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## RECENT TRENDS IN THE COMMUNITY DEVELOPMENT GRANT PROGRAM

PATRICIA HARRIS\*

America's urban areas faced increasingly critical social, economic and environmental problems for which traditional federal categorical grant programs proved ineffective. The enactment of Title I of the Housing and Community Development Act of 1974,<sup>1</sup> the authorizing legislation for the Community Development Block Grant program, presented a sweeping, constructive change in our efforts to meet urban needs in a comprehensive way.

The 1974 Act essentially established a program of annual entitlement grants to all major cities and urban counties, based on an objective needs formula, with discretionary grants to smaller cities awarded on a competitive basis. The legislation cited as its primary objective developing viable urban communities, principally for persons of low and moderate income, and authorized grants for \$8.6 billion through Fiscal Year 1977 to reach this goal.

While the new program had a decided overall impact toward meeting objectives during its first three-year funding period, experience indicated that a change in the distribution and use of funds was clearly needed to fully achieve the major purposes and objectives of the statute. This realization led to policy changes having a significant effect on the program for Fiscal Year 1978. The following Commentary examines these recent trends, preceded by a brief overview of the 1974 Act and the system of categorical grants that led to its enactment.

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\* United States Secretary of Housing and Urban Development.  
1. 42 U.S.C. §§ 5301-17 (Supp. V 1975).

## THE HOUSING AND COMMUNITY DEVELOPMENT ACT OF 1974

Beginning with the Urban Renewal program in 1949,<sup>2</sup> a fragmented system of categorical grant assistance developed in response to specific urban needs, including programs for open space,<sup>3</sup> neighborhood facilities,<sup>4</sup> and water and sewer facilities,<sup>5</sup> culminating with the Model Cities Program in 1966.<sup>6</sup> Applicants submitting detailed project proposals that met established criteria for each specific program were awarded grants on a first-come, first-served basis while funds were available.

Criticism of the categorical grant system was widespread. Each of the programs tended to be narrow in scope, providing assistance on a project-by-project basis for what were, in fact, systemic problems. Excessive federal control and detailed requirements minimized local decisionmaking and delayed application approvals and project execution. Local chief executives were frequently by-passed since semi-autonomous local agencies were often the grantees administering the programs. Rational community development program planning and budgeting were often distorted as communities were influenced to apply not primarily for aid most needed, but for aid that was both available and affordable in light of requirements for local matching funds. Grantsmanship became a prized art. Although the Model Cities Program encouraged a comprehensive, planned attack on physical and social disabilities in low-income neighborhoods, many serious problems endemic to the categorical grant approach were not eliminated.<sup>7</sup>

Seeking to improve this situation by distributing available resources in a more coordinated, orderly manner, a number of legislative initiatives were proposed, resulting in the Community Development Block Grant program under Title I of the Housing and Community Development Act of 1974. The new legislation consolidated existing categorical programs for community development, au-

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2. National Housing Act of 1949, 42 U.S.C. §§ 1401-36 (1970).

3. Housing and Urban Development Act of 1970, § 401, 42 U.S.C. §§ 1500 to 1500d-1 (1970).

4. Housing and Urban Development Act of 1965, § 703, 42 U.S.C. § 3103 (1970).

5. *Id.* § 3102.

6. Demonstration Cities and Metropolitan Development Act of 1966, 42 U.S.C. §§ 3301-74 (1970).

7. *See* STAFF OF HOUSE COMM. ON BANKING AND CURRENCY, 92d CONG., 1st SESS., REPORT AND RECOMMENDATIONS OF THREE STUDY PANELS OF THE SUBCOMM. ON HOUSING 39 (Comm. Print 1971).

thorizing grants to general local governments for a discrete list of essentially similar eligible activities.<sup>8</sup> Each locality is given broad discretion in developing its program, based on local needs identified in a three-year community development plan. The plan demonstrates the utility of having a comprehensive strategy for meeting needs. To coordinate housing and community development, applicants are required to submit a Housing Assistance Plan, which assesses housing conditions, estimates lower-income housing assistance needs, and specifies a realistic annual housing goal for the number of units or persons to be assisted. Moreover, there must be adequate opportunity for citizen participation during the development of the local program.<sup>9</sup>

For metropolitan cities and urban counties (essentially cities and counties in metropolitan areas with populations of at least 50,000 and 200,000, respectively)<sup>10</sup> the apply-and-compete funding procedure used for the categorical programs was replaced by an "entitlement" grant allocation system that assigned funding based on a formula measuring three factors: population, housing overcrowding, and poverty (counted twice).<sup>11</sup> Smaller communities and states, on the other hand, must compete for separate "discretionary balance" funds allocated by the formula to metropolitan and non-metropolitan areas.<sup>12</sup> Communities participating in the categorical programs were entitled to receive their prior funding level for three years, with a gradual phase-in to the block grant funding level.<sup>13</sup> The Act also authorized a special discretionary fund for specific purposes such as innovative projects, disaster assistance and new communities.<sup>14</sup>

Applications from entitlement cities and urban counties not approved or disapproved within seventy-five days of the receipt of a full application are automatically approved.<sup>15</sup> Yet, the Secretary may only disapprove applications where the description of community and housing needs is plainly inconsistent with generally available facts and data, where proposed activities are plainly inappropriate to

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8. Housing and Community Development Act of 1974, § 105, 42 U.S.C. § 5305 (Supp. V 1975).

9. *Id.* § 5304(a)(6).

10. *Id.* § 5302(a)(4), (6).

11. *Id.* § 5306(b).

12. *Id.* §§ 5306(d)(2), 5306(f)(1)(B).

13. *Id.* §§ 5306(c), 5306(g), 5306(h).

14. *Id.* § 5307.

15. *Id.* § 5304(f).

meeting the stated needs and objectives, where the application does not comply with the requirements of Title I or other applicable law, or where it proposes ineligible activities.<sup>16</sup>

### *Major Concerns About the New Program*

The new funding procedures under the block grant program addressed many of the major problems inherent in the categorical grant approach. By combining flexibility, minimal federal control, and local decisionmaking with an orderly, objective funding process, great strides were made in improving the system of urban aid. Nevertheless, with the perspective of three-years' operation, several major concerns developed: (1) the primary statutory objective that principally addressed the needs of low- and moderate-income persons required strengthening; (2) the statutory formula allocation system for block grant funds was inequitable relative to the needs of older established cities and areas experiencing substantial decline; (3) the range of permissible uses of block grant funds was overly restrictive in the area of economic development; and (4) distressed areas required concentrated assistance for medium and large scale development activities.

### *Low- and Moderate-Income Beneficiaries*

The block grant legislation embodies a major emphasis on providing benefits to low- and moderate-income persons. Nowhere is this more evident than in section 101(c), which states:

The primary objective of this title is the development of viable urban communities, by providing decent housing and a suitable living environment and expanding economic opportunities, *principally for persons of low- and moderate-income.* . . .<sup>17</sup>

Section 101(c) cites eight specific objectives that block grant assistance is directed to support, four of which expressly address low- and moderate-income benefits. Moreover, section 104(b)(2), sometimes referred to as the Maximum Feasible Priority Provision, gives explicit recognition to low- and moderate-income beneficiaries since each applicant, as a condition for funding, must certify that its community development program gives maximum feasible priority to activities that benefit low- and moderate-income families or aid in preventing or eliminating slums and blight.

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16. *Id.* § 5304(c).

17. *Id.* § 5301(c) (emphasis added).

In spite of this emphasis, early indications that benefits to lower-income persons might actually diminish prompted the Department of Housing and Urban Development (HUD) to contract with the Brookings Institution to undertake a research project covering one year of experience under the block grant program. Chapter 8 of the Institution's report, entitled *Who Benefits?*, examined the impact of block grant funds on different income groups, concluding that, for the sample cities as a whole, low- and moderate-income groups emerged as beneficiaries of only fifty-two per cent of the first year block grant allocations.<sup>18</sup> Another determination revealed that "far and away the predominant approach to community development under the block grant program in its first year of operation involved a neighborhood conservation and growth strategy designed primarily to prevent urban blight."<sup>19</sup> Thus, of the three possible certifications for program activities mandated by section 104(b)(2), "aid in the prevention or elimination of slums or blight" clearly predominated.

In addition to the Brookings Institution Monitoring Study, congressional comments, citizens' criticism, and HUD's own evaluation indicated a growing concern that the block grant program failed to accomplish the statute's primary objective. Important management initiatives designed to reorient the program were instituted early in 1977. This effort significantly shifted departmental policy from the initial years of the program, when monitoring policies were primarily concerned with reviewing procedural requirements. For example, although all HUD field offices were advised in May of 1976 that applications must be reviewed to assure that each activity in the applicant's community development program met one of the requirements for eligibility under the three-prong test of section 104(b)(2), judgments could not be made between activities, and no priority was given to the objective of principally benefiting low- and moderate-income persons.

At the outset of this Administration, in April 1977, a major management directive to HUD field staff emphasized the importance of subjecting applications for block grant assistance to a thorough and meaningful review. This review looked beyond conformity with eligibility and technical requirements to the substance of the activities

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18. THE BROOKINGS INSTITUTION, FIRST REPORT ON THE BROOKINGS INSTITUTION MONITORING STUDY OF THE COMMUNITY DEVELOPMENT BLOCK GRANT PROGRAM 308 (1977) [hereinafter referred to as BROOKINGS STUDY].

19. *Id.* at 327.

to ascertain how statutory objectives were served.<sup>20</sup> The instructions provided, for the first time, detailed review criteria to determine whether an activity could principally benefit low- and moderate-income persons.

No requirement was developed, however, mandating the applicability of the principal benefit test to the program as a whole, rather than as a test for funding eligibility pertaining to specific activities, until the publication of proposed regulations by HUD in October 1977. During the period provided for public comment, the authority by which the Department intended to implement such a requirement was questioned, since section 104(b)(2) appeared to give equal status to activities that address problems of slum and blight.

Nevertheless, the regulations promulgated for final effect on March 1, 1978, imposed a program-wide rule emphasizing low- and moderate-income benefit. Under the new regulations an application is presumed to principally benefit low- and moderate-income persons, absent substantial evidence to the contrary, where at least seventy-five per cent of the program funds available during the three-year period covered by the applicant's community development and housing plan will be used for that purpose. All other applications are subject to examination by HUD prior to funding to determine whether they meet the "principal benefit" program requirement.

To further strengthen the Administration's position, subsequent detailed instructions to HUD field offices in April 1978 further stressed that "principal benefit" represented a major policy initiative of the Department, and that the review process should devote particular attention to this aspect of each applicant's proposed community development program.<sup>21</sup>

From the Department's perspective there is no conflict between this policy and either the legislative text or spirit of the 1974 Act or its 1977 Amendments. Neither enactment resolves any statutory inconsistencies on the issue. The regulations promulgated by the Department are consonant with the enabling legislation and its primary objective, and reflect many lessons learned during the first three years of the Block Grant Program. Emphasizing the "principal benefit" objective alone does not disturb section 104(b)(2), since each activity funded under the revised policy must still meet one of that section's three certification categories.

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20. Community Planning and Development Notice No. 77-10 (April, 1977).

21. Community Planning and Development Notice No. 78-9 (April, 1978).

### *Funding Allocations*

A second important development tries to ensure an equitable allocation of the finite grant resources for the Block Grant Program. While the 1974 statutory allocation formula improved the funding system by providing assistance on an annual basis with maximum certainty and minimum delay, upon which communities could rely in their planning, the formula failed to sufficiently target limited federal resources to those localities in greatest need. Studies of the Block Grant Program undertaken by several sources, including HUD and the Brookings Institution, clearly indicated "that the cities with the most severe socioeconomic and fiscal problems tend to receive less funding under the block grant program than under the folded-in grant programs for community development, while better-off cities with brighter fiscal outlooks tend to gain funds."<sup>22</sup> In this connection, HUD evaluation research efforts were directed towards identifying an operational formula that provided greater assistance to entitlement communities having the most pressing community development needs.

The 1977 Amendments included this Administration's proposal to implement a second, alternative formula that would more accurately reflect the needs of older, more deteriorated areas. Under the new dual formula system, a metropolitan city or urban county receives the higher amount computed under one of two formulas: the present formula based upon population, housing overcrowding, and poverty counted twice; or a second formula based upon age of housing counted 2 1/2 times, poverty 1 1/2 times, and growth lag counted once.<sup>23</sup> This second formula is based on the determination that growth lag and age of housing correlate closely with factors of urban distress. The restructured allocation mechanism meets the original objectives of the 1974 Act by utilizing objective needs that reflect physical blight, deterioration, and aged housing stock. Although the revised block grant formula gives more aid to distressed areas than in previous years, no entitlement community will receive less than last year because of increased funding levels.

In addition, the 1977 Amendments reflected a growing awareness of and concern for the community development needs of smaller communities. The Department's experience in funding smaller,

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22. BROOKINGS STUDY, *supra* note 18, at 161.

23. Housing and Community Development Act of 1974, 42 U.S.C. § 5306(b) (Supp. V 1975).



nonentitlement communities during the first three years of the program proved less than satisfactory. The 1977 Amendments provided specific guidelines concerning how the basic discretionary component of the Block Grant Program is to be administered, as well as the factors that determine distribution of these funds. Congress added the option of multiyear funding commitments for "comprehensive" programs to nonentitlement applicants, and shifted from balances for each standard metropolitan statistical area to statewide metropolitan balances that give HUD greater flexibility to encourage larger, more comprehensive grants.<sup>24</sup> The new legislation also mandates that HUD undertake a study of small city community development needs and report to Congress on this subject by October 12, 1978.<sup>25</sup> Work on this study is already well underway.

In response to these legislative changes, and with an increased sensitivity to the nonentitlement constituency, HUD completely revised the regulations governing distribution of these discretionary funds.<sup>26</sup> Now labeled the Small Cities Program, these new rules allow communities to compete for either of two types of grants: Single Purpose grants, designed to meet a specific community development need, or Comprehensive grants for two or more interrelated activities that address a substantial portion of the identifiable community development needs within a defined geographical area. The latter can be awarded for a period of up to three years.

Separate rating systems for the Single Purpose and the Comprehensive grants, while emphasizing national objectives, promote greater local flexibility in the design of programs. Major emphasis is placed on the benefit to low- and moderate-income persons. Single Purpose grants must address such problem areas as housing, economic conditions, or deficiencies in public facilities that affect public health or safety, with a special set-aside available for needs involving an imminent threat to public health or safety. Consistent with congressional intent, the regulations ease application, citizen participation, and Housing Assistance Plan requirements for Single Purpose grants.

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24. Housing and Community Development Act Amendments of 1977, 42 U.S.C.A. § 5306(d)(2), (3) (West Supp. 1978).

25. *Id.* § 5313.

26. 43 Fed. Reg. 8,481(1978).

### *Economic Development Activities*

A third major recent development focuses on a greatly expanded role for economic development under the program. One of the most urgent problems in urban America is a need to create jobs that strengthen local economies. Unemployment exacts a high cost, weakening the national economy, depriving cities of revenues, increasing the need for social welfare services, and draining available public funds.

Early experience with the use of block grant funds for economic development reflected its limited statutory role under the 1974 Act. The only specific statutory reference to economic development in the list of eligible activities dealt with providing "public services," thus imposing major constraints on the availability of that activity.<sup>27</sup> While economic development under the 1974 Act could be undertaken through indirect means, such as land acquisition to eliminate slums and blight that yielded an economic development reuse, absence of a broad approach integrating economic development activities at both the neighborhood and city-wide level impaired the long-term impact of the Block Grant Program on economic problems.

The 1977 Amendment provided significant improvements in this area. The new law shifts economic development from the marginal activity of supportive public services to a wholly separate provision, making eligible a broad range of economic development carried out by public or private nonprofit entities.<sup>28</sup> As part of their economic development strategy, applicants may now use block grant assistance for acquiring real property, for constructing, reconstructing, rehabilitating or installing public facilities and improvements not otherwise eligible, and for commercial or industrial buildings and real property improvements.

Further, the new law and its implementing regulations permit applicants to provide grants directly to neighborhood-based nonprofit organizations, Small Business Investment Companies (SBIC's), and local development corporations for community economic development or neighborhood revitalization projects determined by the applicant as necessary or appropriate to accomplish its community development program.<sup>29</sup> Such activities may include using block

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27. Housing and Community Development Act of 1974, § 105(a), 42 U.S.C. § 5305(a)(8) (Supp. V 1975).

28. Housing and Community Development Act Amendments of 1977, § 105, 42 U.S.C.A. § 5305(a)(14) (West Supp. 1978).

29. *Id.* § 5305(a)(15).

grant funds for assistance through grants, loans, guarantees, interest supplements, or technical assistance to new or existing small businesses, minority businesses and neighborhood nonprofit businesses for working capital or operational funds; capital for land, structures, property improvements, and fixtures; capitalization of an SBIC or local development corporation, where required, for assistance under other federal programs; assistance to minority contractors to obtain performance bonding; and other activities not otherwise excluded that are appropriate for community economic development or neighborhood revitalization if prior authorization is obtained.

Economic development is vitally important to the nation's urban areas, with its potential for attracting industries back to the cities and helping rebuild a stable employment base. The Department views the increased emphasis on economic development, reflected in the 1977 Amendments, as a hopeful sign of a more effective program.

#### *Urban Development Action Grants*

A final legislative change offering great promise is the Urban Development Action Grant program, popularly known as UDAG.<sup>30</sup> UDAG is a creative investment proposal that has the potential to correct many of the imbalances between the cities and the suburbs.

In the past, block grants to severely distressed cities were insufficient to respond to new problems or take advantage of new opportunities. Funding, although adequate to complete limited short-term community development projects, proved insufficient to permit major new undertakings requiring heavy front-end investments.

In response to the need for a source of funds capable of providing substantial additional investment, as well as leveraging significant private investment, the Urban Development Action Grant Program was enacted, authorized at a funding level of \$400 million per year for three years. Conventional HUD approaches to economic development reflected a reluctance to confront the processes that produced urban disinvestment. Thus the 1977 Amendments added, as a specific block grant objective, "the alleviation of physical and economic distress through the stimulation of private investment and community revitalization in areas with population outmigration or a stagnating or declining tax base."<sup>31</sup> Economic development activities, including the Urban Development Action Grant Program, are ele-

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30. *Id.* § 5318.

31. *Id.* § 5301(c)(8).

vated to a specific legislative objective, concomitantly deserving more emphasis than mere activity eligibility.

Both distressed cities and distressed urban counties are eligible recipients of action grant assistance. They are required to develop programs that attract private investment, stimulate investment in restoring deteriorated or abandoned housing stock, or solve critical problems resulting from loss of employment or chronic unemployment in the community. Primary emphasis is placed on revitalizing and conserving viable residential neighborhoods and the stimulation of commercial and industrial development essential to the vitality of central cities and their residential neighborhoods. Projects may be designed to either restore seriously deteriorated neighborhoods, reclaim for industrial purposes under-utilized real property, or renew commercial employment centers. At least twenty-five per cent of the action grants must be made to small cities.

The primary selection criterion mandated by the legislation is the comparative degree of physical and economic distress among applicants, measured by factors that consider the differences in growth lag, the extent of poverty, and the adjusted age of housing in the metropolitan city or urban county. Other factors considered in selecting among applicants include demonstrated performance of the city or urban county in housing and community development programs; impact of the action grant proposal on the special problems of low- and moderate-income persons and minorities; extent of financial participation by other public or by private entities; impact on the physical, fiscal, or economic deterioration of the city or urban county; and feasibility of accomplishing the program in a timely fashion within the grant amount available. Each application must evidence a firm commitment of private resources that have a clear, direct relationship to the activities for which federal funding is being requested.

The first round of action grant approvals is already completed. Forty-five cities were awarded more than \$150 million to carry out fifty separate projects. This infusion of federal funds is supported by \$978.8 million in private commitments, and will assist in creating or saving 43,203 jobs. The awards included such diverse proposals as the "recycling" of the Narragansett Race Track in Pawtucket, Rhode Island, for industry, business, and new housing; a construction loan by the City of Louisville, Kentucky, to renovate an historic hotel with the eventual recapture of the federal funds to aid businesses and increase the housing supply; and a Compton, California, proposal that will establish a joint venture between that city and a firm using

proven modular housing techniques to expand the housing supply, improving the local economic base and increasing employment opportunities for lower-income persons.

Recent experience showed that an influx or reinvestment of private capital in the form of a critical project or set of activities could often change the perception of the private sector regarding the desirability of the investment climate of the city, thus altering the image of decline. When this perception changes, the private sector appears more likely to invest substantial funds in the city rebuilding process without additional public subsidy.

The Urban Development Action Grant Program, with its leveraging requirement, should prove successful in not only attracting private capital but also in stemming urban decline.

#### CONCLUSION

The 1974 Community Development Block Grant legislation represented an important milestone in providing essential changes in the federal mechanism for encouraging and funding local community development efforts. The program simplified a fragmented system of federal assistance by consolidating the major categorical grant programs into a flexible, unified approach, which emphasized minimum application requirements, shortened application processing time, lessened front-end federal review, and established a monitoring control that avoided the restrictiveness of the former programs while still promoting the protection of federal interests in national policy objectives.

Yet inherent inadequacies in the original legislation and the initial administration of the program remain. The 1977 Amendments and HUD management initiatives described above are expected to have a significant impact in improving the effectiveness of the program in developing urban communities into viable economic, political and social entities, providing decent housing and a suitable living environment, and expanding economic opportunities, principally for persons of low- and moderate-income. This mandate, while established by the block grant legislation, also comports with the overall mission of this Department, and presents a worthy and noble challenge in our continuing effort to meet the critical needs of the nation's urban areas.

## **ARTICLES**

