

**Office of
The City Attorney
City of San Diego**

**MEMORANDUM
MS 59**

(619) 533-5800

DATE: August 23, 2011

TO: Councilmembers Carl DeMaio and Todd Gloria

FROM: City Attorney

SUBJECT: Legal Analysis Regarding the Acceleration of Repayment of Community Development Block Grant Debt by the Redevelopment Agency of the City of San Diego

INTRODUCTION

On June 27, 2011, the San Diego Housing Authority approved the one-time use of San Diego Housing Commission funds to support the operation of the Neil Good Day Center (Center). While discussing this item, the Housing Authority expressed interest in exploring the use of Community Development Block Grant (CDBG) funds, specifically the repayment of CDBG debt by the Redevelopment Agency of the City of San Diego (Agency) pursuant to the Repayment Agreement By and Between the Redevelopment Agency of the City of San Diego and the City of San Diego (Repayment Agreement), to support the future operation of the Center. In particular, Housing Authority members DeMaio and Gloria in a joint motion requested that the City Attorney conduct a legal analysis of this issue.

QUESTIONS PRESENTED

1. Is it legally possible to accelerate the Agency's repayment of CDBG debt under the Repayment Agreement?
2. If so, is there a limit on how much of the accelerated repayment funds may be allocated to the Center?

SHORT ANSWERS

1. Yes, it is legally possible to accelerate the Agency's repayment of CDBG debt under the Repayment Agreement.

2. Pursuant to the Repayment Agreement, the funds associated with the Agency's repayment of CDBG debt is considered to be program income. The use of program income for public services such as the Neil Good Day Center is limited to 15 percent of all program income received each program year. 24 C.F.R. §570.201(e)(1).

BACKGROUND

In 2008, the Office of Inspector General (OIG) conducted an audit of the City's allocation of CDBG funds to the Agency for the establishment of various redevelopment project areas. As a result of the OIG audit, the U.S. Department of Housing and Urban Development (HUD) required the City to obtain repayment from the Agency of the allocated CDBG funds.

Accordingly, the City and the Agency entered into the Repayment Agreement on June 30, 2010, which was approved by HUD. The Repayment Agreement requires the Agency to repay CDBG debt to the City in the amount of \$78,787,000 over a ten-year period. Exhibit A of the Repayment Agreement sets forth the "Schedule of Annual Repayments" which requires the Agency to make an annual payment on or before June 30th of each fiscal year from 2010 through 2019. For your reference, a copy of the Repayment Agreement is attached to this memorandum.

ANALYSIS

I. THE AGENCY'S REPAYMENT OF CDBG DEBT TO THE CITY MAY BE LEGALLY ACCELERATED

The Repayment Agreement allows, but does not require, the Agency to accelerate the repayment of the CDBG debt. Specifically, Section 2(c) states in relevant part that "the Agency, with the consent of the City, has the right, but not the obligation, to make prepayment of all or a portion of any of the annual amounts set forth in the Schedule of Annual Repayments. Such prepayment shall be acknowledged in writing by the Agency Executive Director or designee, on behalf of the Agency, and by the Mayor or designee, on behalf of the City, and shall be identified as a credit to the Schedule of Annual Repayment accordingly."

The Repayment Agreement states that a prepayment by the Agency to the City only requires written acknowledgment by the Agency Executive Director and the Mayor. Therefore, a prepayment by the Agency to the City would not require a modification of the Repayment

Agreement. However, in the event that any other terms not already expressed in the Repayment Agreement are negotiated, the Repayment Agreement may need to be amended pursuant to section 6(d), which specifically states that “[t]his Agreement may be amended in writing upon the mutual approval of the governing bodies of the Agency and the City.”

II. THE COUNCIL MAY ALLOCATE UP TO 15 PERCENT OF EACH ANNUAL REPAYMENT BY THE AGENCY TO SUPPORT PUBLIC SERVICES SUCH AS THE OPERATION OF THE CENTER

The Repayment Agreement sets forth that “[a]ll repayments from the Agency to the City pursuant to the Schedule of Annual Repayments shall be treated by the City as program income to the San Diego CDBG Program.” Repayment Agreement § 2(f). HUD regulations involving the use of CDBG funds limit the use of program income for public services to no more than 15 percent of the program income received by the City. 24 C.F.R. § 570.201(e)(1). The operation of the Center, a day center for homeless individuals, constitutes a public service. *See* 24 C.F.R. § 570.201(e). Therefore, if the Agency makes a prepayment, then up to 15 percent of that prepayment amount could be allocated by the Council to the operation of the Center. The remaining 85 percent of the prepayment amount could not be allocated towards the Center or any other project under the public services category.

It should be noted that an Agency prepayment of the CDBG debt could create some difficulty for the City in complying with HUD’s regulation that CDBG funds must be committed and expended in a timely manner. *See* 24 C.F.R. § 570.902. This “timeliness rule” prohibits the City from having more than 1.5 times its annual allocation sitting in its line of credit at the U.S. Treasury. *Id.* HUD is entitled to withhold future grants if the City chronically retains CDBG funds in an amount more than 1.5 times its line of credit. Therefore, if the Agency proposes to make a prepayment of the CDBG debt, this Office suggests that the City’s CDBG staff establish a plan which ensures that the City properly allocates the prepayment CDBG funds and remains in compliance with all applicable HUD regulations.

CONCLUSION

The Agency may legally accelerate repayment of CDBG debt to the City as agreed to by the Agency Executive Director and the Mayor. As set forth in the Repayment Agreement approved by HUD, the Agency’s repayment of CDBG debt to the City constitutes program income. And, according to HUD regulations, up to 15 percent of program income received by the City in any program year may be allocated to fund public services such as the operation of the Center.

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Because of the intricacies involved with the proper handling of CDBG funds, it is recommended that the City's CDBG staff be involved with any contemplated prepayment involving the Repayment Agreement to ensure proper compliance with HUD regulations.

JAN I. GOLDSMITH, CITY ATTORNEY

By



Kenneth R. So
Deputy City Attorney

KRS:mm

Attachment

cc: Mayor Jerry Sanders
Councilmembers
Andrea Tevlin, Independent Budget Analyst (IBA)
Beth Murray, Deputy Director,
City Planning & Community Investment
Janice Weinrick, Deputy Executive Director,
Redevelopment Agency

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