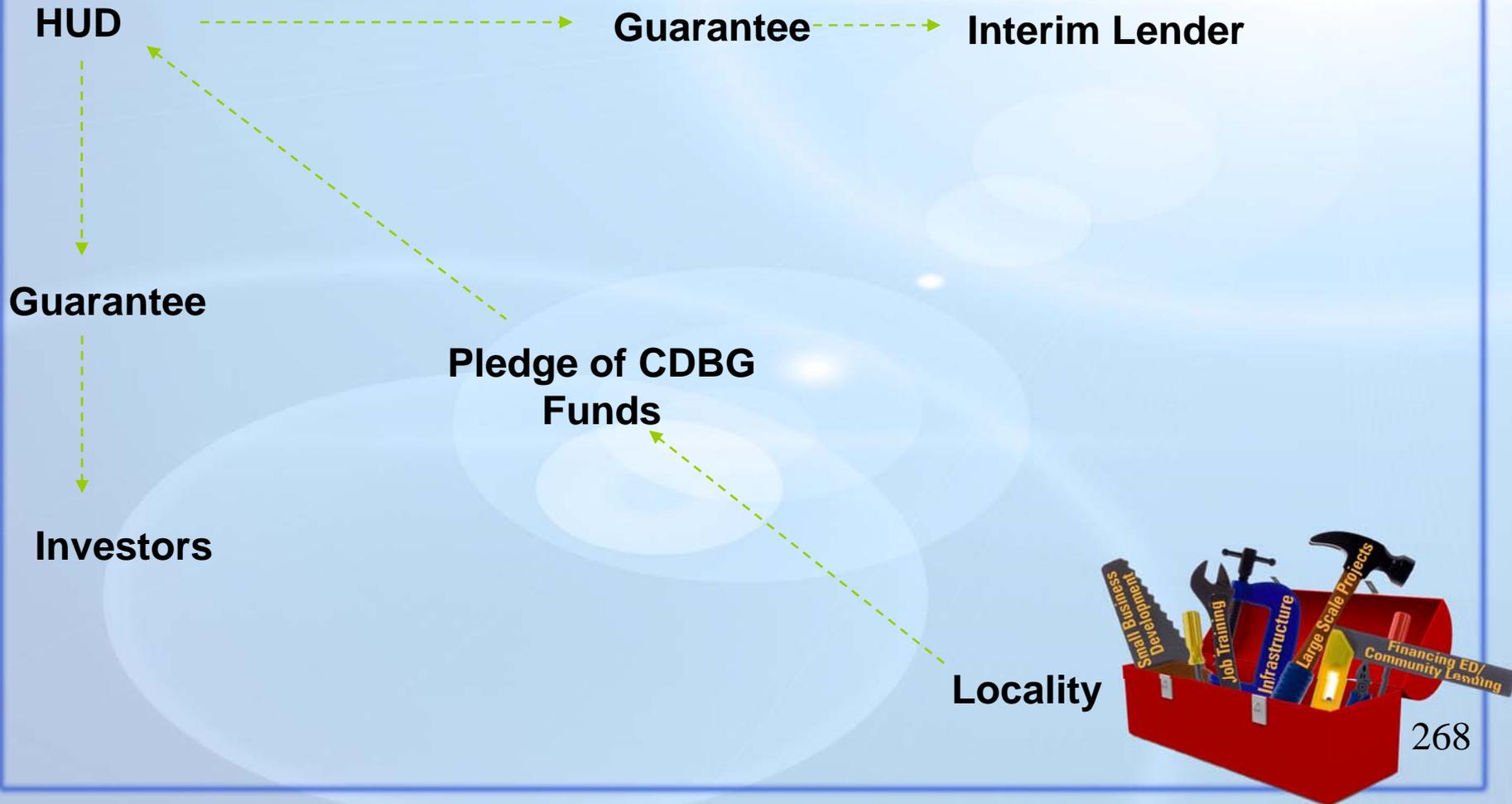


# Typical Projects

- Loans
  - Industrial expansion
  - Hotels
  - Shopping centers
  - Business incubators
- RLFs
- Public facilities
  - With alternative collateral and income streams



# Section 108 Guarantee



# Levels of Transactions

- Level # 1:  
Communities borrow from investors
- Level #2:  
Communities undertake activities or re-lend



# Players & Roles

- Community
- HUD
- Underwriter
- Fiscal Agent
- Private Investors
- Third-Party Borrowers



# Interim Loans

- Public offering usually once a year
- Interim loan available until public offering
- Must close Level # 1 transaction
- Fiscal Agent makes interim loan
- Interest rate: 90 day LIBOR + 20 basis points
- Interim loan is taken out by permanent financing at next public offering



# Risks of Using Section 108

- Loan v. grant
- City must pay back 108 even if third-party borrower defaults
- Contingent use of future CDBG
- Political resistance to borrowing
- Interest rate changes



# Risk Management

- Institute prudent underwriting
- Diversify portfolio (if revolving fund)
- Establish loss reserves
- Maintain minimum leverage requirements
- Limit balloon payments
- Certify costs



# Risk Management

- Avoid construction financing
- Conduct cost benefit analysis
- Require letters of credit
- Limit high-risk loan categories
- Allow for rate changes
- Systematic credit review early



# Repayment of 108 Loan

- Community assumes ultimate risk
- May transfer risk but obligation is recourse
- HUD provides guarantee
- Grantee provides security
  - Future CDBG
  - Program income
  - Additional security



# Defeasance

- Covers early payment
- Technically cannot prepay but by guaranteeing the income stream, borrower is defeasing (voiding) the obligation
- Community places deposit (usually in form of Treasury bills) with Fiscal agent which will provide promised income stream to investor
- Penalty is possible



# APPLICATION & IMPLEMENTATION



# Overview of Process

- Screen project
- Submit application
- Approval
- Close
- Disburse
- Service



# Project Screening

- Screen projects prior to HUD application
- Look at:
  - Credit
  - Eligibility



# Application Types

- Generic Applications
  - No transaction identified
  - HUD approves underwriting criteria
  - Capitalizes a revolving loan fund
  - Apply for eligibility determination as projects materialize
- Detailed Application
  - Funds earmarked for specific project



# Presubmission Requirements

- Amend CD plan or incorporate Section 108 in final plan
- Citizen participation
- Advertise needs hearing
- Conduct needs hearing
- Publish proposed statement and projected uses
- Advertise second public hearing
- Conduct second public hearing



# Citizen Participation

- Provide adequate notice of hearings
- Provide technical assistance to low/mod persons
- Provide access to records
- Address needs of non-English-speaking persons
- Respond to comments, grievances, and/or complaints



# Submission

- Application to HUD should include:
  - Project description
  - National objective
  - Repayment schedule
  - Certifications



# HUD Review

- Review by area office
- Review by central office



# Approving & Closing

- HUD approves & notifies
- Then can close 108 loan
- Level #1 and level #2 transactions separate closings



# Disbursing & Servicing

- Custodial lender holds funds until used by community
- Fiscal agent services level #1
- Community must establish system for level #2
- Custodial Accounts
  - Loan Guarantee Account
  - Loan Repayment Account



# Loan Portfolio Management

- Collections
- Monitoring & accounting
- Collateral preservation
- Anticipate & deal with problems
- Foreclosure



# RELATED INITIATIVES



# Economic Development Initiative

- EDI funds help reduce Section 108 risk
  - Funding reserves
  - Over collateralize
  - Credit enhancement
  - Below-market financing
- In years when funds available, EDI and BEDI are competitive



# Brownfields & BEDI

- Brownfields: abandoned, idled, or under-used real property w/ environmental contamination
  - Eligible as a “public use” for eminent domain
- BEDI – assistance linked to Section 108 for brownfields
  - Not currently funded



# Summary: Section 108

- Section 108 provides ability to leverage CDBG allocations, but carries risk
  - Jurisdiction has to repay loan
- Two levels of lending
- Jurisdiction must apply to HUD
- Underwriting & loan servicing necessary
- EDI & BEDI can tied to 108 lending, when funds are available



# PROGRAM ADMINISTRATION (TOOLKIT CH 11)



# Topics

- Program design & administration
- HUD reporting
- Measuring success



# PROGRAM DESIGN & ADMINISTRATION



# Key Questions

- Who should undertake the program?
- How much will it cost?
- Where and how will the program occur?
- How will it be “sold”?
- What records must be kept?
- How well are objectives met?



# Typical Roles in ED Programs

- Intake
- Underwriting
- Loan closing
- Disbursement
- Business counseling
- Loan servicing



# Who Will Manage & Implement?

- Grantees have options:
  - Staff
  - Subrecipients
  - CBDOs
  - CDFIs
  - Contractors



# Policies & Procedures

- Recommend administrative policies & procedures:
  - Program goals
  - Eligible/priority participants & projects
  - Funding or services
  - Underwriting & selection criteria
  - Selection process



# Budget

- Estimate administrative costs carefully
- Estimate loan/assistance volume
- Estimate likely revenues from service delivery and miscellaneous sources
- If new to economic development, consider a startup budget



# Marketing

- Develop a rollout strategy (marketing plan) & schedule:
  - Step-by-step timetables
  - Technical assistance hurdle
  - Milestones
  - Assignment of marketing responsibility



# Recordkeeping

- Important element!
- Must be well thought out and efficient
  - How?
  - Who?
  - What?



# Program-Wide Records

- Consolidated Plan
- Executed grant agreements
- Personnel files
- Citizen participation plan & compliance
- Other Federal: fair housing, relocation, etc.
- HUD monitoring correspondence



# Financial Records

- Chart of accounts
- Manual on accounting procedures
- Journals and ledgers
- Source documentation
- Procurement files
- Real property inventory



# Financial Records

- Bank records, including revolving loan
- Draw down requests
- Payroll records
- Financial reports
- Audit files
- Relevant financial correspondence



# Project Records

- Eligibility
- National Objective
- Location and characteristics of beneficiaries
- Subrecipient agreement, bids, & contracts
- Compliance with special program requirements:  
*environmental review, other Federal compliance*
- Budgets and expenditures
- Status



# Subrecipient

- Subrecipient application
- Written agreement
- Financial records
- Audits
- Progress reports
- Draw down requests
- Monitoring reports
- Correspondence



# Recordkeeping

- Record retention
  - Four years following program year
  - Consistent with Consolidated Plan
  - Consistent with HOME
- Access
  - Citizens must have reasonable access
  - Citizens must be provided timely information



# HUD REPORTING



# HUD Requirements

- GPRA & PART: HUD outcome framework
  - New data collection
  - Reporting (in IDIS)
  - Changes in Con Plan
  - Changes in timing of information collection
  - Requires outcome, objective, indicators



# Objectives

- Suitable living environment
  - Possible for ED that improves living environment (e.g., commercial revitalization in blighted business district)
- Decent affordable housing
  - Unlikely for ED activities
- Creating economic opportunities
  - Most likely ED objective (job creation/retention, increased economic activity/opportunities)



# Outcomes

- Availability/accessibility
  - ED activities that improve availability/accessibility of goods/services or jobs
- Affordability
  - May be possible for activities that make capital affordable to businesses
- Sustainability
  - ED that increases sustainability of neighborhood or community



# Indicators & Reporting

- Grantees must report certain data on ED activities
- Reporting not necessarily tied to objective & outcome chosen
- Instead, based on:
  - Use of Job Creation/Retention National Objective AND
  - Whether businesses assisted under certain IDIS Matrix Codes



# Jobs Reporting

- For job creation:
  - Total number of jobs created in program year
  - Number of jobs with employer-sponsored health care
  - Number of persons who were unemployed prior to taking job created
  - Number of jobs by EDA job classifications



# Job Reporting (cont)

- For job retention:
  - Total number of jobs retained in program year
  - Number of jobs with employer-sponsored health care
  - Number of jobs by EDA job classifications



# Businesses Assisted Reporting

- Applies to the following ED activities:
  - Commercial or industrial improvements by a grantee or nonprofit (IDIS Matrix Codes 17A-D)
  - Rehab of a publicly or privately owned commercial or industrial buildings (IDIS Matrix Code 14E)
  - Direct ED assistance to private, for-profit companies including micros (IDIS Matrix Codes 18A-C)



# Businesses Assisted Reporting (cont)

- Report:
  - Total number of businesses assisted
  - Number of new businesses assisted
  - Number of existing businesses assisted
    - Number of businesses expanding
    - Number of business relocations



# Businesses Assisted Reporting

- Number of businesses with commercial façade or business building rehab
- Number of businesses that provide goods/services to meet needs of a service area/neighborhood/ community
- DUNS number for each business assisted



# MEASURING ED PROGRAM SUCCESS



# Measuring Success

- Measures of success:
  - Flow of capital into the community
  - Economy diversified; tax base enhanced
  - Jobs created & skills increased
  - Assets expanded
  - Self sufficiency & access for LMI persons
  - Barriers to employment reduced



# Monitoring

- Grantees are responsible for:
  - Following program requirements
  - Ensuring that subrecipients and beneficiaries comply with rules & achieve their performance objectives
- Grantee should have a formal monitoring plan



# Monitoring Plans

- Define monitoring objectives
- Standardize monitoring procedures
- Identify “risky” entities
- Establish monitoring schedule
- Prepare for the monitoring visit
- Conduct monitoring visit & followup



# Monitoring Actions

- Technical Assistance & Reporting
- Probation
- Restrict draws
- Sanctions
  - Repayment
  - Suspend or terminate agreement
- Initiate legal action



# HUD Program Monitoring

- HUD will review four primary areas:
  - Compliance with primary & national objectives
  - Timeliness
  - Consolidated Plan
  - Equal opportunity and fair housing



# Summary: Administration

- CDBG ED activities require administration
  - Multiple roles & responsibilities
- HUD requires performance measure reporting
- Jurisdictions should also monitor and evaluate their activities for results



# ACTIVITY: PROJECT/ACTIVITY RECORDS



# Wrap Up

- Final questions
- Evaluation

