

Legal Opinion: GCH-0074

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Subject: Use of CIAP or CGP Funding for Revolving Loans

June 17, 1993

MEMORANDUM FOR: Dom Nessi, Acting Director, Office of Resident
Initiatives, PR

FROM: Robert S. Kenison, Associate General Counsel, Office of
Assisted Housing and Community Development, GC

SUBJECT: Use of CIAP or CGP Funding for Revolving Loans or other
Financial Lending Programs

This is in response to your memorandum, dated April 28, 1993, in which you requested a legal opinion regarding the use of CIAP or CGP funds for revolving loans, other financial assistance to residents starting or operating businesses related to the management and physical improvement or general operations of public housing.

Both the CIAP Handbook 7485.1 REV-4, paragraph 2-3(b)(7), and the CGP Handbook 7485.3, paragraph 4-9 D., indicate that resident business development or operating financial assistance may be funded through revolving loan funds, following issuance of guidance from Headquarters. As noted in the correspondence attached to your memorandum, advice has not been issued. At the time that this statement was included in the Handbooks, there were contrary opinions and policy concerns regarding the use of modernization funding for resident business activities. It was decided that to resolve at least the Office of General Counsel's nonconcurrence, this statement would be added to provide PIH/ORI additional time to draft guidance for our review. To date, we have not received any draft guidance for review. The correspondence attached to your memorandum are the first examples provided for our consideration. We have been advised that housing authorities have provided modernization assistance to resident businesses without prior HUD approval. It is our understanding that a notice is being issued to all housing authorities which prohibits the use of modernization funding for revolving loans for resident businesses until further notice.

It should be noted that the objection regarding revolving funds is not the specific authority to establish such a fund, but the purposes of the fund. See 31 U.S.C. 3302(b); 44 Comp. Gen. 87 (1964) (A Federal agency, but not its grantee, would need specific authority to establish a revolving fund). Although grantee expenditures are not subject to the same restrictions as direct Federal expenditures, it should be noted that grantees are obligated upon acceptance of grant funds to spend them for the purposes and objectives of the grant, subject to any statutory or special conditions imposed on the use of assistance funds. See 42 Comp Gen. 682 (1963); 2 Comp. Gen. 684 (1923). Also, a revolving fund would be subject to Treasury approval. Cash advances to a grantee are limited to the minimum amounts needed and are to be timed to be in accord only with the actual, immediate cash requirements of the

grantee in carrying out the purpose of the approved program or project. The timing and amount of cash advances are to be as close as is administratively feasible to the actual disbursements by the grantee for direct program costs and the proportionate share of any allowable indirect costs. 31 CFR ¹205.4.

Revolving funds are also addressed in section 402 of the Annual Contributions Contract (ACC). Section 402(C) provides as follows:

If the Local Authority operates other projects or enterprises in which the Government has no financial interest, it may, from time to time, withdraw such amounts as the Government may approve from monies on deposit under the General Depository Agreement for deposit in and disbursement from a revolving fund provided for the payment of items chargeable in part to the Projects and in part to other projects or enterprises of the Local Authority: Provided, That all deposits in such revolving fund shall be lump sum transfers from the depositaries of the related projects or enterprises and shall in no event be deposits of the direct revenues or receipts.

(emphasis added). This paragraph illustrates that a housing authority may have separate interests and assets which it may use for purposes such as fostering resident businesses. A housing authority could establish separate accounting for these assets or it could pool these funds as described above. A likely source of such funds would be section 8 excess administrative fees or locally funded housing income.

Section 14(b) of the United States Housing Act of 1937 provides that the Secretary makes modernization assistance available to public housing agencies "for the purpose of improving the physical condition of existing low-rent public housing projects and for upgrading the management and operation of such projects to the extent necessary to maintain such physical improvements." This assistance may be made available only for low-rent housing projects which are owned by public housing agencies; are operated as rental housing projects and assisted under section 5 or section 9 of the United States Housing Act; are not assisted under section 8 of the United States Housing Act; and which meet such other requirements of the Secretary.

Economic development costs are eligible in both CIAP (¹ 968.210(e)(3)(ii) and CGP (¹ 968.310(g)(1)) as part of management improvement costs. Management improvements, development-specific or PHA-wide in nature, are eligible costs where needed to upgrade the operation of the PHA's developments, sustain physical improvements at those developments or correct management deficiencies. Management improvements and planning costs may be funded as a single modernization project. Economic development activities, such as job training, resident employment and contracting with resident businesses, for the purposes of carrying out activities related to the eligible management and physical improvements are eligible costs, as approved by HUD. HUD encourages PHAs, to the greatest extent feasible, to hire residents as trainees, apprentices, or employees to carry out the modernization program in CIAP or CGP, and to contract with resident-owned businesses for modernization work. See 24 CFR part 963, published May 11, 1992, at 57 Federal Register 20184.

Based on these statutory, regulatory and ACC requirements, we have considered the examples provided in the correspondence attached to your memorandum and offer the following advice:

1. Project Entrepreneurship - Frederick, Maryland.

The Executive Director of the Housing Authority of the City of Frederick, Maryland requested approval of this program to assist housing authority residents in starting their own businesses, specifically for the purposes of carrying out activities related to the management and physical improvement or general operation of the project. Under CIAP, \$35,000 was to be used to contract with a consultant to provide technical assistance and training to housing authority residents or resident groups who wished to start their own business. After completion of procurement procedures, a contract was awarded to a consultant to implement this program in the amount of \$14,400. It is now requested that the remaining \$20,000 be used to establish a revolving loan fund, for the use by residents attempting to start a business.

We would agree that the contract with the consultant would be an eligible economic development cost under CIAP; however, the revolving loan fund, subsidized by CIAP, is not an eligible economic development cost because it is not specifically related to management or physical improvement activities. Further, the housing authority must make its payments pursuant to the cash management requirements of HUD and Treasury and must use the established letter of credit system. The housing authority has no legal authority to disburse grant funds for other than program purposes. The housing authority may use the grant funds directly or award contracts to perform the grant-related work. In awarding contracts, the housing authority must in addition to following the statutory and programmatic restrictions, adhere to the basic principles of open and competitive bidding. See 24 CFR part 85; 55 Comp. Gen. 390 (1975). By using the resident-owned business contracting regulations at 24 CFR part 963, the housing authority may be able to achieve the same goals as a revolving loan fund. The Executive Director's letter indicates that local banks, and even the Small Business Administration are reluctant to loan money for start-up costs to these residents, as generally they have no assets, collateral, or credit history. This problem could also be solved through contracting. The housing authority could award labor-only contracts and provide the necessary supervision, materials, equipment and tools needed. Resident training could also be incorporated into these contracts. After completing up to \$500,000 (threshold established in part 963) in project-related work, the resident business will have gained experience, references and sufficient capital for their newly-formed business.

2. CIAP Economic Development Loan Agreement, Dover Housing Authority.

The Dover Housing Authority used CIAP management improvement funds in the amount of \$31,500 to fund the start-up costs of a resident-owned laundromat. The Authority wishes to enter into a repayment agreement with the Resident Management Corporation (RMC) and establish, with the repaid funds, a revolving loan fund for financing resident initiative programs. After the loan is repaid, the RMC would resume paying rent to the Authority.

Any income other than dwelling rental income is subject to the requirements at 24 CFR ¹ 990.109 and must appear in budgets approved by HUD. This income would be added to the projected average dwelling rental income per unit to obtain the Projected Operating Income Level. 24 CFR ¹990.109(e)(3). The Operating Income is then offset by operating subsidy (i.e., the operating income is counted in the performance funding system and reduces the amount of subsidy). 24 CFR ¹990.101(c)(5). The Authority could use its income for

program purposes, but it would have to be able to compensate for the reduced operating subsidy. Resident initiative programs (economic development or resident management as described in parts 986 or 964) would be appropriate program purposes, and the manner in which to fund these programs (i.e., revolving loan fund) would be the Authority's choice.