

# TRANSMITTAL

To:  
**THE COUNCIL**

Date: **SEP 14 2015**

From:  
**THE MAYOR**

**TRANSMITTED FOR YOUR CONSIDERATION. PLEASE SEE ATTACHED.**



Ana Guerrero

**ERIC GARCETTI**  
Mayor



Eric Garcetti, Mayor  
Rushmore D. Cervantes, General Manager

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September 14, 2015

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Council District: Citywide  
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Honorable Eric Garcetti  
Mayor, City of Los Angeles  
Room 303, City Hall  
200 N. Spring Street  
Los Angeles, CA 90012

Attention: Mandy Morales, Legislative Coordinator

**COUNCIL TRANSMITTAL: STATUS OF COMMUNITY DEVELOPMENT BLOCK GRANT BALANCES ON PROJECT AND PROGRAM ACCOUNTS, AS WELL AS TIMELINESS OF EXPENDITURES AND RECOMMENDATIONS FOR REPROGRAMMING OF CDBG FUNDING**

**SUMMARY**

The Los Angeles Housing and Community Investment Department (HCIDLA) is transmitting the results of its review of the Community Development Block Grant (CDBG) accounts with City departments administering the projects and programs. This is in preparation for a workout plan requested by the US Department of Housing and Urban Development (HUD) in response to the City's missing the CDBG timeliness standard set by HUD. This report discusses reprogramming recommendations, as well as recommendations for getting the City on track with its CDBG spending. One of the main recommendations includes resuming the use of the CDBG Expenditure Policy and Guidelines, last approved and revised by Council in 2003 (CF 01-2765-S2).

**RECOMMENDATIONS**

The General Manager of the Los Angeles Housing and Community Investment Department respectfully requests that:

- I. Your office schedule this transmittal at the next available meeting(s) of the appropriate City Council committee(s) and forward it to City Council for review and approval immediately thereafter;

II. The City Council, subject to the approval of the Mayor, take the following actions:

A. Authorize the General Manager of HCIDLA, or designee, to:

1. Request Council Offices, the City Administrative Officer (CAO), and the Chief Legislative Analyst (CLA) work with HCIDLA and report in two weeks to identify CDBG-funded projects that can have funds reprogrammed and identify projects that could receive the CDBG funds and expend the funds by January 30, 2016
2. With the assistance of the CAO and CLA, develop a revised CDBG Expenditure Policy and Guidelines, based on the 2003 version, and report to Mayor and Council within 60 days, providing sufficient time to ensure the policy is ready to be used for the drafting of the Program Year 42 Action Plan
3. With the assistance of the CAO and CLA, prepare a workout plan to HUD describing the City's plans to address the CDBG timeliness problems and report to Mayor and Council within 30 days with this plan

D. Authorize the Controller to:

1. Transfer appropriations to reimburse the General Fund for related costs

**From:**

Account	Title	Amount
22J108	Building and Safety – 39 <sup>th</sup> Year PACE	\$12,529.39
43K108	Building and Safety – 39 <sup>th</sup> Year PACE	58,694.92
43L108	Building and Safety – 40 <sup>th</sup> Year PACE	59,014.71
	Total	\$130,239.02

**To:**

Account	Title	Amount
22K299	Reimbursements to General Fund	71,224.31
43L299	Reimbursements to General Fund	59,014.71
	Total	\$130,239.02

- E. Authorize the General Manager of HCIDLA, or designee, to prepare any Controller's instructions needed to implement actions approved by the Council and Mayor on matters presented in or deriving from this transmittal, and/or to make necessary technical adjustments, subject to the approval of the City Administrative Officer; and further, request that the Controller implement the instructions.

**BACKGROUND**

On February 5, 2015, HCIDLA received a letter from HUD regarding the City exceeding the regulatory requirement of having no more than 1.5 times our annual grant remaining in the line of credit, 60 days prior to the end of the program year (Attachment A). This has been commonly referred as the CDBG timeliness test and HUD is requiring the City to submit a workout plan, or corrective action plan, identifying how we are addressing timeliness. HUD reviews the performance of the City to determine whether it is carrying out its CDBG-assisted activities in a timely manner. HUD considers an

entitlement recipient (the City) to be failing to carry out its CDBG activities in a timely manner if 60 days (January 30) prior to the end of the grantee's current program year (March 31), the amount of entitlement grant funds available to the recipient under grant agreements but undisbursed by the U.S. Treasury is more than 1.5 times the entitlement grant amount for its current program year (24 CFR §570.902[a]). The City must spend program income before entitlement funding; therefore timeliness is also affected by the total program income received during the year. The penalty for not correcting the timeliness issue this year would be HUD taking the amount of money that exceeds the 1.5 times the grant—last year the City exceeded the timeliness standard by \$1.3 million.

The majority of projects where expenditures are behind schedule are due to problems with the process the City uses when approving projects in the Action Plan. Frequently, capital projects are approved by Mayor and Council for CDBG funding before the scope of work is determined, CDBG eligibility is established, and other funding needed for the project's total development cost are secured. During the time it takes for these elements to be identified and reviewed, CDBG funding stays in the City's accounts and hinders the City in meeting the CDBG timeliness standard. Additionally, many City departments that will have to administer the future projects were not consulted before the planned project award, frequently resulting in the new projects not aligning with departments' prior strategic plans and staffing constraints. Further, the practice of providing funding to projects as "seed money," while the developer seeks alternate sources money to fully fund the project, has proven to be unsuccessful.

The City submitted a response to HUD outlining the development of the workout plan, indicating that it would be submitted after Mayor and Council approval (Attachment B). One of the main reasons for the decrease in CDBG spending is a result of the loss of the category of Community Based Development Organizations (CBDO). In January 2014, the HUD issued a letter disallowing the City's method of using CBDOs to provide services in the City. Starting in April 2014 (Program Year 40), the City CDBG budget changed from having \$31 million in services through public services and CBDOs to \$15 million in public services only. This represented a decrease of over \$16 million in services, where costs are incurred and CDBG is drawn down monthly from HUD. The CDBG budget went from capital representing 49 percent of the budget in Program Year (PY) 39 to 61 percent of the budget in PY 40 and 66 percent in PY 41. As many capital projects have not been ready to go during the year in which they were funded, the amount and portion of the CDBG funding tied to capital is increasing, and significantly contributing to the City's timeliness problem.

#### Changes in Percentage of Capital Projects in CDBG Budgets over Time

Program Year	Services (Public Services and CBDO)	Capital (Econ Dev, Housing, Neighborhood Improvements)	Administration & Planning	Total
PY 39	\$31,108,964	\$44,073,836	\$13,904,449	\$89,087,249
	35%	49%	16%	100%
PY 40	\$15,899,424	\$45,702,073	\$13,863,380	\$75,464,877
	21%	61%	18%	100%
PY 41	\$11,800,099	\$48,930,429	\$13,133,703	\$73,864,231
	16%	66%	18%	100%

The City has had issues with CDBG timeliness in the past, as HUD found the City to be out of compliance with the timeliness standard in 2000 and 2007. After the 2000 finding, the Mayor proposed



a CDBG Expenditure Policy and Guidelines (see Attachment C). Staff from the offices of the Mayor, CLA, CAO, and the former Community Development Department refined the policy, which was adopted by Council (CF 01-2765-S2). This policy still has elements that the City could follow to address the City's systemic problems in spending CDBG.

**TIMELINESS**

As of April 1, 2015, the start of PY 42, there was nearly \$140 million in CDBG allocated to projects. These projects spanned from 2006 to 2015 and cover 265 accounts and represent approximately 136 projects or programs. As of August 21, 2015, there was over \$104 million (74 percent of the budget) that was not yet in a contract and encumbered. An additional \$14.5 million (10 percent) was encumbered and not yet expended, and only \$21 million (15 percent) had been expended and drawn down from HUD for reimbursement.

CDBG	Funds	Percentage
Appropriations at start of PY 41, incl. program income and prior year funds	\$139,861,333	·
<b>Status of Funds through 8/21/15:</b>		
Unencumbered Funds <sup>1</sup>	\$104,176,530	74%
Encumbered Funds <sup>2</sup>	\$14,547,699	10%
Expenditures	\$21,137,105	15%

HCIDLA has been monitoring the amount of CDBG entitlement and program income that the City has on hand. As of August 14, the City is at 2.31 times the entitlement. To resolve this problem, by January 30, 2016, the City needs to expend a minimum of \$14 million above the current projected spending.

**Timeliness and Reprogramming Needed to Meet HUD's 1.5 Timeliness Requirement**

CDBG	Funds
<b>1. Grant balance on hand as of 4/1/15, the start of PY 41</b> (includes PY 41 entitlement and remaining prior years' funds and program income)	\$119,717,514
<b>2. Grant expenditures needed to meet timeliness at start of PY</b> (includes projected program income)	\$54,591,279
<b>3. Estimated expenditures through 1/30/16:</b>	
a. Expenditures thru 8/21/15 for housing, economic development, and neighborhood development and public facilities projects <sup>3</sup>	\$13,221,400
b. Projected expenditures for services and staff through 1/30/16	<u>\$27,035,299</u>
<b>c. Subtotal of estimates of expenditures through 1/30/16</b>	<b>\$40,256,699</b>
4. Grant expenditures needed (row 2) less estimated expenditures (row 3c) = <i>Minimum amount needed to be reprogrammed to meet timeliness</i>	<b>\$14,334,580</b>
5. CDBG balance remaining, if City were to meet timeliness requirement	\$74,931,798

<sup>1</sup> Unencumbered funding has not yet been set aside for a contract, frequently because the project is not ready and the PEP has not been completed.

<sup>2</sup> An encumbrance is the portion of the set aside for a contract. An encumbrance is a projection and not yet an expenditure. If project conditions continue as they were when budget was set, then the encumbrance will become an expense. Conditions, however, may change over the course of the project.

<sup>3</sup> Actual expenditures will be higher through January 2016, but future expenditures are unknown for these capital projects.

If the City were to meet the timeliness goal at the end of January, we would still have nearly \$75 million of CDBG funds remaining. To achieve timeliness for this year, we need to reprogram funds and spend a minimum of \$14.3 million. However, due to the uncertainty of the projected expenditures, HCIDLA recommends that at least \$20 million be reprogrammed to ensure that the deadline is met.

### CDBG FUND MANAGEMENT

As part of the administration of CDBG, at mid-year the administrator of CDBG, now HCIDLA and formerly the Community Development Department, sends out the balances of accounts associated with CDBG projects, programs, and administration. On July 8, 2015, HCIDLA sent out a list of CDBG projects and their balances to City departments requesting the status of projects, funding, and whether funds could be made available for other projects, a process frequently referred to as *reprogramming*. Departments were also asked to submit milestone reports for capital projects that were perceived as being the highest risk for the City.

HCIDLA led meetings in July with City departments, along with staff from the offices of the Mayor and the CLA, to review CDBG projects. Meetings were held with the following departments and bureaus: 1) Building & Safety; 2) City Attorney; 3) Cultural Affairs; 4) Economic and Workforce Development; 5) Engineering; 6) Housing and Community Investment; 7) Housing Authority; 8) Office of the Board of Public Works; 9) Recreation and Parks; 10) Street Lighting; and 11) Street Services. The status of projects was discussed, including impediments to ongoing projects and CDBG unspent savings available for reprogramming, and HCIDLA staff briefed the City staff on the HUD CDBG timeliness standard.

### ANALYSIS

City departments with CDBG capital projects were asked to prepare a milestone report for higher risk projects. HCIDLA staff ranked projects on a scale of one to four, with four being projects of the highest risk to the City for not being completed on time, funds not being spent, potential audit issues, or a combination of reasons. Risk was assigned based on the dollar value of the project, age of the project (with older projects being of greater risk), or a combination of the two.

Risk	Rationale
4	High—due to high dollar value and/or age (PY 39 or older capital projects)
3	Medium (≥\$400K and/or PY 40 or older services or admin)
2	Low—needs attention, maybe just administrative, or smaller project
1	Lower—project mostly done, moving PY 40 projects, PY 41 of <\$400K

From meeting with staff from the other City departments and reviewing CDBG projects and expenditures, HCIDLA staff found there were many opportunities for improvement as to movement and expenditures of projects. See Attachment D for a summary of the status of CDBG projects from the July meetings. A number of large projects will not complete construction until December 2016 at the earliest, and more are not scheduled to be completed until at least 2017 to 2019.

Based on current spending and the reported progress on CDBG projects, the City is not on track to meet the CDBG timeliness standard by January 30, 2016.



**NECESSARY REPROGRAMMING**

Through discussions with the City departments, nearly \$6.5 million was identified as available for reprogramming (see Attachment F); however, \$550,043.20 of it is needed to cover accounts that were approved for reprogramming as part of the PY 41 Action Plan, but were not actually available. Two projects with funds totaling \$550,043.20 had already had invoices paid and therefore, though Council approved the funds to be taken, they were in fact not available, resulting in an over obligation of funds for PY 41. As a result, the balance of \$5.9 million is the only amount currently identified as available for reprogramming.

Funding	Amount
Funds identified for reprogramming	\$6,498,627.74
Over obligation of funds	-550,043.20
<b>Funds available for reprogramming</b>	<b>\$5,948,584.54</b>

Based on current spending and estimated expenditures, approximately \$14 million (see page 4) needs to be reprogrammed to projects that can spend the funds before January 30, 2016. Funds have to be reported and drawn down from HUD to be counted in HUD’s timeliness calculations. To date, \$5.9 million has been identified as available for reprogramming, leaving nearly \$8.4 million needed.

Below is a list of projects that need additional funding and could potentially expend additional CDBG funds by January 30, 2016. Reprogramming at least \$20 million is recommended to ensure the City is able to meet the next timeliness text with adequate flexibility. Reprogramming funds into existing CDBG projects could potentially accelerate spending of CDBG. For example, if a project has gone through the environmental clearance and has an executed contract with the City, depending upon the scope of work for the additional funds, they may not need another environmental clearance and could do a contract amendment, rather than needing to start a brand new contract. From the list below, funding should be moved to the most viable of the projects; those being projects most likely to spend the funds by January 30, 2016.

Project	CD	<u>For PY 41</u> Could be spent by January 2016	<u>For PY 42</u> Amount identified as needed
1. Multifamily projects—acquisition and/or rehabilitation	Citywide	\$18,800,000	TBD
2. Marlton Square land acquisition	10	\$4,148,800	
3. Marlton Square Section 108 interest payment	10	823,000	
4. LA BusinessSource Program <sup>4</sup>	Citywide	900,000	
5. Homeownership Program (can spend by March 2016, not January)	Citywide	500,000	
6. Hillview Mental Health Center in Sunland Tujunga Hansen Dam Homeless Facility Improvement <sup>5</sup>	7	500,000	
7. Loco'l Restaurant & Commissary Project by Welocal 1, LLC	15	275,000	

<sup>4</sup> With \$100,000 for each of the nine BusinessSource Centers.

<sup>5</sup> Project was funded in PY 39 and working toward contract execution in March 2015. Funding was reprogrammed through PY 41 Action Plan. This would restore funding to the project.

Project	CD	For PY 41 Could be spent by January 2016	For PY 42 Amount identified as needed
8. Bradley Ave. Green Alley with Pacoima Beautiful (part of NIF RFP, CF 14-0310)	7	250,000	
9. Bradley Plaza Project	7	200,000	
10. LA Theater Center	14	35,000	
11. Central Avenue Façade Improvements	9		500,000
12. ADA Housing Modifications	Citywide		TBD
13. Aging ADA modifications for Senior Centers	Citywide		TBD
14. FamilySource ADA modifications for Centers	Citywide		TBD
<b>Subtotal</b>		<b>\$26,431,800</b>	<b>\$500,000</b>
<b>Grand Total</b>			<b><u>\$26,931,800</u></b>

This reprogramming will only be a short-term solution to meeting the current and ongoing timeliness crisis. The City's current process for planning and approving projects has systemic problems, and unless we change the way we plan and operate with CDBG, the City will be facing this problem again next year, with an even larger financial overage, as the amount of funds in nonmoving capital projects continues to increase.

In conjunction with the CAO and CLA, HCIDLA will report in two weeks with detailed reprogramming recommendations. Approving the transfer of funds to another project is just one step toward spending the funds. We need to act urgently to have authority to execute contracts; get environmental clearance with approval to begin work; submit and approve PEPs; execute contracts; perform the scope of work; submit invoices; drawdown funds; etc. to get the funds expended by January 30, 2016, in order for them to count toward the timeliness requirement. City departments also need to invoice regularly for CDBG expenditures for capital projects, services, and administration to ensure tracking of progress and status of timeliness is as current as possible. Additionally, after a capital project is completed, it must have the ability and funding to be maintained to meet a CDBG national objective. If it does not, the project will raise audit issues with HUD, and could potentially require repayment to HUD with general funds. As the City moves forward with reprogramming to meet the timeliness requirement, the funding of projects may occur irrespective of Council boundaries and reprogramming of funds may move across and between districts to position funds in projects that are ready and moving quickly.

### PROCESS IMPROVEMENTS

The offices of the Mayor and City Councilmembers, working with the CAO and CLA, and the assistance of the City departments and HCIDLA, should identify projects that meet the CDBG criteria and are able to spend funds by January 30, 2016. The first priority is to identify projects that are not moving and could be terminated or delayed. The second priority is to identify alternate projects that are already under way and can use more CDBG funds by the deadline or are CDBG eligible and have other federal funds that could be exchanged for CDBG funds

Additionally, HCIDLA, with the assistance of the CAO and CLA, should review the City's former CDBG Expenditure Policy and make recommendations for policy changes that take historical problems into consideration. A number of projects that used CDBG funds to acquire property did not have the



needed additional funding to complete them and meet a national objective, and which have resulted in audit findings. The City is now having to address these audit finding and may have to use general funds to reimburse HUD.

Additionally, if the City were to try to reduce the CDBG backlog by making float loans, we need to make sure that they are secure investments. Float loans use CDBG funding that is already programmed for other projects, but which we do not expect to need the funding for some time. It is essential that the activity funded by the loan meet CDBG requirements for eligibility and national objective. Float loans can provide construction financing or pay for land acquisition before the permanent financing comes from another source. Projects being funded should have permanent financing to make sure float loan will be repaid on time. Rushing to use float loans before adequately ensuring the investment is eligible could raise future audit issues with HUD, thereby creating other problems while trying to find solutions to timeliness. A float loan must be repaid within 2½ years, and one of the issues with using them as a solution is that unless the City fundamentally changes the way we plan for and award CDBG to projects, we would merely be pushing our problem two years into the City's future, rather than solving our spending issues.

If there are capital projects that are funded with federal funds, we should explore the possibility of exchanging CDBG funds for those federal funds. We cannot trade CDBG funds for general funds, however, as that would be supplanting the local funds with CDBG, and federal law prohibits recipients of federal funds from replacing state, local, or agency funds with federal funds.

Any of the changes that the City works to implement would be considered a substantial amendment to the annual Action Plan and needs to have a 30-day public comment period.

### RECOMMENDATIONS FOR FUTURE SYSTEMIC CHANGES

The intent of the CDBG Expenditure Policy and Guidelines, adopted in 2003, was for the City to clarify and delineate how CDBG funds will be allocated within the Housing and Community Development Annual Action Plan and how savings will be reprogrammed during a program year. The policy provides a readiness standard by which all projects will be reviewed in advance of any CDBG funding allocations, and indicates that capital projects would be funded incrementally and funding only provided for the portion of the project that can be expended within one program year. The policy includes caveats on the borrowing of CDBG funds, deadlines for the repayment of borrowed funds, outlines the process for operating departments to apply for CDBG funding, and what the department needs to submit about each project. Much of what is in the policy, especially about what needs to be done before a project will be funded, would assist the City in meeting timeliness in the future. It is recommended that the policy be updated and presented to Mayor and Council for approval.

Suggestions to change our system of funding CDBG projects include:

- 1) Use multiyear planning for projects so funding priorities are identified in advance
- 2) Minimize standalone mid-year reprogramming of funds as the reviewing of proposed projects is not given sufficient time (as is given during the Consolidated Planning process)
- 3) Schedule meetings with HCIDLA, individual Council offices, and City departments to discuss CDBG applications in advance of applications being submitted and consider:
  - a) Project's eligibility for CDBG and whether it will meet a national objective
  - b) A department's capacity to manage the project during that year, in addition to the other planned projects

- c) The Council office priorities for the district
  - d) Whether there are funds identified to maintain the project once completed, which is part of meeting HUD's national objectives for CDBG
- 4) Hold follow up meetings after applications submitted to review:
- a) Are there sufficient funds for the project?
  - b) Will funding for project be spent during the proposed program year?
  - c) Is the project eligible?
  - d) Is the department that would be managing the project aware and in support of the project?
  - e) Does the Council office or Mayor's office support the project?

If the City uses the CDBG Expenditure Policy, funding would be given in blocks of money that could be spent each year as projects are able to spend them. The revised policy would be the backbone of the City's workout plan to HUD describing how we will change our process to meet CDBG timeliness requirements. In the interest of time and getting the workout plan to HUD, HCIDLA will submit the workout plan to HUD and to Mayor and Council under separate cover. The workout plan must include:

1. Identification of main causes of excess backlog
2. Identification of activities to be modified or terminated
3. Reprogramming available funds
4. Planned actions
5. Long range plans
6. Milestone schedule
7. Drawdown projection
8. Progress reports
9. A commitment to execute the workout plan

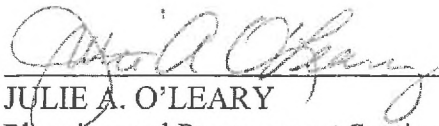
HCIDLA will continue working with the various departments administering CDBG to develop the milestone and drawdown projections to include in the plan. Working with staff from offices of the Mayor, Councilmembers, CAO, and CLA, HCIDLA will draft the long range plans for the City to change the systematic problems in how we plan for CDBG capital projects, with the goal to meeting CDBG timeliness standards in the future, as well as providing the best possible projects to benefit and serve low-income individuals in the city.

### FISCAL IMPACT STATEMENT

This report includes Controller instructions to transfer appropriations in the amount of \$130,239.02 to reimburse the General Fund for prior year Building and Safety related costs associated with the PY 39 and PY 40 Proactive Code Enforcement Program. These funds are prior year grant funds previously approved for this purpose. This amount will be reflected as CDBG expenditures after the funds are drawn down from HUD and transferred to the general fund.

Other actions in this transmittal do not directly impact the General Fund. However, if CDBG funds are taken or repayment is required by HUD in the future, the General Fund may be impacted.

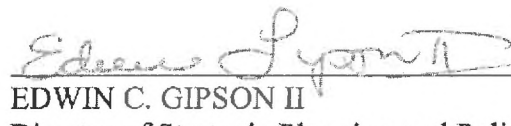
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LAURA K. GUGLIELMO  
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Approved by:



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RUSHMORE D. CERVANTES  
General Manager

RDC:LKG:EDG:JO

Attachments:

- A. February 5, 2015 letter from HUD to City
- B. March 6, 2015 response letter from City to HUD
- C. CDBG Expenditure Policy and Guidelines
- D. Summary of Status of CDBG Projects
- E. Timeliness calculations for PY 41
- F. Status of CDBG Balances through August 21, 2015