

OVERVIEW OF FEDERAL PROGRAM INCOME

The U.S. Department of Housing and Urban Development (HUD) makes important distinctions in how it defines Program Income for the HOME Investment Partnerships Program (HOME) and the Community Development Block Grant Program (CDBG). If your property received either, or both, of these funding sources, you are required to annually report the amount of Federal Program Income your property generated, distinguishing between HOME Program Income and CDBG Program Income.

HOME Program Income, as defined by HUD at 24 CFR 92.2, means the gross income received by the “participating jurisdiction” (that is, the City of San Francisco, acting through the Mayor’s Office of Housing). This includes *payments of principal and interest made on HOME loans originated by the City*.

CDBG Program Income, by contrast, as defined by HUD at 24 CFR 570.500, means the gross income received by the CDBG “recipient” -- generally, the borrower of CDBG funds lent by the City -- less costs incidental to the generation of the CDBG program income times the percentage CDBG funds made up the project’s total development cost. Thus, CDBG Program Income is the result of multiplying *net cash-flow* which the borrower is allowed to retain as “surplus” (i.e. revenues generated from the rental of real property purchased or improved with CDBG funds less all regular operating expenses, debt service, and reserve deposits associated with operating that property) *times the proportion of CDBG funds to total project development cost* (i.e. CDBG participation percentage). Depreciation and Partnership Management Fees are not included as a regular expense or reserve fund in calculating CDBG program income. Also, for clarification, Property Management Fees are not considered program income but are included as a regular operating expense item.

For example, if a building has a cash flow surplus of \$10,000, and 10% of total project development cost was CDBG funded, then \$1,000 would be considered CDBG Program Income. *Only after all building expenses and adequate operating and replacement reserves are funded does the building generate CDBG Program Income.*

Eligible Uses of CDBG Program Income

CDBG Program Income that is generated on rental housing projects has restrictions on how it may be used by the borrower. In addition, the City is required to report to HUD the amount **and** eligible use of program income received by recipients of housing development funds.

CDBG Program Income can be used for any CDBG-eligible activity -- including predevelopment activities -- as long as it is also consistent with the City’s current Consolidated Plan and the City’s current Action Plan. As most of you know, CDBG eligible activities are found at 24 CFR 570.201-206. The most likely eligible activities for which you could use CDBG Program Income include: acquisition, rehabilitation and preservation activities, and planning activities.

Please consult the CDBG program regulations (see <http://law.justia.com/cfr/title24/24-3.1.1.3.4.html> or <http://www.hud.gov/offices/cpd/communitydevelopment/library/ch2tabl.pdf>) to verify that your specific intended use is actually eligible. You should also check to verify that your proposed activity is not identified as an ineligible activity as described at 24 CFR 570.207. Please note that all building reserves must be funded and approval is required before funds can be used on any activity other than the property which generated the Program Income.

Distribution of Program Income

Please review each project's loan agreements for specific distribution requirements, and bear in mind that, in general, the distribution of Program Income *shall not* be made under any of the following circumstances:

1. **Notice of Default:** When written notice of default has been issued by any entity with an equitable, legal or beneficial interest in the project; or when the City has determined that the Borrower or the Borrower's management agent has failed to comply with City's written notice of any reasonable requirement for proper maintenance of the property; or
2. **Debt Service and Operating Expenses:** If all currently required debt service and operating expenses for the property have not been paid; or
3. **Replacement and operating reserves:** If the replacement reserve account and/or operating reserve account is not adequately funded; or
4. **Future Payments:** If the City determines that the Borrower has not set aside adequate funds to cover future payments on other loans or liabilities that are secured by and/or accruing against the property; or
5. **Annual Program Compliance Reports:** If the Annual Program Compliance Reports have not been submitted for that year; or
6. **City Approval:** Without prior written approval by the City of the amount of such distribution.