

## EXHIBIT 4-H

### PROGRAM INCOME

Program income means gross income that is received by either a recipient or sub-recipient and has been directly generated from the use of CDBG funds. When program income is generated by an activity that is only partially assisted with CDBG funds, the income shall be prorated to reflect the percentage of CDBG funds used.

Note: This exhibit applies to both the CDBG Housing Program and the CDBG Economic Development Program. Please refer to Chapter 8 for additional requirements related to CDBG economic development activities.

#### A. EXAMPLES OF PROGRAM INCOME

1. Program income examples include, but are not limited to, the following:
  - Proceeds from the disposition by sale or long-term lease of real property purchased or improved with CDBG funds;
  - Proceeds from the disposition of equipment purchased with CDBG funds;
  - Gross income from the use of rental of real or personal property acquired by the grantee with CDBG funds, less costs incidental to generation of the income;
  - Gross income from the use or rental of real property, owned by the grantee that was constructed or improved with CDBG funds, less costs incidental to generation of the income;
  - Payments of principal and interest on loans made using CDBG funds;
  - Proceeds from the sale of loans made with CDBG funds;
  - Proceeds from sale of obligations secured by loans made with CDBG funds;
  - Interest earned on funds held in a revolving fund account;
  - Interest earned on program income pending its disposition; and
  - Funds collected through special assessments made against properties owned and occupied by households not of low and moderate income, where the assessments are used to recover all or part of the CDBG portion of public improvement.

2. Program income does **not** include, but is not limited to, the following:

- Interest earned on grant advances from the U.S. Treasury. Any interest earned on grant advances is required to be returned to the U.S. Treasury;
- Proceeds from fund-raising activities carried out by sub-recipients that are receiving CDBG assistance to implement eligible activities;
- Funds collected through special assessments that have been made to recover the non-CDBG portion of a public improvement;
- Proceeds from the disposition by the grantee of real property that has been acquired or improved with CDBG funds when the disposition occurs after grant close-out for entitlement grantees;
- Proceeds from the disposition of real property that has been acquired or improved with CDBG funds, where the disposition occurs within a five-year period after expiration of the agreement between the grantee and sub-recipient.
- Proceeds from CDBG economic development loans that are used for economic development activities through a community development organization are not considered program income.

## **B. PROGRAM INCOME PLAN**

MDOC will allow local government grantees to retain program income after project closeout. To do so, a grantee must submit a plan for the proposed use of the program income. (Preferably, a local government would do so within its project application or management plan.) The decision to permit a local government grantee to retain program income will be based upon the grantee's final plan for use and administration of such program income.

## **C. PROGRAM INCOME CONTRACTUAL REQUIREMENTS**

If MDOC determines that program income is to be retained by a grantee, the program income plan will specify the activities that will be undertaken with the program income and that all provisions of the program income plan shall apply to the specified activities. Accordingly, the contract will contain the following provisions that will be modified during contract negotiations to fit the specific program income situations that exist.

The grantee will be permitted to retain program income generated by the activities described in the contract under Section 5, Scope of Activities. Program income

received before the project is closed out by MDOC must be expended on project activities before additional CDBG funds are requested by the grantee. MDOC will deduct the amount of program income on hand as shown on the drawdown form from the amount requested by the grantee. The receipt and expenditure of program income shall be treated as additional CDBG funds, subject to all applicable requirements governing the use of CDBG funds. The receipt and expenditure of program income shall be recorded as part of the financial transactions of the grant program. At the time of closeout, MDOC will specify the conditions and requirements that will apply to program income received after closeout by the grantee.

The CDBG Program Officer preparing the contract will insert specific program income requirements that relate directly to the project, based on the application, other open or closed CDBG projects, current MDOC policy for program income, the existence and purpose of revolving loan funds, and the source of program income that is expected to be generated from project activities.

#### **D. USES OF PROGRAM INCOME**

1. After Project Closeout -- For the years of 1992 and prior:
  - If the grantee does not have an on-going grant that was received directly from MDOC at the time of closeout, the MDOC encourages the use of program income for CDBG eligible activities that assist a minimum of 51% low and moderate-income persons.
  - Program income should be expended on activities as specified in the local government's program income plan and/or closeout agreement.
2. Before Project Closeout -- For the years of 1993 and later (*this applies only to program income managed by local governments*):
  - Program income received by a grantee before closeout must be used in accordance with the provisions of Title I. As such, all the regulations and requirements that applied during the term of the project will apply to the program income received before closeout. For the most part, this means that program income must be used for eligible CDBG activities, and that a minimum of 51% of the funds must be used for activities that are clearly designated to meet identified needs of persons of low and moderate income.
3. After Project Closeout -- For the years of 1993 and Later (*this applies only to program income managed by local governments*):

MDOC has developed the following proposed policy for expenditure of program income after close-out which will meet the federal national objective

of benefiting low and moderate income persons (LMI) and allow local governments some flexibility with their program income:

- As program income is received, the following applies: For CDBG housing and public facilities activities: a maximum of 15% would be allocated to an administration fund and a minimum of 85% allocated to an activity fund for each state fiscal year;

For CDBG economic development activities: a maximum of 18% would be allocated to an administration fund and a minimum of 82% allocated to an activity fund for each state fiscal year.

- Under the activity fund, 70% of the expenditures of that fund in any year would have to principally benefit LMI (51%) persons, be a CDBG eligible activity, and meet federal Title I regulations. The "70%" derives from the federal statutory requirement that requires states to demonstrate to HUD that at least 70% of CDBG funds expended are used to assist LMI persons or households.
- The remaining 30% of the activity fund could be used for any CDBG eligible activity as long as it meets Title I requirements. Grant recipients would still need to submit a program income report for any program income generated. ► This strategy assures that program income is being spent on CDBG eligible activities that principally benefit 51% low and moderate-income persons, the original intent of the program, but allows some flexibility to carry out eligible CDBG activities in those communities that are not 51% LMI community-wide.

All program income received by a grantee after closeout must continue to be used in accordance with the provisions of Title I (Davis Bacon wage rates, environmental review, etc.). As such, all regulations and requirements that applied during the term of the project will apply to the program income received after closeout.

Exception: Federal Title I requirements do not apply to funds which are less than \$25,000 received and retained in a single year by a grantee. A grantee may use this amount for any eligible CDBG activity that benefits at least 51% low and moderate-income persons. The first annual period for which it may be applied begins with fiscal year 1994, beginning July 1, 1993.

4. For CDBG economic development payments made to a qualified non-profit:

Payments made to a community development organization that uses the funds for continued economic development activities do not have to

meet any Federal requirements. However, the local government can still establish requirements for re-use of the funds, and require some CDBG requirements to be followed through grant agreements between the local government and the community development organization. A revolving loan fund plan must be executed that is agreeable to the local government. The local government must also execute a sub-recipient agreement with the community development organization for management of the revolving loan fund.

The Department encourages community development organizations to continue to use loan proceeds for CDBG eligible activities that benefit 51% low and moderate-income persons, and to follow activities specified in the revolving loan fund plan.

#### **E. USE OF PROGRAM INCOME IN LIEU OF GRANT DRAWDOWNS**

If at the time of closeout the grantee has another on-going CDBG grant from MDOC, the funds received after closeout will be treated as program income of the on-going grant program, unless MDOC specifies otherwise in the grant agreement or there is a Revolving Loan Fund set-up. MDOC may specify in the grant agreement or in a future grant agreement that program income from an earlier CDBG project will be used for a CDBG project awarded at a later date.

The receipt and expenditure of program income shall be recorded as part of the financial transactions of the grant program in the grantee's financial records. Program income received before grant closeout may be retained by the grantee, with MDOC approval, if the income is treated as additional CDBG funds. If the grantee chooses to retain program income, that income shall affect withdraws of grant funds from the U.S. Treasury as follows:

- Program income in the form of repayments to, or interest earned on, a revolving fund, as defined above, shall be substantially disbursed from the fund before additional cash withdraws are made from the U.S. Treasury for the same activity.
- Substantially all other program income shall be disbursed for eligible activities before additional cash withdraws are made from the U.S. Treasury.

This requirement could lower the total amount of CDBG funds received from MDOC that are actually expended (as opposed to requested and budgeted) for the project. MDOC will decide whether to allow the remaining CDBG funds to be used for further project activities, such as additional housing rehabilitation or to reallocate the remaining funds to other CDBG projects.

## **F. USING PROGRAM INCOME FOR FOR-PROFIT ENTITIES**

A grantee proposing to use CDBG program income, regardless of source, for economic development activities must determine that assistance to for-profit entities is appropriate, as defined in the current Montana CDBG Application Guidelines and HUD policy.

The grantee will have to retain records to document compliance with this requirement, including the financial analysis conducted to determine whether the financial assistance to the for-profit was "necessary and appropriate."

## **G. REVOLVING LOAN FUND(S)**

### **1. Definition and Purpose**

HUD defines a revolving fund as a separate fund with a set of accounts independent of other program accounts, established for the purpose of carrying out a specific activity that, in turn, generates payments to the fund for use in carrying out such an activity. An example is a revolving fund set up for financing housing rehabilitation loans. Loan repayments are paid into the fund and used to finance other rehabilitation loans or loans to businesses.

### **2. Establishment**

Typically, a revolving fund will be established at the time the specific activity begins to generate program income, e.g., principal and interest received by the grantee from payments on rehabilitation loans or business loans.

### **3. Optional Fund Requirements**

The grantee may maintain a separate revolving fund for housing activities and a separate revolving fund for economic development activities. Or, the grantee may opt to utilize a single revolving fund for both activities.

### **4. Mandatory Fund Requirements**

Due to Title I changes, the grantee will be required to maintain a separate fund for revolving activities covered under 1992 and prior contracts, and a separate fund for revolving activities covered under 1993 and future contracts, or combine the two and follow the post-1992 requirements.

### **5. Rules Applying To A Revolving Fund**

Revolving fund activities are subject to the same rules as other CDBG grant activities. They must be eligible activities that meet a national objective and must be carried out in compliance with all applicable program requirements.

## H. REVOLVING LOANS

### 1. Loan Management

The making of real estate and business loans by the grantee parallels in importance the function of a financial institution, such as bank or savings and loan association. Consequently, proper management of these loans is paramount to the success of the CDBG Program.

The guidelines that follow, while not all inclusive, should help the grantee in the management of real estate and business loan activities.

- a. Applicable loan committees should be established to provide citizen involvement and guidance;
- b. All amortized loans made should be supported by amortization schedules and they should be kept current. The loan amortization schedule(s) will serve as the subsidiary loan receivable records;
- c. All loan repayments of principal and interest should be collected directly by the grantee (unless a sub-recipient agreement has been executed between the grantee (local government) and a non-profit community development organization to manage the funds through a revolving loan fund plan);
- d. The person who receives the loan repayments should not be the same person who keeps the records;
- e. All loans made and resulting transactions should become a part of the general accounting records;
- f. A system should be established to monitor all loans outstanding;
- g. A formal policy for dealing with delinquent loans should be established and enforced;
- h. Delinquent loan reports should be issued periodically and used for follow-up;
- i. All loans should be secured by trust indentures;
- j. All borrowers should protect the grantee against insurable risks (where applicable) and the policies underwritten should be on file with the grantee;

- k. Any grants made that provide a contingency for repayment should be appropriately accounted for and secured by the filing of liens.

## 2. Accounting And Reporting Treatment for Revolving Loans

Authoritative literature on accounting for loans, often referred to as revolving loans, is skimpy at best. The December, 1989 GAAFR Review, published by the Government Finance Officers Association, discusses the pros and cons of several possible treatments - each having some theoretical defect. However, the most favored, and recommended, treatment is to report the loan receivable on the balance sheet with a corresponding amount of deferred revenue.

### I. **RECORDKEEPING REQUIREMENTS**

Communities planning to utilize program income must maintain, at a minimum, the following records:

- Sources of program income, including interest earned;
- A schedule of anticipated program income receipts;
- Designated persons(s) or entity(ies) responsible for tracking loan payments and servicing the loan(s);
- Policies and procedures for determining how the program income funds will be expended and for what activities;
- Names of the person(s) or board(s) responsible for implementing the program income plan and for ensuring compliance with applicable requirements;
- Dates and amounts of program income deposits and disbursements; and
- The activities funded with program income.

These records must be available for review. The grantee must retain such records for at least three years from the end of the fiscal year in which the last receipt of program income occurs.

### J. **MDOC OVERSIGHT AND MONITORING OF PROGRAM INCOME**

Because MDOC has ultimate responsibility for the program income retained and used at the local level, it must ensure that such program income is used in a manner

consistent with CDBG requirements. To do so, MDOC has instituted a reporting process that will require an Annual Program Income Report from each grantee.

For the reporting convenience of the grantee, MDOC has designed two versions of the Annual Program Income Report, Version A and Version B.

1. Version A (See **Exhibit 4-H.1**)

The grantee should utilize Version A when it opts to combine the reporting of housing or public facility program income activity. However, such program income activity must be reported separately for the contract years of 1992 and prior and for the contract years of 1993 and later.

The compliance certification on this report must be signed by the appropriate local official. In so doing, the grantee certifies that it has adhered to all Title I compliance requirements as required.

2. Version B (See **Exhibit 8-I**)

The grantee should utilize Version B when reporting CDBG economic development activities for primary and secondary loans.

3. Reporting Period And Filing Deadline

For CDBG housing or public facility activities: The Program Income Report(s) will cover the fiscal year of July 1, through June 30. The reports must be filed with MDOC no later than August 15 of each year.

For CDBG economic development activities: The Revolving Loan Fund Report will cover the calendar year January 1, through December 31. The reports must be filed with MDOC no later than January 31 of each year. Reporting forms will be sent to revolving loan fund managers each December.

Version A

City/Town/County of

Annual Program Income Report  
Receipts, Disbursements and Changes in Fund Balance(s) - All Funds  
for CDBG Housing or Public Facility Activities

For the Fiscal year Ended June 30, 20\_\_

	1992 And Prior	1993 And Later	Totals
<b>Receipts:</b>			
Interest	\$ 15,000	\$ 5,000	\$ 20,000
Principal	10,000	5,000	15,000
<b>Total Annual Receipts</b>	<u>\$ 25,000</u>	<u>\$ 10,000</u>	<u>\$ 35,000</u>
<b>Disbursements:</b>			
Loans	\$ 10,000	\$	\$ 10,000
Grants	5,000		5,000
<b>Total Annual Disbursements</b>	<u>\$ 15,000</u>	<u>\$</u>	<u>\$ 15,000</u>
<b>Transfers Out:</b>			
Drawdowns	\$ 5,000	\$	\$ 5,000
General Government		5,000	5,000
<b>Total Annual Transfers</b>	<u>\$ 5,000</u>	<u>\$ 5,000</u>	<u>\$ 10,000</u>
<b>Total Disbursements &amp; Transfers</b>	<u>\$ 20,000</u>	<u>\$ 5,000</u>	<u>\$ 25,000</u>
Excess Receipts over Disb. & Trans. or Excess Disb. & Trans. over Receipts	\$ 5,000 ( )	\$ 5,000 ( )	\$ 10,000 ( )
Fund Balance(s) Beginning	<u>35,000</u>		<u>35,000</u>
Fund Balance(s) Ending	<u>\$ 40,000</u>	<u>\$ 5,000</u>	<u>\$ 45,000</u>

## PROGRAM INCOME - TITLE I CERTIFICATION

Amendments to Title I of the Housing and Community Development Act require that local governments continue to spend all program income for eligible Community Development Block Grant (CDBG) activities according to all Title I requirements, even after close out of the CDBG project. The following certification is to be executed by the chief local government official to certify in its annual program income report to the Department of Commerce that these requirements have been met.

### Certification

I hereby certify that all program income expenditures generated by Community Development Block Grant (CDBG) activities for the local government of \_\_\_\_\_, were expended for eligible CDBG activities, according to requirements of Title I of the Housing and Community Development Act of 1974, as required by amendments to the Act dated October, 1992.

\_\_\_\_\_  
Chief Local Government Official

\_\_\_\_\_  
Date