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MOVING THE CDBG PROGRAM FORWARD: A LOOK AT THE ADMINISTRATION'S REFORM PROPOSAL, WHERE DO WE GO FROM HERE?

HEARING

BEFORE THE

SUBCOMMITTEE ON FEDERALISM AND THE CENSUS

OF THE

COMMITTEE ON GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

ONE HUNDRED NINTH CONGRESS

SECOND SESSION

JUNE 27, 2006

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MOVING THE CDBG PROGRAM FORWARD: A LOOK AT THE ADMINISTRATION'S REFORM PROPOSAL, WHERE DO WE GO FROM HERE?

TUESDAY, JUNE 27, 2006

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON FEDERALISM AND THE CENSUS,
COMMITTEE ON GOVERNMENT REFORM,
Washington, DC.

The committee met, pursuant to notice, at 10 a.m., in room 2154, Rayburn House Office Building, Hon. Michael R. Turner (chairman of the subcommittee) presiding.

Present: Representatives Turner, Clay, Dent, and Foxx.

Staff present: John Cuaderes, staff director; Shannon Weinberg, counsel; Juliana French, clerk; Adam Bordes, minority professional staff member; and Jean Gosa, minority assistant clerk.

Mr. TURNER. Good morning. We will call the hearing of the Subcommittee on Federalism and the Census to order. We welcome you to the Subcommittee on federalism and the Census oversight hearing entitled, "Moving the CDBG Program Forward: A Look at the Administration's Reform Proposal, Where Do We Go From Here?" This is a followup to the subcommittee's series of hearings held regarding the Community Development Block Grant [CDBG], program and our committee report on the hearings and the program.

The Community Development Block Grant program [CDBG], is one of the largest Federal direct block grant programs in existence. State and local governments use CDBG grant moneys to fund various housing, community development, neighborhood revitalization, economic development, and public service provision projects. For over 30 years, the CDBG program has been a critical tool in the arsenal of cities to help create livable communities for individuals and families. Without question, the program provides vital funds for addressing poverty as well as community development needs, from eradicating blight to providing building infrastructure.

While CDBG is a valuable tool that enables States and local governments to accomplish many of the objectives outlined in the original authorization, the program exhibits several problems that require remedy. Since 1978, the factors used in calculating poverty and community development need have remained constant while the demographic compositions of the Nation have changed dramatically. In particular, the number of entitlement communities has grown.

In fiscal year 2004, there were more than 1,100 designated entitlement communities. More than 250 new entitlement communities

were certified since 1993 alone as compared to only 128 new entitlement community designations between 1982 and 1993. And while the number of communities sharing the entitlement portion of CDBG funds continues to grow, the overall funding of this program has not kept pace.

Thus, a larger portion of the population is sharing a relatively static portion of CDBG funds, resulting in smaller per capita grants per jurisdiction. At the same time, the number of non-entitlement communities grows smaller, effectively increasing their share of the 30 percent portion of CDBG.

Additional questions of fundamental fairness have arisen in recent years. First, there are instances of "richer" communities receiving higher per capita awards than "poorer" communities. Second, similarly situated communities often get disparate per capita awards.

The subcommittee held five hearings in 2005 examining the CDBG program. Those hearings culminated in an extensive report, which was unanimously voted out of the full committee in December. The report contained numerous findings on the effectiveness of the program and recommendations for improved fairness, efficiency, efficacy, and program administration.

These recommendations were formed with significant government partner and stakeholder input. In particular, the report focused on the growing inequity of the grant formula over time, the subjective nature of the needs index, and the apparent lack of grantee performance measures and related enforcement capability.

In another attempt to address some of these issues, the administration proposed legislation to reform the CDBG program. This proposal, the Community Development Block Grant Reform Act of 2006, chiefly addresses three areas: the grant formula, performance measures, and incentives for quality community development.

First, the act eliminates the two dualities of the grant formula. Currently, grant funds are disbursed to entitlement and non-entitlement communities based on two formulas. By law, the collective pot of CDBG funds must be split between the entitlement and non-entitlement communities 70 percent to 30 percent. Under the CDBG Reform Act, all communities would be treated as "formula grantees" rather than entitlement and non-entitlement communities with separate grant allocation calculations.

Second, the act directs the Secretary to establish new performance measures and grantee accountability standards. The act specifies that State grantees must submit for approval a housing affordability strategy. All other grantees must submit a "Performance Plan," which must include specific performance measure objectives.

The act also directs the Secretary to perform periodic reviews of grantee activity and use of funds. If the Secretary finds grantee performance inadequate, the Secretary may reduce or limit block grant assistance.

Third, the act authorizes $200 million for a new grant program: the Challenge Grant Fund. The Challenge Grant Fund would reward grantees with additional funds to be used "in neighborhood revitalization strategy areas as a targeted strategy for activities eligible under this title that expand economic opportunities." A grantee must demonstrate "measurable progress" toward certain goals

using CDBG funds. Eligible entities will be ranked on their performance and funds awarded accordingly.

We commend the administration for recognizing that CDBG would be most effective remaining at HUD. We also applaud the administration's recognition that, while an important and beneficial program, there is room for improvement within the CDBG program.

At the same time, we are concerned that formula reform is the greatest and most complex of the reform challenges and cannot be undertaken lightly. Additionally, there are a number of non-controversial reforms identified in this committee's CDBG Report that were not mentioned in the administration's reform proposal. We are here today to explore the administration's reform proposal in depth. We hope to discover more about the decisionmaking process and the reasoning behind the choices made in crafting the reform proposal.

To help us with these questions today, we have witnesses from both HUD and GAO. We welcome the Honorable Pamela Hughes Patenaude, Assistant Secretary of the Office of Community Planning and Development at the U.S. Department of Housing and Urban Development; Stanley J. Czerwinski, Director of Intergovernmental Relations for Strategic Issues at the U.S. Government Accountability Office; and Michael Springer, Assistant Director of Strategic Issues at the U.S. Government Accountability Office.

I look forward to your expert testimony and I thank you all for your time. I believe Mr. Clay has an opening statement which we can give him an opportunity to provide us as the hearing progresses.

[The prepared statement of Hon. Michael R. Turner follows:]

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SUBCOMMITTEE ON FEDERALISM AND THE CENSUS
Congressman Michael R. Turner, Chairman

OVERSIGHT HEARING
STATEMENT BY MICHAEL R. TURNER, CHAIRMAN

Hearing Topic: *"Moving the CDBG Program Forward: A Look at the Administration's Reform Proposal. Where Do We Go From Here?"*

10:00 a.m., Tuesday, June 27, 2006
Room 2154 Rayburn House Office Building

OPENING STATEMENT

Welcome to the Subcommittee on Federalism and the Census' oversight hearing entitled "*Moving the CDBG Program Forward: A Look at the Administration's Reform Proposal. Where Do We Go From Here?*" This is a follow up to the Subcommittee's series of hearings held regarding the Community Development Block Grant (CDBG) program and our Committee Report on the hearings and the program.[1]

The Community Development Block Grant program, or CDBG, is one of the largest federal direct block grant programs in existence. State and local governments use CDBG grant moneys to fund various housing, community development, neighborhood revitalization, economic development, and public service provision projects. For over thirty years, the CDBG Program has been a critical tool in the arsenal of cities to help create livable communities for individuals and families. Without question, the program provides vital funds for addressing poverty as well as community development needs, from eradicating blight to providing building infrastructure.

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[1] BRINGING COMMUNITIES INTO THE 21ST CENTURY: A REPORT ON IMPROVING THE COMMUNITY DEVELOPMENT BLOCK GRANT PROGRAM (Report 109-365).

While CDBG is a valuable tool that enables States and local governments to accomplish many of the objectives outlined in the original authorization, the program exhibits several problems that require remedy.

Since 1978, the factors used in calculating poverty and community development need have remained constant while the demographic composition of the nation has changed dramatically. In particular, the number of entitlement communities has grown. In FY2004, there were more than 1,100 designated entitlement communities – more than 250 new entitlement communities were certified since 1993 alone as compared to only 128 new entitlement community designations between 1982 and 1993. And while the number of communities sharing the entitlement portion of CDBG funds continues to grow, the overall funding of the program has not kept pace. Thus, a larger portion of the population is sharing a relatively static portion of CDBG funds, resulting in smaller per capita grants per jurisdiction. At the same time, the number of non-entitlement communities grows smaller, effectively increasing their share of the 30 percent portion of CDBG.

Additional questions of fundamental fairness have arisen in recent years. First, there are instances of "richer" communities receiving higher per capita awards than "poorer" communities. Second, similarly situated communities often get disparate per capita awards.

The Subcommittee held five hearings in 2005 examining the CDBG program. Those hearings culminated in an extensive report, which was unanimously voted out of the full Committee in December. The report contained numerous findings on the effectiveness of the program and recommendations for improved fairness, efficiency, efficacy, and program administration.

These recommendations were formed with significant government partner and stakeholder input. In particular, the report focused on the growing inequity of the grant formula over time, the subjective nature of the needs index, and the apparent lack of grantee performance measures and related enforcement capability

In another attempt to address some of these issues, the Administration proposed legislation to reform the CDBG program. This proposal, the Community Development Block Grant Reform Act of 2006, chiefly addresses three areas: the grant formula, performance measures, and incentives for quality community development.

First, the Act eliminates the two dualities of the grant formula. Currently, grant funds are disbursed to entitlement and nonentitlement communities based on two formulas. By law, the collective pot of CDBG funds must be split between the entitlement and nonentitlement communities 70 percent to 30 percent. Under the CDBG Reform Act, all communities would be treated as "formula grantees" rather than entitlement and nonentitlement communities with separate grant allocation calculations.

Second, the Act directs the Secretary to establish new performance measures and grantee accountability standards. The Act specifics that State grantees must submit for a approval a housing-affordability strategy. All other grantees must submit a "Performance Plan," which must include specific performance measure objectives. The Act also directs the Secretary to perform periodic reviews of grantee activity and use of funds. If the Secretary finds grantee performance inadequate, the Secretary may reduce or limit block grant assistance.

Third, the Act authorizes $200,000,000 for a new grant program – the Challenge Grant Fund. The Challenge Grant Fund would reward grantees with additional funds to be used "in neighborhood revitalization strategy areas as a targeted strategy for activities eligible under this title that expand economic opportunities."

A grantee must demonstrate "measurable progress" toward certain goals using CDBG funds. Eligible entities will be ranked on their performance and funds awarded accordingly.

We commend the Administration for recognizing that CDBG would be most effective remaining at HUD. We also applaud the Administration's recognition that, while an important and beneficial program, there is room for improvement within the CDBG program. At the same time, we are concerned that formula reform is the greatest and most complex of the reform challenges and cannot be undertaken lightly. Additionally, there are a number of non-controversial reforms identified in the Committee's CDBG Report that were not mentioned in the Administration's reform proposal. We are here today to explore the Administration's reform proposal in depth. We hope to discover more about the decision-making process and the reasoning behind the choices made in crafting the reform proposal.

To help us with these questions today, we have witnesses from both HUD and GAO. We welcome the Honorable Pamela Hughes Patenaude, Assistant Secretary of the Office of Community Planning and Development at the U.S. Department of Housing and Urban Development; Stanley J. Czerwinski, Director of Intergovernmental Relations for Strategic Issues at the U.S. Government Accountability Office; and Michael Springer, Assistant Director of Strategic Issues at the U.S. Government Accountability Office.

I look forward to the expert testimony we will receive today from both HUD and GAO. Thank you all for your time today and welcome.

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Mr. TURNER. We will begin with our witnesses. As it is the policy of this committee, we do swear in all of our witnesses. I would ask if you would please stand and raise your right hands.

[Witnesses sworn.]

Mr. TURNER. Please note that all the witnesses have responded in the affirmative by saying I do. And we note that two additional witnesses from HUD have also been sworn in who have not been identified in our list but who might be called on by the Secretary.

We will now start with the witnesses. Each witness has kindly prepared written testimony which will be included in the record of this hearing. Each witness has also prepared an oral statement summarizing their written testimony.

Witnesses will notice there is a timer with a light on the witness table. In order to be sensitive to everyone's time, we ask that witnesses cooperate with us in adhering to the 5-minute time allowance for their oral presentation. The green light indicates that you should begin your remarks and the red light indicates that your time has expired. The yellow light indicates that you have 1 minute to conclude, and we will follow that with a question and answer period.

We begin with the Honorable Pamela Hughes Patenaude.

STATEMENTS OF PAMELA HUGHES PATENAUDE, ASSISTANT SECRETARY, OFFICE OF COMMUNITY PLANNING AND DEVELOPMENT, U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT; STANLEY J. CZERWINSKI, DIRECTOR, INTERGOVERNMENTAL RELATIONS, STRATEGIC ISSUES, U.S. GOVERNMENT ACCOUNTABILITY OFFICE; AND MICHAEL SPRINGER, ASSISTANT DIRECTOR, STRATEGIC ISSUES, U.S. GOVERNMENT ACCOUNTABILITY OFFICE

STATEMENT OF PAMELA HUGHES PATENAUDE

Ms. PATENAUDE. Thank you, Mr. Chairman. I am pleased to be here today on behalf of Secretary Jackson to discuss the administration's proposal to reform the Community Development Block Grant program.

The President's fiscal year 2007 budget retains and consolidates the CDBG program at HUD. We have proposed the reform because the program's intended purpose to the Nation's neediest communities has decreased over time. Quite simply, the current formula that allocates billions of dollars is no longer as fair as it used to be.

Over the past three decades, demographic and socioeconomic changes, development patterns and other factors have created significant distortions in the distribution of CDBG funds. There has been a steady erosion in the ability of the formula to target funding to places with the greatest needs.

The CDBG formula has been untouched since the 1970's. Reform is also necessary because HUD must be able to hold grantees accountable for performance and provide incentives to maximize the impact of these limited and valuable funds. To address these issues, the administration proposes the CDBG Reform Act of 2006. The three main elements of the act are formula reform, the intro-

duction of a challenge grant and enhanced performance measurement requirements.

To explain further, Mr. Chairman, I call your attention to the first chart displayed on the screen. Chart One illustrates the current formula. These vertical jagged lines represent the 1,100 entitlement communities and their per capita grant. The solid line from the lower left to the upper right is the measuring stick that represents the community development needs index.

The least needy communities are shown on the left and the ones with the most needs on the right. As you can see on the right, under the current formula, many high need communities are receiving amounts far below their needs index. The biggest problem with the current formula is that grantees with similar needs are receiving significantly different per capita amounts. Based on the needs index, these grantees should be receiving roughly the same per capital amount.

Next slide, please. Chart Two shows a more equitable distribution of the Community Development Block Grant funds under the new or proposed formula. It demonstrates the ability of the new formula to more fairly target funds to communities with greater needs.

Next slide, please. And finally, Chart Three provides an overlay of the current formula with the proposed formula to demonstrate how we intend to allocate grants in a way that more fairly ensures funding to places that need it most.

Grantees with similar need profiles will receive a more equitable amount per capital and most importantly, the proposed formula will ensure funding to the most needy communities. The second element of the CDBG Reform Act of 2006 is the introduction of a $200 million competitive CDBG challenge grant. This fund would give communities the opportunity to compete for additional funding to carry out economic development revitalization in distressed neighborhoods.

In order to be considered for the challenge grant, distressed entitlement communities are required to have both a strategy and a track record of concentrating investment in distressed neighborhoods. Communities are selected based on objective criteria, including the extent to which they target their assistance to distressed neighborhoods and expand economic opportunities for lower income households. HUD will award challenge grants to communities that achieve the greatest results in their neighborhood revitalization strategies.

The third element of CDBG reform is to strengthen performance measurement requirements to improve the effectiveness and viability of the program. HUD is currently implementing a new framework that clearly establishes measurable goals. The CDBG Reform Act will give HUD the authority to hold grantees accountable.

CDBG has helped communities across the Nation address a variety of community and economic development needs. Reforms are necessary to ensure the program's continued ability to improve the lives of low and moderate income Americans.

Thank you, Mr. Chairman, for the opportunity to discuss a proposal on CDBG reform.

[The prepared statement of Ms. Patenaude follows:]

WRITTEN STATEMENT OF
ASSISTANT SECRETARY PAMELA H. PATENAUDE
U.S DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

HEARING ON THE CDBG REFORM ACT OF 2006

BEFORE THE

SUBCOMMITTEE ON FEDERALISM AND THE CENSUS

COMMITTEE ON GOVERNMENT REFORM

UNITED STATES HOUSE OF REPRESENTATIVES

WASHINGTON, DC

JUNE 27, 2006

Thank you, Mr. Chairman. I am pleased to be here today, on behalf of Secretary Jackson, to discuss the Administration's proposal to reform the Community Development Block Grant program.

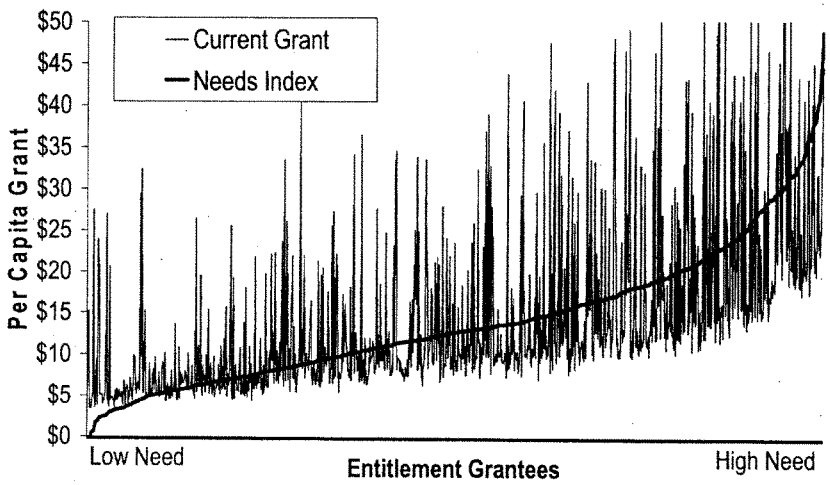
The President's Fiscal Year 2007 Budget retains the CDBG program at HUD. We have proposed the reform because the program's intended impact to the nation's neediest communities has decreased over time. The CDBG formula has been untouched since the 1970's. Since then, we have witnessed steady erosion in the ability of the formula to target funding to cities with the greatest community and economic development needs. Demographic and socio-economic changes, development patterns, and other factors have created significant distortions in the distribution of CDBG funds. In addition to addressing problems with the formula, HUD must be able to hold grantees accountable for performance and provide incentives to maximize the impact of these limited and valuable funds.

To address these issues, the Administration proposes the CDBG Reform Act of 2006. The three main elements of the Act are formula reform, a 200 million dollar Challenge Grant, and enhanced performance measurement requirements.

The chart below illustrates the basic problems with the existing CDBG formula.

Chart One

Current Entitlement Formula – Targeting to the Needs Index



Let me explain what the chart illustrates. The least needy grantees are shown on the left and the most needy on the right. The solid line sloping upward from the lower left to the upper right represents the community development needs index developed by HUD's Office of Policy Development and Research. The index is a measure of needs against which the current formula is evaluated. The jagged line represents the per capita grant of each grantee under the current formula. In the lower left corner, we see low need grantees receiving a high amount of funds relative to the needs index. The right side of the chart shows high need grantees receiving amounts below the amount indicated by the needs index and, in some cases, less than the amounts provided to low need grantees. For example, Newton, Massachusetts, a low-need suburb of Boston, gets the same $24 per capita as Lawrence, Massachusetts, a high need community.

The biggest problem with the current formula is that grantees with similar needs are receiving significantly different per capita amounts. Based on the needs index, these grantees should be receiving roughly the same per capita amount. For example, St. Louis, Detroit, and Miami are all distressed cities and have similar overall needs according to HUD's needs index. Yet under the current formula, St. Louis receives $59 per capita; Detroit receives $43 per capita; and Miami receives $22 per capita. Over the past three decades, per capita grant amounts to the neediest grantees have been declining.

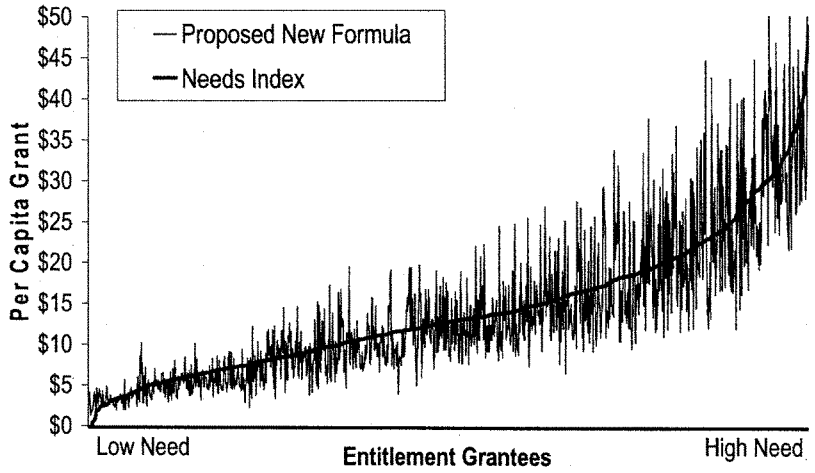
The formula proposed in the CDBG Reform Act is based on Alternative 4 from the HUD study released in February 2005 that was provided to Members of Congress. This single formula approach will apply to all grantees and eliminates the existing structure of dual formulas and the 70/30 split between entitlement and state grantees. A common set of factors that reflects community distress and fiscal capacity will be used. These are:

- Persons in poverty excluding full-time college students,
- Housing units over 50 years old and occupied by a poverty household,
- Female headed households with children under 18,
- Housing overcrowding and
- Fiscal capacity.

The second chart shows a more equitable distribution of CDBG funds under the proposed formula. It demonstrates the ability of the new formula to target funds to grantees with greater community development needs.

Chart Two

CDBG Reform Act Formula Proposal – Targeting to the Needs Index



By comparing charts 1 and 2, you can see the improved targeting that would occur. Low need grantees, shown on the left side of the chart, would no longer receive large per capita amounts. Previously underfunded high need grantees would generally experience increases in their grant amounts. Grantees with similar need profiles would receive more equal per capita grant amounts. The new formula will distribute more funds to the most needy grantees.

The CDBG Reform Act also contains a proposal to establish a minimum grant size. Communities that do not meet the threshold would be eligible to receive funding through a State or urban county program.

The second element of the CDBG Reform Act of 2006 is a 200 million dollar CDBG Challenge Grant. This fund would permit grantees to compete for additional funding to carry out community and economic development revitalization to improve the quality of life in distressed neighborhoods.

In order to be considered for the Challenge Grant, entitlement communities will be required to have both a strategy and a track record of concentrating investment in distressed neighborhoods. Communities will be selected based on objective criteria including the extent to which communities concentrate their assistance to distressed

neighborhoods and expand economic opportunities for lower income households, and the viability of target neighborhoods. This will be reflected in per capita expenditures in distressed areas, improvements in employment, income levels, housing affordability, and homeownership. HUD would award Challenge Grants to communities that achieve the greatest results in their neighborhood revitalization strategies.

The third element enhances performance measurement requirements to improve the effectiveness and viability of the program. HUD is currently implementing its new performance measurement and accountability framework establishing clear, measurable goals, as well as community progress indicators. While implementation of this framework is a significant step forward, HUD must have the tools necessary to hold grantees accountable for achieving their goals. The CDBG Reform Act would give HUD the authority to hold grantees accountable.

Consistent with the Administration's goal of reforming community and economic development programs, first proposed through the Strengthening America's Communities Initiative last year, we have introduced these reforms.

CDBG has helped communities across the nation address a variety of community and economic development needs. Reforms are necessary to ensure the program's continued ability to improve the lives of low- and moderate-income Americans. The CDBG Reform Act of 2006 reaffirms the national objectives of the program. By revising the formula, adding a competitive Challenge Grant, and implementing the performance measurement framework, we will improve the effectiveness of the CDBG program.

Thank you for this opportunity to discuss the Administration's proposal on CDBG reform.

Mr. TURNER. Mr. Czerwinski.

STATEMENT OF STANLEY J. CZERWINSKI

Mr. CZERWINSKI. Mr. Chairman, Mr. Clay, thank you for the opportunity to be here to speak today about the administration's reform proposal.

As you noted, Mr. Chairman, about 30 years of CDBG have resulted in many valuable things happening in this country. We see communities revitalized, we see living conditions improved. The committee's examination today is very timely for several reasons. First of all, as you know, we are facing a long-term fiscal crisis characterized by growing deficits. Second, as you noted, Mr. Chair, the economics and demographics of the country have changed significantly since the program began in the 1970's.

And third, as you also know, Mr. Chairman, there has been a continuous decline in funding for CDBG. For example, today the per capita funding of the program is one-quarter what it was at its inception. Our view is the best way to save this program is to improve its targeting. In that view, Mr. Chairman, the administration's proposal is a step in the right direction. However, it is not a final step. More needs to be done.

Today I would like to speak about two things. First of all, to give you a quick reaction to the administration's proposal, and second, I would like to discuss the work that we are undertaking at the subcommittee's request. As you mentioned, last month the administration unveiled its latest proposal to reform the CDBG program. I will not summarize the proposal, because Ms. Patenaude has already done an excellent job of that.

However, what I would like to do is share some observations. First of all, the single formula that the administration proposes is a significant step forward. It represents better targeting. For about 25 years, GAO has been noting problems with this area, and this is the kind of problem that you noted in your opening statement, Mr. Chairman, with sometimes communities that are more well off actually get more benefits than those that are less well off.

The variables in the single formula that the administration proposes also represent improvement but they do raise some concerns. Most significant is the inclusion of a cost of living adjustment. Right now, CDBG is disbursed without regard to how expensive it is to live in an area. We support HUD's attempt to adjust for cost of living. However, we are concerned with the way that HUD goes about it. Because there may be some unintended consequences. The proposal that HUD has would take the cost of living for a community and compare it to the cost of living for its neighbors. By doing such, you run the risk of penalizing those communities with poor neighbors while rewarding those with rich neighbors. For these reasons, we will be evaluating both how the cost of living assessment is going to be made and other different measures of the cost of living as we do the work for you.

I would now like to briefly describe the work that we are undertaking at the committee's request. There are three primary tasks that GAO will be undertaking. First, as I mentioned, an alternative measure of need. Second is looking at the feasibility of measuring capacity of local communities. Right now, as you know, CDBG is

allocated according to need only. It does not take into account the capacity of the communities. This can have some distorting effects.

For example, those communities that have a strong local capacity may be able to address some of their needs on their own, while those with weaker capacity may have a greater need for Federal help, and the current formula does not do that.

Finally, as you requested, what we will come up with are options on the various formula decisions the committee will face. As you requested, we will not be making recommendations, because frankly, that is the prerogative of Congress. As everyone knows, this is a very technically demanding and sensitive area. We are just beginning our work. I estimate that it will take us about a year to complete that work.

Before closing, I would like to highlight two things that we will be doing in that work. First of all, GAO has contracted with the National Academies of Sciences to provide the technical expertise, statisticians, economists and those with local government experience, i.e., hands-on understanding of the program. We expect these expert panels to help us come up with ideas on variables to include the formulas, how to evaluate those variables, and finally, to study the implications of different formula options.

Second, and this may seem like a small point, but I actually think it is an important one, is we will be working closely with representatives of State and local recipients. They are the ones most affected by the program and any changes to the program. We have already begun a dialog with representatives, and in fact, I see some of them in the room behind me today. We will continue that dialog throughout.

Finally, HUD has already been very cooperative and very helpful with us as we have done our work. I would like to thank them for their assistance, and we will continue to engage with them as the work progresses.

In closing, we support the committee's efforts to better target CDBG. We stand by to help the committee as it does its work. Frankly, this is probably the only way that we will preserve a very valuable program, that is by better targeting to those who need it the most.

That concludes my statement, Mr. Chairman. I will be glad to respond to questions that you may have.

[The prepared statement of Mr. Czerwinski follows:]

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Testimony

Before the Subcommittee on Federalism and the Census, Committee on Government Reform, House of Representatives

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COMMUNITY DEVELOPMENT BLOCK GRANT FORMULA

Options for Improving the Targeting of Funds

Statement of Stanley J. Czerwinski,
Director, Strategic Issues

GAO-06-904T

June 27, 2006

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Highlights

Highlights of GAO-06-904T, a testimony before the House Committee on Government Reform, Subcommittee on Federalism and the Census

COMMUNITY DEVELOPMENT BLOCK GRANT FORMULA

Options for Improving the Targeting of Funds

Why GAO Did This Study

The subcommittee asked GAO to testify at this hearing whose purpose is to examine the Community Development Block Grant (CDBG) Program administered by the Department of Housing and Urban Development (HUD) and the Administration's proposal to reform this federal government program. This proposal would use a single formula and five variables to allocate funds. This hearing is a follow-up to a series of subcommittee hearings that GAO participated in during 2005 on the CDBG program. Based on the principles of formula design that GAO outlined in its 2005 testimony, the subcommittee had requested GAO to undertake a body of work to help the Congress explore alternative formulas to allocate CDBG funds among the nation's diverse communities. This work is underway. In this hearing, GAO addresses its ongoing work on options for improving the targeting of CDBG funding as contributions to these efforts and to determining next steps.

What GAO Found

The CDBG is a significant direct federal-to-local grant program, supporting a wide range of local community development activities that benefit low- and moderate-income people. Since its inception in 1974, the program has provided about $113 billion to help the nation's communities focus on challenges ranging from reducing economic isolation to the elimination of neighborhood blight.

Due to the long-term fiscal crisis the nation currently faces, GAO advocates a thorough assessment of all federal tax and spending programs and policies across the board. In particular, GAO has suggested that programs such as the CDBG be measured according to the degree to which assistance is targeted to those with the greatest needs and the least capacity to meet them.

Since 1978, real per capita spending for the CDBG has declined by almost three-quarters from about $48 to about $13 per person. Limited resources coupled with increasing concerns with effectiveness require better targeting to high-need communities. This involves a new look at the way the CDBG program assesses community needs and the capacity to meet those needs.

The significant economic and demographic changes that have occurred over the last three decades make this reassessment especially important. Not only have the economy and population changed, but we have a better understanding of community problems like concentrated poverty. In light of such change, the Administration introduced its latest CDBG reform proposal which would use a single formula and five variables to allocate funds. The Administration's proposal raises important issues regarding how to systematically allocate funds based on community need.

In ongoing work for this subcommittee, GAO is looking at additional options for the CDBG formula, focusing on 1) refining a set of indicators of the development needs facing the nation's communities, 2) assessing potential indicators of communities' capacities to address those needs on the basis of their own fiscal and economic resources, and 3) exploring ways to adjust such indicators for local cost-of-living differences. The objective is to design a set of options to assist the Congress in addressing critical policy choices in choosing a formula to allocate CDBG funds.

www.gao.gov/cgi-bin/getrpt?GAO-06-904T.

To view the full product, including the scope and methodology, click on the link above. For more information, contact Stanley Czerwinski at (202) 512-6806 or czerwinskis@gao.gov.

Mr. Chairman and Members of the Subcommittee:

I am pleased to be here today to discuss our ongoing work on options for improving the targeting of Community Development Block Grant (CDBG) funds as the subcommittee examines the CDBG program and the Administration's proposed reforms. CDBG is a significant direct federal-to-local grant program, supporting a wide array of local community development activities that benefit low- and moderate-income people. Since its inception in 1974, the program has provided about $113 billion, according to the Department of Housing and Urban Development (HUD), to help the nation's communities focus on challenges ranging from reducing economic isolation to the elimination of neighborhood blight. To do this, HUD is required to use a complex dual formula system to allocate CDBG funding. Under this dual formula approach, grants are calculated under two different formulas and grantees receive the larger of the two amounts. The formulas take into account poverty, older housing, population, housing overcrowding, and other factors.

Much has transpired over the past three decades and it is time to carefully consider whether the program's funds are directed towards those communities with the most compelling needs and the least capacity to address them from their own resources. As you have asked us, we have begun a body of work to help the Congress explore alternative formulas to allocate CDBG funds among the nation's diverse communities.

21st Century Challenges Drive Need for CDBG Formula Reassessment

As discussed in our 2005 report on 21st Century Challenges,[1] the federal government's financial condition and long-term fiscal outlook present enormous challenges to the nation's ability to respond to emerging forces reshaping American society. Given the size of our projected deficits, traditional incremental approaches to budgeting will need to give way to more fundamental and periodic reexaminations of existing spending and revenue policies and programs. A periodic reexamination offers the prospect of addressing emerging needs by weeding out programs and policies that are outdated or ineffective and updating those policies and programs that remain relevant by improving their targeting and efficiency. For example, programs such as the CDBG should be judged according to whether they target assistance to those with the greatest needs and the

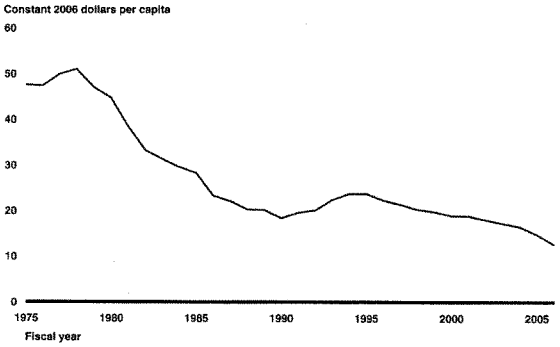
[1]GAO, *21st Century Challenges: Reexamining the Base of the Federal Government*, GAO-05-325SP (Washington, D.C.: February 2005).

least capacity to meet them. While prompted by fiscal necessity, such a fundamental review also provides an opportunity to address the role and responsibility of the federal government in responding to challenges faced by communities throughout the nation. The Administration's proposal to restructure assistance for community development opens up important issues regarding systematically allocating funds based on community need.

Budget Resource Trends Underscore Need for More Effective Targeting of Available Funding

Since 1978, real per capita funding for the CDBG has declined by almost three-quarters from about $48 to about $13 per capita. (See fig. 1.)

Figure 1: Trends in CDBG Funding Per Capita 1975-2006



Source: GAO analysis of Census, HUD, and OMB data.

The number of communities receiving funds directly from the federal government through the CDBG formula grant has nearly doubled from 606 in fiscal year 1975 to 1,128 in fiscal year 2006. This trend can be expected to continue both because population will continue to grow and because new standards for designating metropolitan areas, as promulgated by the Office of Management and Budget and used by the program, are also likely to increase the number of eligible communities. In addition, provisions in the current formula allow communities to continue to receive funds even if they lose their eligibility.

The policy implications of these trends are that with more limited resources, increases in concerns with effectiveness require better targeting to high-need communities. This involves a new look at the program's uses and the way it assesses community needs and capacity to meet those needs. Given these implications, you have asked us 1) to review the use of CDBG funds and how HUD oversees the CDBG program and 2) to assess alternative formulas to allocate CDBG funds among localities, including evaluating formula options that take into account both community development needs and localities' abilities to fund their needs from local resources. In response to your first request, we will be issuing a report to you later this summer which will examine the uses and oversight of CDBG funds. Our work on your second request, which I will be discussing today, will focus on developing various formula options and highlighting the key policy choices that the Congress will have to make when selecting from among those options.

Changing Circumstances Call for CDBG Formula Reassessment

The CDBG program was originally designed to address the pressing urban problems the nation faced in the mid-1970s. However, as HUD has rightly noted, the formula for allocating CDBG funds is today no longer as good a measure as it once was of communities' needs. For example, the amount of pre-1940s housing no longer works very well as a proxy for community development need. Communities that embraced urban renewal and tore down their blighted housing—a statutory goal of CDBG—are penalized, while cities with older rehabilitated housing occupied by higher income families are rewarded.

At the same time, since the inception of CDBG in 1974, the understanding of the underlying problems facing the nation's communities has expanded.[2] For example, we have become more aware of the adverse consequences of geographic concentrations of very low-income households and the negative effects of growing up in a single parent household regardless of income. This greater awareness has led to a variety of federal programs such as HUD's "Moving to Opportunity" initiative, which allows low-income households to move out of areas of concentrated poverty, and a variety of efforts to keep nonresident fathers involved in their children's lives. It is now time to use the knowledge we have gained to reassess the CDBG program.

[2]See, for example, HUD's series of five studies on the CDBG program from 1976 through 2005.

Administration Proposes to Reform the CDBG Program

HUD is required to use a complex dual formula system to allocate CDBG funding.[3] Under this dual formula approach, grants are calculated under two different formulas and grantees receive the larger of the two amounts. The existing approach takes into account poverty, older housing, population, housing overcrowding, and other factors. However, it provides widely differing payments to recipients with similar needs and funds going to the neediest communities have decreased over time on a per capita basis.

In recognition of the significant and dynamic demographic and socioeconomic changes the country has undergone since the mid-1970s, on May 25, 2006, the Administration introduced its latest proposal to reform the CDBG program. At the heart of the Administration's proposal is the use of a single formula. This proposed formula would use five variables to allocate funds:

- the per capita income (PCI) of the community relative to the PCI of its metropolitan area;
- the number of overcrowded housing units;
- the number of households living in poverty, excluding full-time dependent college students;
- the number of female heads of households with minor children; and
- the number of homes 50 years or older occupied by a low-income family.

Because we have not yet reviewed HUD's proposal in detail, we cannot comment on it as a whole at this time. However, we do have some observations on some of the variables that HUD has included. Although we recognize the potential value of introducing a relative PCI variable as HUD has done, we are concerned about HUD's decision to use metropolitan PCI. For example, if there were two identical communities located in different metropolitan areas, the community in a metropolitan area with a lower PCI would receive less aid than the community in a metropolitan area with a higher PCI. In another case, HUD's continued use of overcrowded housing, one of the variables included in the current formula, may be more indicative of a strong local economy that reflects strong demand pressures in the local housing market than it is indicative of economic decline. Nevertheless, HUD's proposal certainly represents a

[3] 42 U.S.C. §5306.

significant contribution to serious discussions of options for allocating CDBG funds.

GAO Is Assessing Additional Options to Improve Targeting under the CDBG Formula

In response to your request that we assess alternative formulas to allocate CDBG funds among localities, it is our intent to build on the foundation created by HUD's work. Our ongoing work is focusing on 1) refining a set of indicators of community development need among the nation's communities, 2) assessing potential indicators of the capacities of communities to address those needs on the basis of their own fiscal and economic resources, and 3) exploring ways to adjust such indicators for local cost-of-living differences. Designing formulas to allocate CDBG funds among the nation's communities involves more than technical issues. It also involves difficult policy choices which are most appropriately the province of the Congress. Our objective is to design a set of formula options that will assist the Congress in making the critical policy choices inherent in choosing a formula to allocate CDBG funds.

In our work to refine indicators to more accurately capture key aspects of community need, we intend to take a fresh look at indicators that are being used in the current formula and those in the Administration's proposal as well as to explore the use of some new need indicators. Next, we will consider whether a CDBG allocation formula can be designed to reflect variations in local funding capacity in order to address local community development needs with local resources. This is because high-income communities generally have stronger tax bases from which to fund program needs without relying on federal assistance than lower-income areas do. Additionally, we plan to explore options for making cost-of-living adjustments within the formula, such as size of population in poverty based on poverty thresholds adjusted for variations in the cost of living. One area we intend to look at for arriving at a cost-of-living factor is the use of fair market rents.

In our analysis, we will use statistical techniques to calculate and weight the relative influence of the indicators, identifying a set of them that effectively represents community development need. Additionally, we will consider potential indicators of the ability of CDBG grantees to address their community development needs from their own resources. We will use the findings from these analyses to develop formula alternatives that link closely to need, incorporating appropriate variables and weights. For the formula options that we develop, we will highlight the key policy choices inherent in selecting a formula to allocate CDBG funds.

Fully recognizing the complexity and controversial nature of the work that lies ahead of us, we are reaching out widely for input and ideas. First, the National Academies of Science are assembling a panel of experts to provide input throughout our project on all phases of our work. The Academies are seeking individuals with both high levels of technical expertise and practical experience regarding community development in local communities. Next, we are working and will continue to work closely with representatives from national organizations of state and local governments and community development associations to obtain their uniquely related perspectives and to identify the concerns of those most responsible for making the CDBG program work. And lastly, but no less importantly, HUD staff have been generous in sharing their considerable expertise and knowledge with us on the CDBG formula and the work they have done. We will continue to consult and discuss technical issues with them.

Concluding Remarks

As we work through the ways that formula options could be shaped, the critical policy choices that will have to be made are most appropriately in the hands of the Congress. Our goal is to provide the necessary information and analyses so that the Congress can systematically examine the implications and make informed choices.

In closing, I would like to emphasize that the targeting issues raised by HUD's proposal are important no matter what level of financial support the Congress provides for community development activities. Additional formula options do need to be explored as part of the process of reaching a decision on how best to target CDBG funding, and we plan to continue to participate in that process with our work for you. Central to any reexamination is assessing how to better target federal assistance to those with the greatest needs and the least capacity to meet those needs.

Mr. Chairman, this concludes my statement. I would be happy to answer any questions you or other members of the subcommittee may have.

For future comments or questions regarding this testimony, please contact Stanley J. Czerwinski at (202) 512-6806. Individuals making key contributions to this testimony included Michael Springer, Joyce D. Corry, Katherine Wulff, Sara Williams, Anna Maria Ortiz, Jerry C. Fastrup, and Bob Dinkelmeyer.

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Mr. TURNER. Mr. Springer.

Mr. SPRINGER. I have no testimony.

Mr. TURNER. Well, first, thank you so much for your participation today and for your preparation. This has been a topic throughout community development groups and organizations, as the administration has begun the process of identifying CDBG as a program that needs reform. And then the discussion as to how that reform should take place.

As I stated in my opening statement, this act that would reform CDBG but would retain it at HUD is certainly an improvement over what we faced with the Strengthening America's Communities initiative that would have dismantled the CDBG program and taken it to Commerce. This is at least a reflection of HUD's expertise.

Obviously, this is just an initial hearing to begin the discussion and the review of the act that is proposed. There are a number of factors and impacts that will have to be reviewed and the communities that are affected will have to study its impacts and weigh in as to the benefits or lack of benefits or negative impacts of this act.

So today, it is not our attempt to go exhaustively into each of the aspects of this, but we are going to have to start, obviously, from some of the discussion that began from the administration in targeting CDBG as a reformed program. In our first hearing on CDBG reform, it was noted that the administration had targeted CDBG as a program that needed reform, as a result of the PART analysis that the administration undertakes in determining whether or not a program is working.

The PART analysis that was applied to CDBG had this first assessment, and the question was under the PART performance measurements used by the administration for evaluating programs, is this program purpose clear. The sentence that follows says, the program does not have a clear and unambiguous mission. Both the definition of community development and the role CDBG plays in that field are not well defined.

Ms. Patenaude, the first thing that I would like to start with of course is, the administration has now, through HUD, proposed this act, in part to address the lack of performance that is identified in part. And in looking at the act, I note that it would now provide to recipients of funds, to formula grantees, performance measures objectives. And the first one is, foster a suitable living environment within the community for families and individuals.

Could you please tell me how that is defined within the act and how that might fare under a PART analysis?

Ms. PATENAUDE. If I may, Mr. Chairman, start with the PART analysis. We obviously have taken OMB's recommendation seriously, and have been addressing the PART score for more than 2 years. We don't completely agree, because we think the statute is clear and that the program is not ambiguous.

The performance measurement framework is an attempt to capture the outcomes. Obviously there is a tremendous amount of flexibility with the program. There are numerous eligible activities with the CDBG program, so these categories were designed to capture activities and outcomes that are certainly in accordance with the statute and the purpose of the program.

Mr. TURNER. As a measurable outcome, how are you going to measure delivering a suitable living environment within the community?

Ms. PATENAUDE. We will measure indicators in neighborhoods' improvements.

Mr. TURNER. Such as?

Ms. PATENAUDE. Employment, reduced crime rate, the affordability of housing, jobs created.

Mr. TURNER. Turning to the chart that you provided us, you have the graph of the needs index and then the entitlement grantees and the disparity, if you will, between the different amounts that communities receive. In the initial HUD review of the grant formulas, there were four different alternative formulas that were presented before this committee last year. The proposal that we have before us appears to more closely relate to alternative four. Would you please give us the rationale for choosing that one over the other three?

Ms. PATENAUDE. Sure. As you know, Mr. Chairman, there are four formulas. The first three are very distinct. The fourth one is a modification of the third alternative. The decision was made, obviously by Secretary Jackson, to go with alternative four. But based on feedback that we received after the formula study was sent to the Hill and from stakeholders, we modified the definition of poverty. So it is based on formula four, and we feel that it best targets the community development need in line with what the statute intends for the program.

Mr. TURNER. I would like to walk you backward, then, to the description of the line that appears on the chart, the line of which the grantees are plotted against, where it says low need and high need. Could you please describe the factors that go into the determination of low need versus high need and how that plays, then, into the graph that we see?

Ms. PATENAUDE. As I stated in the testimony, the solid line is the needs index, or the measuring stick. There were 17 variables used in the needs index and, Mr. Chairman, are we talking about the proposed formula?

Mr. TURNER. We are talking about the 17 needs.

Ms. PATENAUDE. The 17 variables?

Mr. TURNER. You are right. You are going right down where I am going to ask you questions about. So please continue.

Ms. PATENAUDE. The expert on the variables is behind me, but I am going to take an attempt to answer your question, sir.

The 17 variables are grouped, the factors, to represent proxies for community development need, such as poverty, unemployment, crime rate, and the formula is measured against the community needs index.

Mr. TURNER. My understanding is that you did not modify that needs index. You are modifying the allocation of the grant formula, but not the needs index, which, would you please tell me the rationale as to why you did not modify the needs index?

Ms. PATENAUDE. As you know, we partnered with the Office of Policy Development and Research and the experts in PD&R believe that the variables that they used when it comes to the needs index

are time tested and reliable indicators. And the needs index is the same needs index in the old formula as the new formula.

Mr. TURNER. Because if you have an assignment as a program administrator to fashion a grant formula that more accurately approximates need, your outcome is going to be inherently biased by what your underlying definition of need is. And so the reason why I raise the question is that, without a significant review of where the first line is, the need line, your process of narrowing the variants between communities and the amounts that they receive is going to be biased to a needs index that you have not undertaken a review of.

Ms. PATENAUDE. As I said, the 17 variables were reviewed, so it is obviously a very broad range of community development needs in that measuring stick. And the data that was used is reliable data that is consistent and available to at least 800 of the entitlement grantees that we can get consistent data from the census.

Mr. TURNER. Mr. Czerwinski, you were nodding. Perhaps you can assist in this discussion more eloquently than I have as to describing the bias inherent in this process.

Mr. CZERWINSKI. Actually, Mr. Chairman, what I was thinking about is the nature of your request to us was to do exactly that, and that is examine the needs. I think there are two themes here, one going back to your original question, the quality of the program. This program does match up with congressional intent. The issue, though, is how you measure performance and how you then allocate funds.

The second theme is that this is an effort that is going to take quite a bit of time. We are in the early stages of it. HUD I think is stepping in the right direction, but I would not say that the answer is final by any means. What we really need to do is really just as you said, to reexamine the needs index, to calibrate the various variables and formula for allocating funds against that needs index, and then there is a whole dialog that has to go on with all the different players and then finally, it really is a congressional decision.

Mr. TURNER. Do you think there is a rationale that would justify the review of that needs index prior to changing the grantee formula, since we would be performing the program to conform to a needs index that was previously established?

Mr. CZERWINSKI. I would hope so, Mr. Chairman. Because GAO has a protocol that when requests come in to us from the Congress, we do evaluate whether they are worthy requests. And yours came in and we said, oh, this is a really good one to do. So yes, I would say there is a rationale.

Mr. TURNER. Great.

Mr. Patenaude, as you are aware, this subcommittee undertook a review of CDBG last year. And the full committee passed out a report with various recommendations as to issues that should be addressed with CDBG. Could you please tell me to what extent HUD took into consideration that bipartisan, unanimous committee report prior to delivering the act to Congress?

Ms. PATENAUDE. Thank you, Mr. Chairman. The CDBG Reform Act and the work that went into the act was actually on parallel tracks with the committee's work. Obviously we have read the com-

mittee report and we have taken some of the things into consideration. But some of the work had begun before we actually saw the report from the committee. And we obviously focused a tremendous amount of our energy on the formula.

Mr. TURNER. One of the issues that was raised in the hearings that we held on the proposed four formula changes that HUD was reviewing was the concept that is adopted in the proposed act, looking at the ratio of per capita income between a recipient community and their metropolitan area. Could you please describe HUD's decision to include that ratio?

Ms. PATENAUDE. The fiscal capacity?

Mr. TURNER. Yes.

Ms. PATENAUDE. The fiscal capacity adjustment would measure a community's per capita income against that of the greater metropolitan area, and that is one of the variables that we use in the proposed formula.

Mr. TURNER. Why?

Ms. PATENAUDE. I would have to defer to Mr. Richardson, Mr. Chairman.

Mr. TURNER. Mr. Richardson.

Mr. RICHARDSON. Thank you, Mr. Chairman.

Mr. TURNER. Please note for the record Mr. Richardson was sworn in at the beginning of the hearing.

Mr. RICHARDSON. This variable accomplishes three things. It captures a community's tax base relative to the cost to provide services in the area. It tends to address some of the inequities caused by the poverty variable, it tends to actually deal with some of the cost of living issues that GAO has discussed. And third, it significantly increases funding for more needy communities over the less needy communities.

We think that this is a very strong variable. There is past research that supports it. David Rusk has done previous work that supports this variable. We very much look forward to the GAO doing a careful review to see if they have any alternative approach.

Mr. TURNER. Could you just describe in the act how it is proposed to be utilized, how it applies to a grantee's formula? You told me your basis then for including it. Could you please tell me now how it works?

Mr. RICHARDSON. How it works, I am sorry.

Mr. TURNER. No, that is my next question. You answered the first one correctly. The second one is, how does that work?

Mr. RICHARDSON. So, let's take Dayton, for example. Dayton's per capita income relative to its metro area is less than that of, it is about 70 percent that of the metropolitan area. So Dayton's grant would be adjusted, you first do a flat allocation using the four variables that we are proposing, the poverty variable, the old housing occupied by a poor family, the overcrowding variable, and the female head of households variable. You make an allocation based on each community's proportional share of those variables, using those variables. And then you adjust that grant using this per capita adjustment.

So Dayton's grant from after this flat grant would be increased 25 percent in this particular case, because the maximum that could be increased is 25 percent, and Dayton's grant would be increased

the maximum amount. Whereas another community, Kettering, for example, which has a higher per capita income than the metropolitan area, it would have its grants reduced.

Mr. TURNER. You mentioned the issue of housing occupied by an individual that is in poverty. The previous grant formulas took into consideration the age of the housing stock. By limiting the element of the age of housing stock to only those that are occupied, you have eliminated any recognition of communities that have abandoned housing stock.

Could you please describe to me, my understanding in our first hearings on this matter was that HUD's goal was to remove from the grantee's calculations housing that was greater in age of 50 years that might have been occupied by someone who in fact was wealthy. So by then going to limiting the structures that have individuals that are in poverty, you are also then not recognizing in the available housing stock those properties that are just vacant, for which CDBG funds would be targeted.

Almost any mayor who has been before us will testify of an abandoned house that was a source of criminal activity, a blighting influence on a community and its desire to remove that, either having it renovated and placed in the hands of a family so that it can be occupied once again, or removing it from the community by demolition and then looking hopefully to an in-fill opportunity. The impact on the community and community development is clear. In the factors, though, it appears that it would not recognize a community's distressed nature of abandoned housing.

Ms. PATENAUDE. Mr. Chairman, we obviously appreciate the impact that abandoned housing has on neighborhoods and particularly declining neighborhoods. But we did not have available resources that is consistent across the entitlement communities on abandoned properties. I know that the Office of PD&R is working with the Postal Service to try to develop consistent data so that it is possible in the future we would be able to measure that. And by substituting, as you said, the pre-1940 housing that was distorting the formula, particularly in the northeast, by having the poverty household, that is a good proxy for declining neighborhoods.

Mr. TURNER. In the midwest, the number of units that are abandoned in the inner cities by far exceeds the number of families that are in those areas that are wealthy. So the desire to count abandoned housing units as a distressed or blunting influence factor would be very high on the list of communities that are impacted by abandoned housing.

At this point I am going to turn to Mr. Clay for his questions.

Mr. CLAY. Thank you, Mr. Chairman. I would appreciate if I could forego my opening statement and use that time as part of my questions.

[The prepared statement of Hon. Wm. Lacy Clay follows:]

STATEMENT OF CONGRESSMAN WM. LACY CLAY
HEARING ON CDBG REFORM
JUNE 27, 2006

Mr. Chairman, I thank you for holding today's hearing on the Administration's legislative proposal to reform the Community Development Block Grant program. I welcome our witnesses and look forward to their testimony.

As you know, Mr. Chairman, our subcommittee spent an extensive amount of time during 2005 reviewing the merits of the CDBG program, and went so far as to unanimously endorse a committee report of findings and recommendations that would prove beneficial to the program's future. If our efforts clarified anything, it is that CDBG continues to be a successful model for community development due to its widespread participation and flexibility among state and local grantees.

Looking at HUD's proposed reforms for CDBG, however, I have significant reservations concerning changes in the formulas for grantees, particularly for those who are currently entitlement communities. To be blunt about it, taking from Peter to pay Paul is not a productive way to meet the future needs of our cities and counties, although this is what HUD proposes.

Specifically, I remain unconvinced that communities who would lose money under this proposal

have fewer community development needs than those who would gain. My local city and county are a fine example, in which the City of St. Louis would lose nearly half of its annual funding allocation while St. Louis County would sustain a modest 10% increase in funding. Yes, the County does deserve an increase for its needs, but this increase ought not to come at the expense of St. Louis, or any other community that has appropriately demonstrated the needs of its citizens.

In closing, Mr. Chairman, it is my hope that the Administration will not dilute the effectiveness of CDBG through arbitrary formulas that don't account for the true needs of our communities. I thank you, and this concludes my statement.

Mr. CLAY. Ms. Patenaude, your proposal would cause a dramatic shift of resources between grantees and jurisdiction. But it doesn't contain a transitional period for those that lose funding. Why was this not included in your proposal?

Ms. PATENAUDE. Thank you, Congressman Clay. We acknowledge that there will be winners and losers with the redistribution under any of the formulas. We have provided for a 1-year transition period. And that in the first year, if a community is not eligible under the minimum threshold, they will be eligible to receive 50 percent of their previous year grant.

And at the same time, if they are no longer eligible under the minimum threshold, they can either join an urban county or participate through the State CDBG program.

Mr. CLAY. OK. In that instance, in my home town of St. Louis, it is slated to lose 31 percent of its funding under the proposed formula, while St. Louis County only gains 4 percent. Are there specific circumstances to indicate why St. Louis and its surrounding communities are deserving of a 27 percent net loss in funding, and do census population figures justify this?

Ms. PATENAUDE. Thank you, Congressman. We have used this example of Miami, St. Louis and Detroit, all communities with similar needs, not identical needs, but certainly similar needs. And if you look on the chart, this is an example of entitlement communities with similar needs receiving vastly different grant amounts. So those would be the jagged lines on the chart.

Currently, St. Louis is receiving $59 per capita, while Miami is receiving $22 and Detroit $43. So yes, St. Louis would be losing CDBG dollars, but it would bring the formula more in line, it would be fairer treatment. There isn't enough money gained from the communities with low need to give to the high need communities.

Mr. CLAY. OK, well, help me understand now. Have we developed a new definition of poverty? Is there a new definition that you all are operating under as far as what poverty is or what it looks like? That is one of the factors that you consider, am I correct?

Ms. PATENAUDE. Yes, it is, Congressman. Currently, St. Louis is funded under the formula B that measures growth lag, poverty and pre-1940 housing. Under the proposed formula, the factors that are being used measure the number of persons living in poverty, excluding college students. That was a distorting factor under the old formula. The number of housing units 50 years or older headed by a poverty household, the number of female-headed households with children under 18, the extent of housing overcrowding, and finally, there is a fiscal capacity adjustment.

Mr. CLAY. And that is the new formula, right?

Ms. PATENAUDE. Yes, it is, sir.

Mr. CLAY. Well, we fit into all of these categories. I am just bewildered of how we lost 31 percent. I mean, and don't get me wrong, I want transparency, I want accountability in the CDBG program. That is one of the things that St. Louis suffers from now. The supporters of CDBG can contest what I am saying, but I can take them to St. Louis and show them that St. Louis has derived these block grant moneys and has used them for other purposes, OK?

So here is what I need to know. Have you all consulted with any other groups, like the National League of Cities or U.S. Conference of Mayors? Have you gotten any input from them on this proposal?

Ms. PATENAUDE. The development of the formula was done, it was released in February 2005, and I understand the study took more than a year. I do believe that we did listen to our stakeholders. We have quarterly meetings with our stakeholders, and I am sure that consideration was given to their thoughts and ideas.

Mr. CLAY. I have just received a list here that says you have the U.S. Conference of Mayors, National Association of Counties, National League of Cities, National Association of Local Housing, Finance Agency, National Association for County, Community and Economic Development, National Community Development Association do not support the proposal. And so I assume you bounced off——

Ms. PATENAUDE. Congressman, I am not aware of them not supporting the proposal. I am aware of the opposition to the funding level. But we called in all of those stakeholders in May when we rolled out the CDBG reform proposal and briefed them thoroughly. We have been tracking, obviously, their newsletters.

Mr. CLAY. Well, this is a statement to this committee on this day that says, we wish to state at the outset that we do not, do not support this proposal. Let me go on to Mr. Czerwinski. And thank you for your responses.

Please explain how using metropolitan per capita income in the new formula can prove beneficial to higher income metropolitan areas? Wouldn't this leave older industrial cities at a disadvantage to those with high-tech or finance-based economies?

Mr. CZERWINSKI. Mr. Clay, if I may start for a second with the comment that HUD had about this being a measure of fiscal capacity, this may very well be a measure of fiscal capacity, it may not be. We will have to see. I am sorry to digress for a second, but when I was in junior high, I took a math test. I got the answer right, but the teacher marked it down some and said, you didn't show how you got there. And I think that is part of the issue that when you talk about how we got there, that is where your question is going.

Mr. CLAY. Well, let us continue to digress, then—[laughter]—because when I was in law school, I got the answer right, but according to professor, it was wrong. Now, let me ask you about capacity. Explain capacity of a community and what do you mean by targeting? Tell me what that means in layman's terms.

Mr. CZERWINSKI. Sure. When we talk about capacity, we are looking at the strength of the local government, the tax base, its ability to carry out programs. Essentially when you want something done by your city or county, do they have the means to do it.

Now, a great example of capacity is found in the Gulf Coast. There was capacity there, after Hurricane Katrina, there is not capacity.

Mr. CLAY. OK, but now following that train of thought, won't this favor communities that are more well off? I mean, in the end, won't this formula favor those communities and won't they eventually get the lion's share of the block grant money?

Mr. CZERWINSKI. Well, the devil is in the details, Mr. Clay. And it is a matter of how the variables come together and how they are weighted. And HUD's proposal just came out last month. We haven't had a chance to go through it. What we will do is look at their proposal. We will also look at needs and then separate from that capacity and then bring them together. It is almost like, to use the analogy of a math problem, you go back and you do a proof to see if you come up in the same place. At this point, I really can't say where their's will come up.

Now, looking at cost of living, compared to the metropolitan cost of living, in isolation, we can say that in that instance, it would favor those communities who have richer neighbors, because by comparison they will look poorer. But beyond that, I can't say.

Mr. CLAY. Now, maybe, just maybe that accomplishes what I would like to see, is that the money is actually targeted to those neighborhoods that actually need the economic infusion, that actually need the block grant money to rebuild, like you said, houses more than 50 years old. I can take you to St. Louis and show you entire neighborhoods like that, where there are plenty of vacant lots and few houses standing that are in good shape. Even business districts, that were once thriving, that are now dilapidated.

Now, will this new formula, this new proposal help address that, so that my city will not be able to take that money and put it into downtown, thriving business communities, or even well to do neighborhoods, instead of using it where it really needs to be used? Will this address that in any way?

Mr. CZERWINSKI. I don't know whether my answer will satisfy you, because we don't know. What we do know is that HUD shares your goal and ours to effectively target where the funds go. What we don't know is exactly how this works.

And getting back to the other point that you made about those who are at the local level living with this, that the League of Cities, the Conference of Mayors, the NGA, etc., those stakeholders were the starting point for our work. We were just beginning. But that was the very first thing that we did, we called all those people into a room and said, "OK, we are going to be looking at that, at your request. What kinds of things should we be thinking about?"

We didn't guarantee that we would do what they want, we didn't guarantee that we would come out with options that they favor. But we view them as a starting point, because ultimately they are the end point also.

Mr. CLAY. And as the process continues, I think that there will be a real need to put some strings on this money with local communities to ensure that the money goes to those targeted communities that actually need it.

Mr. Chairman, I will stop there. I guess we will get another round. But thank you very much, and thank you both for your responses.

Mr. TURNER. Mr. Dent.

Mr. DENT. Thanks, Mr. Chairman. Thanks for holding this hearing, too.

Questions on this formula change, and I am looking at my own district in Pennsylvania. Clearly we don't do very well. The Commonwealth of Pennsylvania's numbers, other than Philadelphia, ev-

erybody seems to take a cut. I represent the cities of Allentown, Bethlehem and Easton. Allentown does get a slight increase, which is a larger city than Bethlehem and Easton. But Bethlehem and Easton both receive significant reductions, according to this.

I am just trying to understand the methodology of this formula. Can you help me out with this? Allentown, for example, I guess does well on the needs index here and receives a 9 percent increase. But there is another community in Pennsylvania, the city of Chester, that has a 10 on the needs index but receives a 4 percent reduction.

Can you just explain to me what went into this thinking?

Mr. RICHARDSON. This is the most difficult thing about formula reform. It is the very needy communities that might have a reduction in funding because of the proposed change. The way to look at this is not, I know the first way to look, of course, is to see how your community fares, if it is reduced or increased. But the way to think about it in fairness is to look at your community's per capita grant relative to the per capita grants that will go to other communities you see as having similar needs as those jurisdictions.

Pennsylvania was developed some time ago, it has had a lot of population loss. A lot of the communities in Pennsylvania have done well because of the pre-1940 housing in growth lag variables, whereas some communities with very high poverty have not done well, they have been formulaic communities and had very small grants.

To bring some parity to the grant amounts——

Mr. DENT. So you are saying because of population declines in some cities, that has essentially increased the per capita grants to those communities until this change?

Mr. RICHARDSON. That is right. The loss of population is a good measure of need in a lot of communities. But the variable that is used in the current formula is a very sensitive variable, so it only takes very little difference between communities in terms of their population loss to cause very large differences in grant funds. I think a good example would be to compare Pittsburgh and Philadelphia.

Mr. DENT. Yes, Pittsburgh has had substantial decline, as has Philadelphia.

Mr. RICHARDSON. Absolutely.

Mr. DENT. But Philadelphia increases. They have both had substantial population declines.

Mr. RICHARDSON. That is right. Let me go into that. Currently, Philadelphia gets $36 per capita and currently Pittsburgh gets a very different grant amount. They are right next to each other, handily enough on that chart.

Mr. DENT. Yes. Philadelphia receives a 10 percent increase.

Mr. RICHARDSON. So Philadelphia's grant would go up to about $40 per capita, which is closer to how much Detroit gets. And Pittsburgh's grant would fall to $30 per capita, which is closer to how much New York or Chicago gets.

Mr. DENT. I guess the question, then, is this formula overall geared more beneficially toward States with population increases? Because I am looking at the overall list on page—I don't know what page, it is Roman numerals, 23, I guess, XXIII. Alternative

4, table ES 3, if I am looking at alternative 4, which I think is a close comparison to what you have presented here today, it just shows that the southeastern portion of the United States and the southwestern portion of the United States overall seem to receive substantial increases and it is safe to say those are areas of population increase in the recent years. And in Puerto Rico, too, and I can't explain that.

But the bottom line is it looks like the midwest and the mid-Atlantic region where I am, and certainly New York and New England all receive substantial reductions overall. Is it fair to say it is because of the population growth in the south and the west? That is what drives this funding formula?

Ms. PATENAUDE. If I may, Congressman, just answer. We made a conscious choice on this new formula to target the communities in decline. I do believe the northeast benefited in some instances, perhaps unfairly because of the pre-1940 housing in wealthier communities. So the new formula definitely favors declining communities. And as Todd said, it is all relative to need. So comparing a community with similar needs.

Mr. RICHARDSON. If I can add to that, on average, communities that have, in the southwest, that have higher poverty rates, that in the past, got fairly small grants under the formula, their grants do go up, and that is why you see the increase in the southern region of the country. And on average, communities with population loss and older housing in decline do see their grants decline.

But overall, the communities in decline still receive substantially larger grants than the communities that have the high poverty and population growth. I think if we, actually, chart two is a little clearer about this. Could you put chart two up, please?

So the needs index doesn't distinguish well between communities in decline versus communities that have the high poverty. So if we had targeted exactly to the needs index the lines would be much closer to that solid line. But instead, by having the formula proposal target more closely to communities in decline, you still see this difference between, so you see some communities well above the line and some communities below the line. And those reflect that difference between communities in decline versus communities with the higher poverty. There is still a difference, but that gap is narrowed from what that first chart showed about, so that you went from gaps that were quite large to gaps that were smaller. But there is still a favoring of communities in decline over communities with high poverty.

Mr. DENT. I am looking at the city of Easton, PA. I am trying to understand how they receive, it is a city that is landlocked, it has a lot of challenges to say the least. But it receives a 30 percent reduction. It is not a big city, but an entitlement community, and I just see a $294,000 reduction. I guess the per capita number is still high, but it just strikes me as a significant reduction for that community with that type of need. I see what you are attempting to do here. But overall, it just doesn't work very well where I live.

Can you just give me a comment on Easton, why they would have seen such a dramatic decline? Is it because the population has been pretty stagnant, maybe a slight decrease over the last 20 years, but not a huge decline?

Mr. RICHARDSON. Easton certainly is a community with distress, it has 12 percent poverty. Its allocation would be on par with other communities of similar types of distress, like Richmond, Virginia or Toledo, OH. So that is what the allocation is doing, it is adjusting the grants to be similar for communities of similar need. It is obviously difficult for a community that does have high needs to have a reduction in funding, absolutely.

Mr. DENT. All right, then, well, I have no further questions. I will yield back. Thank you.

Mr. TURNER. Mr. Richardson, I am going to go back to the per capita income comparisons. You described Dayton as an example. In my first question, with respect to the per capita income ratio, I asked you, actually Ms. Patenaude deferred to you on the issue of why you would include the ratios. Your answer was because it would take into consideration the tax base to cost of services and inequities in the cost of living.

Now, the provision of the act that the administration has been put forward only does the comparison for the ratio of per capita income of the metropolitan area to the per capita income of the formula grantee within the metropolitan area. Then with the amount that you indicated of the 25 percent cap for adjustment.

There is no element within that, or within this act that I see, and I am asking you to point it out if it is there, of any indication with respect to the elements that you told me as the why this is here, there is no provision that relates to measuring the tax base of cost of services. There is no element that relates to cost of living, so there is nothing that would relate to the inequities of cost of living.

For tax base, for example, some communities are real estate tax dependent. Some communities are income tax dependent. To take into consideration tax base, you would actually have to have some element that goes to the revenue generation of the community and the cost of services. Again, you would have to go to some of the differences in each of the community as to those costs.

Cost of living, cost of services, of course are two different things. You said inequities of cost of living. I don't see anything in here that relates to cost of living. So could you please tell me how it is that by taking into consideration only the ratio per capita income that you expect to capture tax base to cost of services and inequities of cost of living.

Mr. RICHARDSON. You have certainly hit on one of the most challenging things about trying to deal with fiscal capacity. I think GAO will address this, too. Per capita income in itself tends to be, well, I will start off by saying there aren't very many good variables that allow you to capture a community's taxing ability. But per capita income, a measure of income, a community with higher incomes tends to have more ability to tax than a community with lower incomes. I think we can probably agree on that.

Mr. TURNER. If they are income tax based.

Mr. RICHARDSON. How the community chooses to tax itself is up to that community. But if you find a community that has higher incomes, that tends to have higher property values, so if you are land based, that would lead to a higher taxing authority.

In any case, the concept here on the two fronts of fiscal capacity and also on cost of living are as follows. So for fiscal capacity, the concept is that per capita income for a metro area is a rough measure of what it costs to live in the area. Places with higher incomes tend to have higher costs of living.

If you are a poorer community in an area with a high cost of living, you are going to have a harder time raising revenues to be able to buy the services in that area, because the service is more expensive. So you would have your grant increased to reflect that.

Mr. TURNER. Mr. Richardson, would you stop for a second? You are making several statements which are assumptions of which you do not have, from the information that we had presented to us, and the information that GAO reviewed when we had this hearing last time, that your data does not prove. Would you admit that per capita income does not, as a measuring factor, deliver statistical data based upon tax base to cost of living ratio, or inequities of cost of living?

Mr. RICHARDSON. I am sorry, you would like me to confirm what comment?

Mr. TURNER. You are stating several assumptions as to how it gets you close enough to your purposes and goals of measuring tax base to cost of services and inequities of cost of living. But they do not. And I am asking you to acknowledge that measuring per capita income as a ratio does not measure tax base to cost of services or inequities of cost of living.

Mr. RICHARDSON. I disagree.

Mr. TURNER. OK. Well, the GAO and the other studies that we have had before this committee says that it does not, and you have been stating several assumptions. Could you please tell us what data that you have that shows that, how per capita income measures tax base to cost of services or inequities of cost of living?

Mr. RICHARDSON. David Rusk, Cities Without Suburbs, uses this measure extensively and looks at that issue. And so I would have to refer you to that research.

In terms of what the GAO is looking for, I look forward to the GAO reviewing this variable and seeing if it supports the position that we have for the analysis, or if it supports the position that you are stating. I think that would be an interesting analysis.

Mr. TURNER. Well, the committee is familiar with the Rusk studies and his information and data. And what I would like you to do is take some time to supplement your answer after this hearing, indicating how you believe that per capita income ratio measures a tax base of a community or how it measures cost of services in a community, or how it relates to cost of living in a community.

Mr. RICHARDSON. Absolutely.

Mr. TURNER. Along with Mr. Dent, I would like to acknowledge that under this formula, Dayton, OH, my community, would be slated to lose 16 percent of its overall funding in CDBG. That 16 percent loss is to a community that clearly has significant economic distress factors and significant community development factors of abandoned housing and community development needs, which would lend me to question the basis of which this formula is to improve targeting in that, as with Mr. Dent, I can identify several communities in this list that appear to receive additional funding

that have greater financial capacity and perhaps less community development stress than one would see in Dayton, OH.

But in going to the issue of cuts, and Ms. Patenaude, this question is for you, in looking at the split in the previous funding formula between entitlement communities and non-entitlement communities, the amount of the pot of funds that were available to entitlement communities overall appears to be reduced by this proposal. In other words, the total pot of the formerly known entitlement communities has available to it is reduced. Therefore, those communities that are gaining are actually gaining out of a pot that is smaller, and those that are losing out of a pot that was already diminished. Is that accurate?

Ms. PATENAUDE. Thank you, Mr. Chairman. The reform package does eliminate the artificial 70–30 split that is statutory right now. But the breakdown is actually very close to the 70–30. And the entitlement communities, the share to entitlement communities has been shrinking because of the increase in the number of entitlement communities in the last decade. But I believe it is still very close to the 70–30.

Mr. TURNER. But even with the 70–30 split, you have taken another $200 million out with the competitive grant formula. So the overall pot itself is diminished, is that correct?

Ms. PATENAUDE. The challenge grant is only available to distressed entitlement communities. Communities participating through the State program would not be eligible for that, so that is still reserved for entitlement communities, and communities such as Dayton that target their CDBG dollars to distressed communities would have an opportunity to actually gain funding with the challenge grant.

Mr. TURNER. Can you go down the list of recommendations that came out of this full committee in again, in unanimity on a bipartisan basis and the ones that are not addressed at all, I will just identify them and move on, and the ones where we have a difference of opinion are the ones I want to highlight.

We first indicated, the full Committee of Government Reform, not this subcommittee, indicated that HUD should acknowledge that any proposed needs test may be inherently subjective by its nature. Therefore the policy implications of new or additional needs tests should be fully vetted before they are implemented. Ms. Patenaude, you indicated that the needs test is not modified in this recommendation, correct?

Ms. PATENAUDE. The needs index is the same index, that is correct, sir.

Mr. TURNER. The discussion that we had in previous hearings concerning the impact of immigration and how that relates to impacts on communities, this act does not include any review by HUD of the impacts of either legal of illegal, the total category of immigration, correct?

Ms. PATENAUDE. I believe in the proposed formula that we do capture the immigrant growth population.

Mr. TURNER. But there is no other independent data that you looked at with respect to the impact of immigrant populations on distressed communities?

Ms. PATENAUDE. I believe it is considered in one of these factors. Todd, do you want to answer?

Mr. RICHARDSON. I think your question is, have we done further review to determine what the impact of immigrant populations are on communities?

Mr. TURNER. Correct.

Mr. RICHARDSON. We haven't done further review. The original analysis and the analysis we still have to work from is the analysis done by the National Academy of Sciences in 1997, where they did the analysis on the fiscal impact of immigrant populations, which showed a significant impact. The communities had a greater cost than they returned in revenue generated.

Mr. TURNER. We have already dealt with the issue of the income ratio. And the full Committee on Government Reform had a different recommendation than the act presents. The next category is the vacant and abandoned housing stock. We had a recommendation that should be considered as an index factor, and abandoned and vacant housing stock, Ms. Patenaude, is not included in the act, correct?

Ms. PATENAUDE. That is correct, sir, but we are working to collect that data.

Mr. TURNER. The initial proposal for, from which this act is in part derived, had taken out all single non-elderly populations in an attempt to get to student populations. It is my understanding that you did correct that in the act itself, you did instead exclude only unrelated individuals enrolled in college?

Ms. PATENAUDE. That is correct, sir.

Mr. TURNER. The one recommendation that we had, obviously, was that HUD work in conjunction with GAO. GAO's report is not completely finished, so I am assuming that HUD would continue its commitment to work with the GAO as its findings are available in looking at ways that this act might be able to improve?

Ms. PATENAUDE. We will fully cooperate with the GAO, Mr. Chairman.

Mr. TURNER. One of the recognitions of the need to change the grant formula is to look at the fact of the changing demographics of communities. The committee had made a recommendation that periodic review of the CDBG grant formula perhaps should be incorporated in any act reform that would cause as a trigger an automatic review. You have chosen not to set a time period for periodic review. I am assuming that doesn't mean that you are opposed to, on a regular basis, this process being reviewed?

Ms. PATENAUDE. We did not include it in the legislation, but as you know, we have reviewed the formula every 10 years, when we have the decennial census data. But I agree that would be something that should be considered in the legislation.

Mr. TURNER. We had recommended that if the CDBG formula is to be amended, that a phased-in period, to give communities an opportunity to modify their processes, because many communities have advanced planning for community development, the act, from what I understand, has a 2-year phase-in for grantees affected by the minimum allocation threshold, those that would be, in effect, de-funded, I believe.

Do you have a consideration for the transition for all communities?

Ms. PATENAUDE. The communities that would no longer meet the threshold?

Mr. TURNER. Yes.

Ms. PATENAUDE. Would be eligible to participate either as part of an urban county or through the State program. And we have a provision that they would be able to receive their grant the first year, under the new formula, at 50 percent of the previous year grant.

Mr. TURNER. But for communities like Dayton, OH, that under this proposal would have a 16 percent reduction in funding, there would not be a phase-in. Upon the adoption of the act, the funds would be immediately reduced?

Ms. PATENAUDE. Cities like Dayton would qualify to participate in the challenge grant program.

Mr. TURNER. Yes, they have an opportunity to apply to you to receive additional funding. But those funds that they would automatically receive under the act, the reduction that you have identified, HUD has identified as 16 percent, that would happen without a phase-in immediately?

Ms. PATENAUDE. That is correct.

Mr. TURNER. We spent some time in this committee looking at the issue of eligible activities for the use of funds. This act does not address the issue of use of funds. We raised the issue of under the current CDBG program, there is no limitation to the amount of dollars that a local community can spend on its own staff. There certainly is a limitation on administrative funding. But on overall funding that a local community allocates to staff functions, that there is not a limitation, this act does not address the issue of eligible activities, how a community spends their funds, correct?

Ms. PATENAUDE. That is correct. We did not change or suggest a change to the eligible activities, but we certainly are open to that discussion.

Mr. TURNER. Can you tell us why you didn't look at the issue of eligible activities?

Ms. PATENAUDE. The CDBG Reform Act of 2006 focuses on performance and results and obviously encourages communities to target their dollars and concentrate their dollars. And by offering the opportunity to participate in the challenge grant, we believe that communities will hopefully do a better job of using their resources in a concentrated way.

We didn't want to take away any flexibility, so that the local elected officials can make those decisions based on their community development needs. As you know, the three national objectives stayed in place as well.

Mr. TURNER. I'll refer to Mr. Clay for questions.

Mr. CLAY. Thank you, Mr. Chairman.

Ms. Patenaude, I am concerned that newly proposed performance measures will become an expensive administrative exercise for grantees. Should HUD provide technical assistance or supplemental administrative funds for these activities? Is HUD capable of reviewing annual performance outcomes and assisting in remediation efforts for grantees?

Ms. PATENAUDE. Thank you, Congressman. We are currently implementing the performance measurement framework. We have 15 trainings scheduled throughout the country. They are ongoing until the end of August, so all of the entitlement and State grantees have been invited to participate in this training.

We also had thorough discussions with all the stakeholders when we were developing the performance measurement framework, and it certainly is a consensus document. OMB was also part of that working group. We acknowledge that IDIS can be cumbersome, but we have invested a tremendous amount of time and energy in updating the IDIS system. The screens are available right now, and the grantees are already inputting performance measures. By October we will require it and we believe that 1 year from now we will be able to answer that question better. But we do not think it will be an additional burden on grantees.

Mr. CLAY. If a grantee fails to meet benchmarks for performance, what types of penalties should there be imposed?

Ms. PATENAUDE. The act provides for the Secretary of HUD to either withhold or reduce CDBG funding if the community does not meet the targets that they have set in their performance plans.

Mr. CLAY. Thank you very much.

Mr. Czerwinski, I have two major concerns with the inclusion of a new performance measurement requirement. First, will communities have appropriate technical assistance from HUD to comply with these requirements? And I don't want grantees wasting grant money in order to comply with a paperwork exercise. And second, what types of penalties or remediation requirements would HUD prescribe if a grantee was not making adequate progress?

Mr. CZERWINSKI. Mr. Clay, GAO is about to issue a report later this summer that looks at those very issues for this committee. We are asked to look at the uses of CDBG funds as well as HUD's monitoring, which would tie into reporting and information system requirements. So your question is right on target for what we are talking about.

And speaking about a target, probably the key issue there is technical assistance and how the information is used to help the local governments increase their capacity to do what they need to do to get the funds. So those should be the exact targets of such an effort.

Mr. CLAY. OK. Let me lay out a scenario for both of you, and both of you can take a stab at answering. St. Louis County, their inner ring suburbs have become less affluent. City residents have moved to these areas and have stretched the services of those municipalities that they have moved into. St. Louis County only gets a 4 percent increase in CDBG funding. Perhaps we should take another look at population shifts and factor these population trends into the proposed formula. And we should probably also look at this new influx of new citizens, of immigrants that come to communities like St. Louis. We have a large population of Bosnians who have migrated to St. Louis over the last 10 or 15 years.

Would you all consider that once, since you have now gotten some feedback from us, I mean, what would you do to change those formulas?

Ms. PATENAUDE. Congressman, if Mr. Richardson——

Mr. CLAY. Mr. Richardson, you can try to tackle it.

Mr. RICHARDSON. I'm sorry, would you repeat the question?

Mr. CLAY. We have influxes of new populations into St. Louis County inner ring suburb, new immigrants like from the Bosnian community. I am not sure that you factored those considerations into this proposed formula.

Mr. RICHARDSON. There is not a direct measure of new immigrants into the community. But to the extent that new immigrants bring new factors of distress such as increased poverty for a community or increased rates of overcrowding, those do come into account and would affect that community's grant changing and increasing in that particular case, if the community is in decline, if those factors would be measured to allow its grant to increase.

Mr. CLAY. So in the case of St. Louis city or county, that would be an additional factor that you all would take into consideration?

Mr. RICHARDSON. The formula currently has four variables associated with need poverty, older housing occupied by poverty households, overcrowding and female head of households with children under the age of 18. To the extent those variables increase, and to the extent those variables increase at a higher rate for that community than they do for the rest of the country, that community's grant would go up.

If for example the whole country goes up at the same rate, the grant would stay static.

Mr. CLAY. What if one of those factors were not present, like overcrowding? Say you have a less densely populated city, but what then?

Mr. RICHARDSON. To the extent that poverty is increasing, poverty gets weighted at 50 percent. It is the most important variable in the proposed formula. Then your grant would go up.

Mr. CLAY. Thank you for that info. Thank you, Mr. Chairman. I yield back.

Mr. TURNER. I have one final question, and then I want to open it to any closing remarks. Obviously we have had a pretty extensive discussion, and you might have, those who have testified, some thoughts that you want to add to the record or raise as questions that we have not asked for additional review.

One of the things that has interested me, and this is my final question, is the issue of looking at measurable objectives in community development block grant funds. The Strengthening America's Communities initiative that would have moved this CDBG funding and other grant programs from HUD to Commerce had as its cornerstone an issue of trying to impose performance measures in communities as to how they use these funds for community development.

Many times, the description of how a community would be rated are elements of which a community either might not have any control or which do not relate to the effectiveness of their use of CDBG funds. When I look to the list of the challenge grant fund, these are the elements on which a community would be rated. The change in employment rate of residents, income levels of residents, enrollment rate of high school graduates into higher education institutions, date of resident ownership of homes and businesses, and the change in residential real estate values.

In looking at the formula grantees, the non-challenge grants funding, the performance measurements objectives list, suitable living environment, development of decent affordable housing, fostering and creating economic development and opportunity. When I look at these elements that are in the challenge grant, almost every one of them you can go through and identify things that could occur within a community that have nothing to do with the community's administration of its CDBG funds or even the effectiveness of its leadership in economic development strategies.

Ms. Patenaude, if you would please respond to that issue, it was raised before, I believe, by GAO as we look to the proposed formulas and it had been raised in the Strengthening America's Communities initiative. Do you similarly have a concern that the items on which communities might be measured may not relate at all to their community development efforts and their use of CDBG funds?

Ms. PATENAUDE. If I may, Mr. Chairman, clarify the question. You are looking at the objective criteria under the challenge grant versus the objective and outcome measures under the performance measurement system? Comparing the two?

Mr. TURNER. Right. Which are somewhat similar. In looking at both of them, let me give you one example scenario. If a community has one large employer that exits in the community or ceases operations altogether, its impact on the community, and really the occurrence of its exit may not relate at all to how effective the community has been with their CDBG dollars, or in community development or revitalization. But it would significantly impact these factors.

Similarly, change in residential real estate values, a metropolitan community is part of a larger metropolitan area that could see a decline in residential real estate values as you can pick up almost any newspaper and the discussion of what is going to happen in the future of real estate values in some markets that have been identified as overheating. Those are all areas that have nothing to do with how a community uses their CDBG dollars or their effectiveness in community development.

Do you have a concern that these elements might penalize a community that has been very effective with CDBG by elements over which they have no control?

Ms. PATENAUDE. We still have a very important measure, and that is to be sure that the community development block grant funds are targeted 70 percent low-mod income. As you know, more than 70 percent is spent for low and moderate income persons. So I think that is definitely one of the safety nets that we have to measure a program that is as complex and flexible as the CDBG program is difficult. I think some of the things that you were addressing were under the previous proposal, under the Strengthening America's Communities initiative.

Mr. TURNER. Actually, I was reading from that.

Ms. PATENAUDE. Under the challenge grants, we have listed some objective criteria, but we are certainly open to discussion on that. The performance measurement framework was 2 years in the making, working with the stakeholders. So the grantees had a tremendous amount of input. We did not design this in a vacuum.

And OMB participated. So a year from now, Mr. Chairman, I may be able to answer that question better.

Mr. TURNER. Mr. Czerwinski.

Mr. CZERWINSKI. Mr. Chairman, your question cuts right to the heart of performance measurement. There is a tension between trying to find the perfect measures of all the things that we want a program to achieve or, going the exact opposite direction, saying, well, let's just measure the minute program outputs. The real challenge is to get some middle ground there. And I agree completely with Ms. Patenaude, this is going to take some work.

There are measures in the middle, I would say, affordable housing, maybe one that a community has a little bit more control over than some others and that is more closely linked to community development and its objectives in the projects within it. But frankly, we are not there yet.

Mr. TURNER. So you do have some concerns that the elements that are identified may be outside the control of a community and unrelated to their CDBG performance?

Mr. CZERWINSKI. I wouldn't want to be the mayor of some of those communities saying I can control all those things.

Mr. TURNER. Thank you.

Are there any other questions from members of the subcommittee? If not, at this time, then, I will turn to each of you and ask if you have any closing remarks that you would like to place in the record. Also, please include any additional questions that you think that we need to pursue. Even if you don't have the answers for them, they would be important for us to capture as additional items for us to review in the future.

We will start with Ms. Patenaude.

Ms. PATENAUDE. Thank you, Mr. Chairman. We appreciate the opportunity to share the administration's proposal on CDBG reform, and we look forward to feedback from our stakeholders. We feel that there is certainly an urgent need to address the formula and to restore equity to the fairness in the formula. Again, thank you for the opportunity to appear before you today.

Mr. TURNER. Mr. Czerwinski.

Mr. CZERWINSKI. Mr. Chairman, as you know, GAO is full of researchers. So we are policy wonks and we love this kind of discussion. So thank you for being able to give us that format.

There are a few things that came across to me in our discussion today. First of all, it seems to me that we have pretty close to agreement on the objectives of the program and what we want the reforms to achieve. I think we also have a pretty clear, maybe not 100 percent, but pretty close agreement on what the issues and challenges are. And in that regard, I want to make sure that I have been adequately complimentary to HUD. Because they have really advanced the ball here. They have done a lot of good, hard work.

I was struck by what you have to deal with. And I was thinking about what Mr. Dent was saying about what is going to happen to my community. Ultimately you have to decide what the right answer is and go back to the community and defend it.

Then I was thinking about the discussion that we had with you, Mr. Clay, and you, Mr. Turner, on a couple of the variables. We don't get these discussions, I do a lot of testimony. I don't get a

chance to dig into variables, so I really am grateful that we did that.

The two that jumped out at me were immigration and abandoned housing. I was struck by Mr. Richardson's answer, which I think is the right one at this time, is that we don't have direct measures. So what we are coming up with by definition is proxies.

Well, the proxy may work and the proxy may not. But when you make it a policy decision, you are going back to defend it to constituents, that is a really tough position to be in. And so what we are hoping to do in our study is to go behind the variables, particularly those two that you outlined, and try to come up with, if there are direct measures, what are the pros and cons of them, what needs to be done to come up or refine the direct measures, and then what the implications are.

So let's take immigration for a second. When we talk about overcrowding, that may or may not be a good measure of immigration. It may pick up some parts of it. But what we like to look at is what are the characteristics of immigrants, and what kinds of pressures do they bring on the community. And if there is a measure in there, we will try to find it.

As I mentioned, we brought in the National Academy of sciences to help us with the statistics and the local expertise. So what we would like to do is go back and do our work and then consult with HUD and then come back and talk with you about what we found, what works, what doesn't, and then try to give you something you can work with. Abandoned housing is in that same area. Frankly, there isn't a good measure of abandoned housing. My guess is it is going to be several years off before you have one. I do think HUD has a good strategy for abandoned housing.

But it is just going to take time. No matter how good a strategy is, it just takes time.

Mr. TURNER. Mr. Richardson, any closing comments?

Mr. RICHARDSON. Just thank you for your time.

Mr. TURNER. Before we adjourn, I would like to thank each of you for participating today. I appreciate your willingness to share your knowledge, experiences and thought with us today. Undoubtedly, CDBG has been a key component to the many triumphs cities have had over poverty and community development need. We all agree that the program provides vital funds to address critical needs.

Thanks to CDBG, many individuals and families live in safer, cleaner neighborhoods, with improved infrastructure such as street lights, handicap accessible sidewalks and parks and playgrounds, amenities to which everyone should have access. As we have all acknowledged, however, we recognize the need for CDBG funds and applaud the success of the program, there remains room for improvement from the inequitable distribution of funds, and the definition of need, to the lack of performance measures and enforcement capabilities.

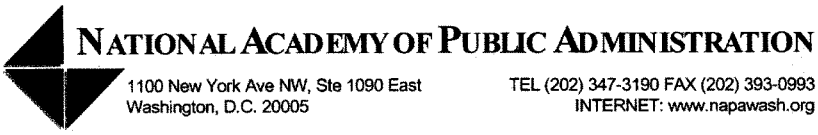
I am encouraged by the administration's response to the need for program modification and I look forward to continuing the dialog with suggestions on how to improve the administration and distribution of these important dollars.

I want to thank GAO for their efforts in continuing to review this and I appreciate HUD's thoughtful look and approach and willingness to continue to work on ways that even the administration's current proposal might be able to be improved. In the event that there may be additional questions that we did not have time for today, the record shall remain open for 2 weeks for submitted questions and answers.

I thank you all. We stand adjourned.

[Whereupon, at 11:35 a.m., the subcommittee was adjourned.]

[Additional information submitted for the hearing record follows:]



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Statement for the Record

The CDBG Reform Act of 2006

THOMAS M. DOWNS
Academy Fellow

U.S. House of Representatives
Committee on Government Reform
Subcommittee on Federalism and the Census

June 27, 2005

Mr. Chairman and Committee Members:

I appreciate the opportunity to submit for the record this statement about major provisions of the CDBG Reform Act of 2006. This statement does not reflect the views or position of the Academy as an institution. Instead, it reflects in large part the work and experiences of an Academy Panel convened to develop effective performance measures for the U.S. Department of Housing and Urban Development's Community Development Block Grant (CDBG) program. The Panel released two reports connected to this work, "Developing Performance Measures for the Community Development Block Grant Program" and "Integrating Performance Measures into IDIS." I was pleased to serve as a member of this Panel.

In this testimony, I would like to offer an assessment of four major provisions of the Act:

- revised Community Development Block Grant (CDBG) formula
- Community Planning and Development (CPD) performance measurement system
- challenge grants for entitlement communities
- consolidation of Section 108 loan guarantee program, Brownfields Economic Development Initiative (BEDI) and Rural Housing and Economic Development Program (RHEDP) into CDBG

The proposed reform is intended to improve targeting of funds to places that cannot meet their community development needs without federal assistance. The second and third proposed reforms work together to strengthen the program's focus and provide incentives for communities and states to invest funds strategically to expand opportunity for their low-income residents. The fourth proposed reform builds on the CDBG program's inherent flexibility by consolidating narrow-purpose programs with the more flexible block grant.

1. Revised CDBG Formula

From Revenue Sharing to Anti-Poverty Program. In reengineering the CDBG grant award formula, the Act replaces the existing "dual formula" for distribution of formula grant funding to entitlement communities and states with a new formula intended to direct most funding to places that cannot meet their own community development needs. In general, at a community level these are places having a higher proportion of low-income population and lacking the local economic base to adequately invest in improved opportunity for this population. The proposed new formula would substantially redirect CDBG funding to those communities. Our review of the current CDBG program formula finds that it has obsolete elements and, in too many instances, directs CDBG funds to jurisdictions that can assume these costs within their own resources, thereby reducing the proportion of funding invested in impoverished places and people. By redirecting funding to those places and people most in need of assistance, the proposed formula reform would necessarily reduce funding to communities with adequate fiscal capacity.

This would be a major improvement over the current CDBG formula, because logic and economics suggest that more affluent communities usually use CDBG funds to replace local resources. In contrast, poorer communities are much more likely to use CDBG funding to increase spending on the needs of their poorer residents. Various formulae options other than this one might improve the allocation of CDBG funding. However, we find that this proposed formula has a solid statistical basis and is relatively straightforward and understandable in its components. Similarly, in establishing a minimum funding threshold for participation in CDBG, the Act concentrates more funding in fewer places with greater needs, thereby increasing the probability that resources will be used to improve the lives of poor people.

Improving Focus and Performance

If the only purpose of CDBG were to increase spending on the needs of low-income communities, then a formula change of this sort might be a sufficient reform. However, CDBG is not just a "revenue sharing" program. Congress intended for these funds to help achieve important national goals. Given the competition for scarce resources and many competing claims on them, CDBG can be and has been fairly criticized for its lack of clear focus, lack of evidence that is contributing to the development of low-income communities, and the weakness of incentives for recipient jurisdictions to use funds strategically and most effectively to achieve the program's goals. The second and third reforms proposed by the Administration are intended to address these program weaknesses.

2. New CPD Performance Measurement System

New CPD Performance Measurement System. The Act would adopt and use a new performance measurement system for CDBG and other HUD community development programs, the design and implementation of which have been in progress for some time. The new system was developed through the joint efforts of CDBG stakeholder groups and associations, HUD program staff, and staff at the U.S. Office of Management and Budget. In previous testimony before this Committee on May 24, 2005, I applauded all parties for their excellent work on the system and encouraged the Committee to support the work whenever possible. I continue to support this exemplary effort, which would now be codified in the proposed Act. The Act would authorize HUD to use the new performance measures as a framework for assessing progress and holding communities accountable for the results they achieve. This would be focused on achieving progress in improving the lives and opportunities of low-income residents of the recipient communities.

Linking Performance, Planning and Mission. Although the new performance measurement system is a major improvement and is exemplary in the federal system, the proposed Act will require additional work by the Congress and the Administration on two tasks: (1) to clarify the expected results of this spending; and (2) to develop a reliable set of universal measures for communities and states, the Administration, Congress and public to use in assessing their progress as they invest CDBG and other programs and

resources in low-income communities. These additional steps will be needed to change CDBG from a mere revenue sharing program to one that uses its funds strategically to cause communities to develop. This begs for a renewed public debate about the purposes of the federal government's community development programs. Congress could statutorily provide CDBG with a new or clarified mission, vision and purpose in which the new performance measurement system should be imbedded; alternatively, it could provide authority for the executive branch to specify long-term performance goals for CDBG and other programs consistent with the general purposes for which those programs are now authorized. If this clarity of purpose is not accomplished by one means or the other, neither HUD nor states or communities will have clear direction about how to use funds most effectively. The new performance measurement system may not be effective unless it is synchronized and focused by clear expectations about intended goals.

3. Challenge Grants for Entitlement Communities

HUD currently awards CDBG funding by formula without regard to performance, aside from minor compliance requirements under the Housing and Community Development Act of 1974 and subsequent CPD regulations. Consequently, entitlement communities and states need not concentrate their use of grants on targeted neighborhoods or use them strategically to leverage other investment that would lead to permanent gains in economic opportunity or quality of life for low-income residents. Therefore, CDBG resources often have been spread thinly and used to ameliorate rather than solve problems caused by

concentrated poverty. This design weakness is a major reason why the program cannot demonstrate a contribution to lasting improvement in the capacity of low-income communities to address their residents' needs for economic opportunity and improved surroundings. The proposed Act would offer entitlement communities additional funding if they invest in Neighborhood Revitalization Strategy Areas (NRSAs) that meet certain selection criteria and invest CDBG and other funding in the development of those areas. In so doing, CDBG brings to bear not only its own funding, but also other public and private funding in a targeted approach. I support this provision as a good first step to reward improved performance. However, over time, it is important that more direct measures of progress in improving the opportunities and lives of low-income residents be developed and applied when awarding these bonus funds. These and other rewards for using funds effectively to achieve specific outcomes consistent with clarified national goals would over time lead to more effective use of CDBG to bring economic opportunity to the poorest communities.

Consolidation

The Administration has proposed consolidating small, narrowly focused programs into CDBG. The intent of this reform is to provide communities with greater flexibility in the choice of how funds are applied, thereby building on the inherent flexibility of CDBG.

4. Consolidating Section 108, Brownfields and RHEDP

In addition to CDBG, CPD manages three inter-related programs—Section 108, Brownfields and RHEDP. Much of what might be done under these programs could be done under the CDBG umbrella, eliminating the need to separately administer and coordinate community development programs. There are no advantages to maintaining separate programs when one would suffice.

I support this provision of the Act. The proposal to consolidate community development programs raises a fundamental issue with regard to the most effective design of federal grant programs that was first addressed in 1974 when CDBG was created by Congress to provide consolidated, flexible support for local community development by combining narrower "categorical" programs. This flexibility has been widely regarded as a strength of the block grant approach. Flexibility *is* a strength – but only if flexibility with regard to activities and strategic approaches is combined with agreement on the national goals to be achieved, decisions on how progress is to be measured, and the establishment of an incentive system that rewards progress measured in terms of that purpose. Congress should consider the Administration's CDBG reform proposals in the broader context of how to improve the performance of all federal programs that contribute to the development of low-income communities.

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Thank you for this opportunity to share my views on the CDBG Reform Act of 2006.

The Academy looks forward to assisting the Committee in the future in any way we can.

Academy Documents on CDBG

Testimony, Thomas M. Downs, Developing Performance Measures for the CDBG Program, presented to U.S. House of Representatives, Committee on Government Reform, Subcommittee on Federalism and the Census, May 24, 2005. www.napawash.org/resources/testimony/CDBGtestimony5-24-05.pdf

Statement for the Record, Community Development Block Grant Funding Allocation Formula, presented to U.S. House of Representatives, Committee on Government Reform, Subcommittee on Federalism and the Census, April 26, 2005. www.napawash.org/resources/testimony/4-26-05CommunityDevelopment.pdf

Staff Report, Integrating CDBG Performance Measures into IDIS, National Academy of Public Administration, February 2005.
http://71.4.192.38/NAPA/NAPAPubs.nsf/9172a14f9dd0c36685256967006510cd/c5c7bf5c8eab9f0e85256fc70070bfd9?OpenDocument

Panel Report, Developing Performance Measures for the CDBG Program, National Academy of Public Administration, February 2005.
http://71.4.192.38/NAPA/NAPAPubs.nsf/9172a14f9dd0c36685256967006510cd/c5c7bf5c8eab9f0e85256fc70070bfd9?OpenDocument

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Testimony of the National Association of Housing and Redevelopment Officials

Before the House Government Reform Subcommittee on Federalism and the Census

June 27, 2006

"Moving the CDBG Program Forward: A Look at the Administration's Reform Proposal. Where Do We Go From Here?"

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On behalf of the National Association of Housing and Redevelopment Officials (NAHRO), thank you for the opportunity to provide written testimony concerning the U.S. Department of Housing and Urban Development's (HUD's) recently released legislative proposal to reform the Community Development Block Grant (CDBG) program.

In testimony presented at the Subcommittee's April 2005 hearing on HUD's CDBG formula study, NAHRO took the position that it would oppose any proposal to alter the CDBG formula structure that would result in an immediate and radical redistribution of funds. That is still our position, and we believe HUD's CDBG Reform Act of 2006 fails to meet that test.

We of course remain supportive of the notion of an equitable distribution of CDBG dollars. If Congress feels change is indeed necessary, it remains our hope that change could happen in a way that mitigates uncertainty and avoids sudden and substantial losses in funding for all existing CDBG grantees. Again, it is our opinion that HUD's proposal falls short in that regard. In fact, under the minimum threshold provision of the CDBG Reform Act of 2006, 312 existing entitlement communities would lose 100% of their current CDBG allocation within two years of implementation.

This statement is not intended as a comprehensive review of the Administration's proposal. Instead, NAHRO sees this statement as an opportunity to review a handful of components within the proposal that are of particular concern to our membership and to the broader community of CDBG grantees.

NAHRO believes that a careful examination of the Department's public statements is needed to discern the Administration's true intent regarding CDBG program reform. HUD Secretary Alphonso Jackson has argued that "communities with the greatest needs deserve more funding compared to relatively less needy places."[1] This is quite different than arguing that needy communities deserve increased allocations relative to their own most recent awards. In reality, the Department's proposed legislation reveals quite clearly that this Administration believes very few communities actually deserve a larger CDBG formula grant than they currently receive.

The True Fiscal Impact of the CDBG Reform Act of 2006

NAHRO is concerned that the Department's public statements do not match the reality of its legislative proposal. The most obvious example is related to the Administration's proposal to slash block grant formula funding by approximately 25 percent for Fiscal Year (FY) 2007.

[1] U.S. Department of Housing and Urban Development, "HUD Offers Proposal to Reform Community Development Block Grant Program," News Release, May 25, 2006, http://www.hud.gov/news/release.cfm?content=pr06-056.cfm.

By way of background, both the Administration's FY 2007 budget proposal and the proposed CDBG Reform Act of 2006 posit $2.975 billion in total funding for the CDBG program for FY 2007. After accounting for a $200 million set-aside for competitive "challenge grants" as proposed by HUD, just $2.775 billion would be available for CDBG formula grants, a 25 percent reduction over the FY 2006 appropriated level of $3.711 billion. The relevant text of the CDBG Reform Act of 2006 reads as follows:

> **SEC. 7. AUTHORIZATION OF APPROPRIATIONS.**
> "(a) IN GENERAL.—There are authorized to be appropriated to carry out Title I of the Housing and Community Development Act of 1974 (42 U.S.C. 5301 et seq.), $2,974,580,000, for fiscal year 2007 and such sums as may be necessary for each fiscal year thereafter.
> "(b) CHALLENGE GRANTS.—Of the amount specified in subsection (a), up to $200,000,000 shall be for fiscal year 2007 and such sums as may be necessary for each fiscal year thereafter."[2]

Because the Administration's proposal to cut formula funding by 25 percent is enshrined in the text of the CDBG Reform Act of 2006, the decision not to support the proposal is an easy one.

Recent comments by Secretary Jackson are revealing with respect to the true impact of the proposal on CDBG grantees. Secretary Jackson, testifying before the House Appropriations Subcommittee on Transportation, Treasury, HUD, the Judiciary and the District of Columbia on March 14, 2006, offered the following argument in favor of formula change:

> "But there are certain cities that clearly in our mind do not need community development block grant programs. They can fund many of these programs themselves.
>
> I always like to use the city that I'm from, because I don't like to use somebody else's city, Dallas, Texas. Dallas, Texas, has been funding housing inspections by their city workers for the last 20 years out of block grants. I don't think that's appropriate. I think block grant is to create infrastructure, to work with cities to build economic development so that the cities will be better off.
>
> There are cities that are very, very devastated that I think really need the money, and not necessarily the cities of Dallas or Palm Beach, for those purposes.
> But I think the key, as I said to the chairman a few minutes ago, is for us to go and reexamine the way we're allocating block grant funds at this point.
>
> We're not doing it based on need; we're doing it based on a formula that was set up in 1974. And that formula today -- it's not specific as it was then.

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[2] U.S. Department of Housing and Urban Development, "The CDBG Reform Act of 2006," http://www.hud.gov/content/releases/pr06-056act.pdf.

> Because -- you know, maybe the best example I can give you may be Palm Beach wasn't as rich as it was in 1974. Today, it is extremely rich. But it receives block grant funds.
>
> But Akron, Ohio, is suffering tremendously. And they're getting less than we perceive that they would need to bring the industry back, to bring the economic development back.
>
> So I think that if we are going to use our money wisely, we should zero in on those cities that are hard hit and say, "Let's try to bring them back. Let's try to bring the economy back. Let's bring the job market back there and give them incentives for doing it."[3]

It is instructive to compare the Secretary's remarks to the reality of HUD's legislative proposal. Let us first examine a scenario in which HUD's proposed formula revision is adopted while overall funding for the CDBG formula program remains constant at the FY 2006 appropriated level. Under this scenario, and according to HUD's own data[4], Akron's allocation would in fact *decline* by 16 percent, from $6.990 million to $5.842 million. Meanwhile, Dallas's allocation would *increase* by 21 percent, from $17.983 million to $21.687 million.

Consider a second scenario in which HUD's proposed formula revision is adopted and CDBG formula grants are funded at $2.775 billion, the level proposed by Administration in its FY 2007 budget as well as the funding level at which the CDBG Reform Act of 2006 seeks to authorize formula funding for FY 2007. Under this scenario, in which HUD achieves both the proposed formula revision and a 25 percent cut to overall formula funding, Akron's allocation would decline by a total of 38 percent compared to FY 2006, falling from $6.990 million to $4.365 million. Importantly, Dallas, supposedly a "winner" under HUD's proposal, would see its allocation fall 10 percent from $17.983 million to $16.204 million.

Secretary Jackson's testimony notwithstanding, HUD's internal analyses consider both Akron and Dallas to be high-need communities. HUD categorizes Akron as an 8 and Dallas as a 9 (out of a maximum need score of 10) using its Needs Decile, a rating factor based on the community development needs index developed by the Department for its February 2005 report on CDBG formula targeting. As previously mentioned, if the

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[3] "House Appropriations Subcommittee on Transportation, Treasury, HUD, the Judiciary and the District of Columbia Holds Hearing on FY 2007 Appropriations," Congressional Transcripts, CQ Transcriptions, March 14, 2006.

[4] HUD has provided interest groups with two tables demonstrating the impact of its legislative proposal on CDBG grantees. The first table, "Proposed CDBG Formula Legislative Change with FY 2006 Appropriation Held Constant," assumes adoption of the Department's proposed formula revisions with funding for formula grants held constant at the FY 2006 appropriated level. The second table, "Proposed CDBG Formula Legislative Change with FY 2006 and FY 2007 Appropriation," shows grantee's projected FY 2007 allocations assuming adoption of HUD's formula change proposal, with overall program funding set at the level proposed in the administration's FY 2007 budget request. In an email to interest groups, a HUD official wrote that the second table "illustrate(s) the full effect of the CDBG reform combined with the FY 2007 funding request."

CDBG Reform Act of 2006 were to be enacted exactly as presented by the Department, then both of these high-need communities would experience a net loss in CDBG formula funding. Their plight would be shared by a number of communities categorized by HUD as high-need.

Assuming level funding for CDBG formula grants, 83 of the 284 grantees rated as 8, 9, or 10 on HUD's Needs Decile would see their formula allocations decrease under HUD's proposed formula revision. For example, St. Louis, Missouri, with a rating of 10 on the Needs Index, would see its CDBG formula allocation decline by 31 percent.

Even more illuminating is an examination of the consequences for America's neediest grantees (as defined by HUD) that assumes adoption of the proposed formula change in combination with a 25 percent cut to overall formula funding. In other words, what would happen to the grantees HUD considers America's neediest if the Administration were to get everything it wants?

Under this scenario, 203 of the 284 grantees with HUD Needs Decile scores of 8, 9, or 10 experience a net loss in formula funding as compared to their FY 2006 grant. Another 15 of the neediest grantees (8, 9, or 10 on the Needs Decile) would lose their entitlement status altogether under the minimum threshold provision of HUD's proposal. Only 61 of the nation's neediest grantees gain enough under the formula revision to achieve a net gain in funding after the application of a 25 percent cut to overall formula funding.

In the State of Ohio, for example, all eleven existing entitlement communities scored 8, 9, or 10 would experience a net loss in funding were HUD's legislative proposal to be implemented exactly as written..

Impact of CDBG Reform Act of 2006 on Neediest Ohio Grantees

Grantee	Needs Decile*	FY 2006 Grant ($000)**	FY 2007 Grant ($000) *(Proposed)***	Change (%)**
Akron	8	$6,990	$4,365	-38%
Cincinnati	9	$13,745	$7,912	-42%
Cleveland	10	$24,573	$16,072	-35%
Dayton	9	$6,505	$4,099	-37%
Lima	9	$1,256	$1,030	-18%
Lorain	8	$1,295	$1,136	-12%
Springfield	8	$2,040	$1,193	--42%
Steubenville	9	$768	$0	-100%
Toledo	8	$8,109	$5,995	-26%
Warren	9	$1,347	$874	-35%
Youngstown	10	$4,144	$2,332	-44%

*Needs Decile from "Proposed CDBG Formula Legislative Change with FY 2006 Appropriation Held Constant" (HUD)
**Grant information from "Proposed CDBG Formula Legislative Change with FY 2006 and FY 2007 Appropriation" (HUD). Assumes $2.775 billion for the CDBG formula grant program.

The same phenomenon holds for the State of Pennsylvania, where all 19 existing entitlement communities scored 8, 9, or 10 would experience a net loss in funding were HUD's legislative proposal to be implemented exactly as written. Note that 15 of these

19 neediest communities would lose funding under the formula revision even in a level-funding environment

Impact of CDBG Reform Act of 2006 on Neediest Pennsylvania Grantees

Grantee	Needs Decile*	FY 2006 Grant ($000)**	FY 2007 Grant ($000) *(Proposed)***	Change (%)**
Allentown	9	$2.830	$2,298	-19%
Bethlehem	8	$1,723	$1,047	-39%
Chester	10	$1,483	$1,059	-29%
Easton	8	$986	$517	-48%
Erie	8	$3,640	$2,270	-38%
Harrisburg	10	$2,153	$1,461	-32%
Johnstown	9	$1,625	$761	-53%
Lancaster	9	$1,842	$1,418	-23%
Lebanon	8	4870	$471	-46%
McKeesport	10	$1,258	$680	-46%
Norristown	9	$1,051	$694	-34%
Philadelphia	10	$53,732	$44.046	-18%
Pittsburgh	9	$17,169	$7,315	-57%
Reading	10	$3,185	$2,644	-17%
Sharon	8	$706	$0	-100%
State College	8	$735	$0	-100%
Wilkes-Barre	8	$1,996	$911	-54%
Williamsport	9	$1,299	$701	-46%
York	9	$1,749	$1,271	-27%

*Needs Decile from "Proposed CDBG Formula Legislative Change with FY 2006 Appropriation Held Constant" (HUD)
**Grant information from "Proposed CDBG Formula Legislative Change with FY 2006 and FY 2007 Appropriation" (HUD). Assumes $2.775 billion for the CDBG formula grant program.

It is admittedly true that a number of grantees would receive larger allocations under HUD's revised formula if the Congress were to provide level funding for the CDBG formula program. Once again, however, it is necessary in our opinion to consider the totality of HUD's legislative proposal. The reality of the proposal is that across the nation, a considerable number of those grantees that "win" under HUD's proposed formula revision would in fact lose funding were the Congress to enact the Administration's preferred funding level for CDBG formula grants.

As a final example, consider the following excerpt from written testimony provided by HUD Assistant Secretary Pamela H. Patenaude during a House Financial Services Subcommittee on Housing and Community Opportunity held April 12, 2006, in Los Angeles, CA:

> "For example, here in California, the cities of Santa Monica and Santa Maria have approximately the same population. Under the current formula, they both receive about 1.3 million dollars. However, in terms of need, they are very different. Santa Monica, with a per capita income of $43,000, has a relatively low level of distress while Santa Maria, with a per capita income of only $14,000 has significantly more distress and thus has greater community development needs.

> Under the formula the Administration will propose, Santa Maria's grant would increase to $1.6 million while Santa Monica's grant would fall to $750,000.
>
> I think we can all agree it is critical to restore equity to the distribution of funds to improve targeting and preserve the fairness of the CDBG program."[5]

Santa Monica received a CDBG formula grant in the amount of $1.382 million for FY 2006, while Santa Maria received $1.307 million. If Congress were to adopt the Administration's proposal exactly as written, Santa Monica's grant would in fact fall to $558,000, while Santa Maria's grant would fall to $1.180 million. In order to "restore equity to the distribution of funds," the Administration's preferred solution is to reduce Santa Monica's grant by 60 percent while cutting Santa Maria's grant by 10 percent.

Eliminating Section 108, BEDI, and RHED

The Department's press release announcing its proposal stated that

> "The CDBG Reform Act...seeks to consolidate several programs that duplicate the broad program goals of CDBG. Those programs include: Brownfields Economic Development Initiative (BEDI); Rural Housing and Economic Development (RHED) Program; and, Section 108 Loan Guarantee Assistance Program."[6]

In reality, HUD's proposed legislation does not specifically reference the Section 108, BEDI, and RHED programs, all of which received no funding under the President's proposed FY 2007 budget. Although the administration has proposed eliminating these programs for a number of years, the FY 2007 budget proposal creatively portrays their elimination as a consolidation of the programs within CDBG. The administration has argued these programs "duplicate the broad program goals" of the CDBG program and are therefore unnecessary. NAHRO disagrees.

Consider the Section 108 program, which allows an entitlement community to borrow up to five times the amount of its most recent CDBG formula allocation. In HUD's own words, Section 108 "provides communities with a source of financing for economic development, housing rehabilitation, public facilities, and large-scale physical development projects," making the program "one of the most potent and important public investment tools that HUD offers to local governments."[7] HUD describes Section 108 as a program that allows grantees to "transform a small portion of their CDBG funds into

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[5] "Written Statement of Assistant Secretary Pamela H. Patenaude, U.S Department of Housing and Urban Development," April 12, 2006, http://financialservices.house.gov/media/pdf/041206php.pdf.
[6] U.S. Department of Housing and Urban Development, "HUD Offers Proposal to Reform Community Development Block Grant Program," News Release, May 25, 2006, http://www.hud.gov/news/release.cfm?content=pr06-056.cfm.
[7] U.S. Department of Housing and Urban Development, "Section 108 Loan Guarantee Program," http://www.hud.gov/offices/cpd/communitydevelopment/programs/108/index.cfm.

federally guaranteed loans large enough to pursue physical and economic revitalization projects that can renew entire neighborhoods."[8]

During the May 25 interest group briefing HUD officials conceded that even with the adoption of the administration's legislative proposal, the CDBG program would be unable to duplicate the leveraging potential created through the Section 108 program. As an alternative, HUD officials suggested that local governments could turn to the proposed "Challenge Grant Fund" as an alternative source of funding for large-scale projects in the absence of Section 108 loans. However, with challenge grants awarded competitively and capped at 50 percent of a grantee's annual formula allocation, even under the best of conditions it would take a grantee a minimum of ten years to secure challenge grant funding equivalent to a maxed-out Section 108 loan.

Targeting Poverty with Greater Precision

HUD's February 2005 report on the CDBG formula included strategies for addressing the so-called "college town phenomenon," a reference to the fact that many college and university towns benefit under the current formula structure due to resident college students being counted as persons living in poverty, even though the parents of many of these students support them financially.

To correct for this "college town phenomenon," HUD in its report proposed using the number of persons in poverty living in a family or elderly household instead of the broader measure of the total number of persons in poverty. In our April 2005 testimony, we referenced a conversation with Dr. Steve Barton, the Director of Housing for Berkeley, California. Dr. Barton had pointed out that the measure proposed by HUD discounts single non-elderly non-student persons living in poverty, especially homeless persons and persons living with disabilities. To their credit, HUD has since conceded that criticism of this proposed variable was valid.

The CDBG Reform Act of 2006 attempts anew to rein in the so-called "college town phenomenon." We are encouraged that HUD has chosen to respond to constructive criticism in a constructive manner. However, the Department's legislative language does not appear to target college students with the precision suggested by the Department's press release, excerpted here:

> "CDBG's formula currently rewards towns with large college student populations by including the incomes of these full-time dependent students in calculating poverty. As a result, the poverty rates in these college and university towns appear high. By excluding the incomes of full-time dependent students who are

[8] Ibid.

> financially supported by their parents, the poverty rate in these college towns drops to a level which is much more reflective of that community's actual need."[9]

Meanwhile, the relevant formula variable in the legislation is described as the ratio between:

> "...the extent of poverty, excluding unrelated individuals enrolled in college, in that formula grantee and the extent of poverty, excluding unrelated individuals enrolled in college, in all formula grantees;"[10]

HUD's intent notwithstanding, the legislative language does not appear to draw a distinction between full-time students and part-time students, nor does it distinguish students who are dependents from those who are not.

Final Thoughts

As Congress considers CDBG formula change, it should endeavor to employ a process that reduces ambiguity and provides some measure of confidence for communities as they consider future Consolidated Planning. A rush to implement the Administration's proposal would be far from prudent in NAHRO's opinion.

The introduction of a proposed formula revision in concert with a proposal to slash formula funding by 25 percent creates the potential for enormous uncertainty within those state and local agencies that administer the CDBG program. This uncertainty is exacerbated by the looming introduction of 2010 Census data as well as the tenuous status of the American Community Survey. Instead of being able to rely upon a reliable and consistent future funding stream, for many CDBG grantees the contemplation of future allocations has in recent years become fraught with confusion and pessimism.

NAHRO is encouraged by the efforts of the Government Accountability Office (GAO) to seek out the counsel of public interest groups that represent CDBG grantees and community development practitioners as it works toward completing a report on the current CDBG formula structure's efficacy. If these efforts continue in earnest, then the GAO report could form the foundation for further Congressional examination of the process by which CDBG formula grants are allocated.

Sine the final report is expected no earlier than the summer of 2007, NAHRO encourages Congress to refrain from taking any action on the formula until it has had the opportunity to examine the GAO's findings. As always, NAHRO believes any effort to alter the

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[9] U.S. Department of Housing and Urban Development, "HUD Offers Proposal to Reform Community Development Block Grant Program," News Release, May 25, 2006, http://www.hud.gov/news/release.cfm?content=pr06-056.cfm.

[10] U.S. Department of Housing and Urban Development, "The CDBG Reform Act of 2006," http://www.hud.gov/content/releases/pr06-056act.pdf.

existing CDBG formula structure must originate within the appropriate House and Senate committees of jurisdiction.

Although we have strong objections to many of the provisions contained within the CDBG Reform Act of 2006, NAHRO appreciates very much the manner in which the Department's Office of Community Planning and Development (CPD) has provided information related to the proposal. Beginning with the March 25 briefing, the willingness of CPD (led by Assistant Secretary Patenaude) to ensure that interest groups are fully informed has been a model of transparency and forthrightness the rest of the Department would do well to emulate.

Finally, we acknowledge the continuing efforts of our partners within the coalition of organizations dedicated to preserving funding for the CDBG program. Many of these organizations have come together to submit their own joint statement for today's hearing, and we wish to express our agreement with the sentiments they have expressed. Indeed, NAHRO has served by their side in the development of CPD's important new performance measurement framework, the implementation of which represents true and meaningful programmatic reform. We are also proud of the role NAHRO played in the development of the survey[11] of CDBG grantees referenced in our partners' statement.

Once again, thank you for the opportunity to share some of our thoughts on the CDBG Reform Act of 2006. As you move forward, NAHRO again encourages you to continue to employ a fully deliberative process that includes ongoing participation and input from local and state governments, public interest groups, and community development professionals. If NAHRO can be of further assistance to the Subcommittee in the future, please do not hesitate to call upon us.

[11] "Consequences for American Communities: A national survey on the impact of recent reductions in Community Development Block Grant Funding," March 12, 2006, http://www.nahro.org/cdbg_survey.cfm.

STATEMENT BY

U.S. CONFERENCE OF MAYORS
NATIONAL ASSOCIATION OF COUNTIES
NATIONAL LEAGUE OF CITIES
NATIONAL ASSOCIATION OF LOCAL HOUSING FINANCE AGENCIES
NATIONAL ASSOCIATION FOR COUNTY COMMUNITY AND ECONOMIC DEVELOPMENT
NATIONAL COMMUNITY DEVELOPMENT ASSOCIATION

TO THE

SUBCOMMITTEE ON FEDERALISM AND THE CENSUS

HOUSE COMMITTEE ON GOVERNMENT REFORM

HEARING ON

THE BUSH ADMINISTRATION'S "COMMUNITY DEVLOPMENT BLOCK GRANT REFORM ACT OF 2006"

JUNE 27, 2006

The U.S. Conference of Mayors (USCM), National Association of Counties (NACo), National League of Cities (NLC), National Association of Local Housing Finance Agencies (NALHFA), National Association for County Community and Economic Development (NACCED), and the National Community Development Association (NCDA) appreciate the opportunity to present this joint Statement to the House Subcommittee on Federalism and the Census regarding the Bush Administration's proposed "Community Development Block Grant Reform Act." We wish to state at the outset that we do not support this proposal.

As we told the Subcommittee last year at its hearing on the Administration's "Strengthening America's Communities Initiative," CDBG is arguably the Federal Government's most successful domestic program. Its success stems from its utility, i.e. providing cities, counties and states with flexibility to address their unique affordable housing, neighborhood revitalization and economic development needs. Based on HUD's most recent data in 2004 alone the CDBG program *assisted over 23 million persons and households.*

CDBG has been performing at a high level for 30 years, and it continues to produce results. In fact, according to HUD, more than 78,000 jobs were created or retained by CDBG in FY 2004. In addition, in FY 2004, 159,703 households received housing assistance from CDBG. Of this amount 11,000 became new homeowners, 19,000 rental housing units were rehabilitated and 112,000 owner occupied homes were rehabilitated. In FY 2004, over 9 million persons were served by new or reconstructed public facilities and infrastructure, including new or improved roads, fire stations, libraries, water and sewer systems, and centers for youth, seniors and persons with disabilities from CDBG funds. In addition, more than 13 million persons received assistance from CDBG-funded public services in FY 2004, including employment training, child care, assistance to battered and abused spouses, transportation services, crime awareness, and services for seniors, the disabled, and youth. In addition, over time grantees provided CDBG-funded loans to businesses located in distressed neighborhoods, with minority businesses receiving approximately 25% of the loans.

CDBG has been achieving results like this throughout its history. An analysis performed by Professor Stephen Fuller of George Mason University in 2001 shows that over the first 25 years of the program CDBG-funded projects created 2 million jobs and contributed over $129 billion to the Gross Domestic Product (GDP).

CDBG has Already Been Reformed

As the Subcommittee is aware, in 2004 a number of the practitioner groups, NACCED, NALHFA, NAHRO, and NCDA, devoted substantial resources to a working group that included representatives of the Office of Management and Budget and the Department of Housing and Urban Development with the aim of developing a Performance Outcome Measurement system. What emerged from the efforts of this working group was a *consensus* framework and specific outcome measures to evaluate the performance of the Community Development Block Grant (CDBG) program, the HOME Investment

Partnerships Program (HOME), the Housing Opportunities Program for Persons With Aids (HOPWA) program, and the Emergency Shelter Grants (ESG) program. HUD is now in the process of implementing the Performance Measures system. This is the real *reform* of the CDBG program. It will finally provide aggregate national data on the many accomplishments of CDBG and the other three formula grant programs.

In its proposal, HUD maintains that statutory language is needed to enforce the performance measurement system now being implemented. It proposes the following:

- Authorizing the Secretary to establish performance measures and accountability standards for formula grantees;
- Requiring, prior to the receipt of grant funds, that a formula grantee submit a Performance Plan to the Secretary for review and approval, including:
    - A statement and a description of the grantee's community development needs and objectives;
    - A projected use of funds; and
    - A list of performance measurement objectives for each of the projects or activities to be funded prospectively with CDBG funds.
- Requiring a grantee to submit to the Secretary, and make available to the public, a report containing:
    - Information documenting the performance outcomes of activities or projects;
    - The nature of, and reasons for, changes in program objectives;
    - Indications of how the formula grantee would change its programs as a result of its experiences;
    - An evaluation of the extent to which funds were used to serve low- and very low-income persons;
    - A summary of public comments received on specific programs; and
    - Information about the procedures that the formula grantee uses to collect and verify data submitted to the Secretary.
- Directing the Secretary to perform a periodic review of the grantee's progress and provide that if a grantee failed to meet its performance measurement objectives and outcomes in a 24-month period, the Secretary could reduce or limit the grantee's access to CDBG funds; the grantee would be required to submit a plan that outlines steps it would take to improve its future performance.

In a briefing for our organizations, HUD maintained that the purpose of this addition to the statute is to put teeth behind the performance measures system now being implemented. HUD hopes this will encourage grantees that aren't reporting accurate and timely data to begin doing so. HUD staff says establishing a review process and defining "lack of progress" would have to be done very slowly and cautiously. It is doubtful that Congress would give HUD the authority to withhold a grantee's funds.

Is this statutory change necessary? We don't believe so. Our members believe that there is a need for a performance measurement system and have embraced the system that HUD is now implementing. Providing a statutory requirement is, in our view, redundant.

Formula Reform

HUD's legislative proposal call for "reform" of the CDBG formula including the following:

- Eliminating the 70/30 funding split between entitlement cities and counties and states
- Removing the $7 million set-aside for insular areas, instead reserving .19% of the appropriations amount for insular area grantees
- Basing the formula on the following factors:
    - Number of persons living in poverty, excluding unrelated individuals enrolled in college (50%)
    - Number of female-headed households with children under eighteen (10%)
    - Extent of housing overcrowding (10%)
    - Number of housing units 50 years or older and occupied by a household living in poverty (30%)
- Adjusting the formula by the ratio of per capita income of the MSA to the per capita income of the formula grantee, with caps such that no grant is adjusted by more than 25 percent
- Requiring a minimum allocation threshold of .014 percent of the total amount allocated; if any current entitlement does not meet the minimum allocation threshold requirement, this grantee would receive 50 percent of their grant amount for the first year after enactment before being eliminated as an entitlement the following year

HUD maintains that this formula modification is about fairness. HUD also believes that the introduction of a minimum allocation threshold requirement – weeding out smaller metropolitan cities and urban counties with less poverty – would foster a more regional approach to CDBG programs. According to the FY 2006 appropriation, the .014% threshold requirement would be the equivalent of $518,000. There are currently 312 city and urban county entitlements that receive less than this amount, and thus, they would be denied direct funding.

It's no surprise that the CDBG formula has not changed since 1977. The difficulty of making a change is finding a new formula that can garner enough votes to pass the House and Senate. Fairness is in the eye of the beholder. For example, under the Administration's proposal applied to the FY 2006 appropriation, 10 communities in Ohio that now receive direct entitlement funding would lose their eligibility and have to compete for funding from the State. Of the remaining entitlements, 23 would see their entitlement grants reduced, some by as much as 65% (Cleveland Heights and Lakewood), while 9 would receive increases, one by as much as 70% (Columbus). Dayton would lose 16% of its grant. In Pennsylvania, 10 communities that are currently receiving direct funding would have to compete for grants from the State under the Administration's proposal. Thirty-one entitlement cities and counties in Pennsylvania would receive smaller grants, one by as much

as 53% (Allegheny County) and one by 43% (Pittsburgh), while four entitlement communities would see modest increase of 3-10% (Philadelphia).

If Congress decides to change the CDBG formula, which we do not support, the only way to prevent losers is to appropriate more money. That is highly unlikely given the current fiscal situation.

Bonus Funding Pool

The HUD "reform" proposal also contains a bonus funding pool called "Economic Development and Revitalization Challenge Grants," a $200 million pot of funds for which entitlement and non-entitlement cities and counties would compete. These grants are intended to provide an incentive to communities to demonstrate results in improving the livability of distressed neighborhoods for its citizens through the targeted use of grant funds and other public and private resources. Other features of the proposal include:

- A grantee must have a population with a minimum poverty rate at least half the national poverty rate;
- In the previous year, a grantee must have expended at least 40% of its last grant amount for activities in Neighborhood Strategy Revitalization Areas (NSRAs);
- For any previous challenge grants received, the grantee must have expended at least 40% of its prior year's grant and 100% of the grant received 24 months prior;
- The grantee must have an operational performance measurement system that shows results and achievements from activities carried out in NSRAs;
- Criteria to score eligible grantees include:
    - Concentration of public funds and leveraged private investment in designated NSRAs;
    - Relative improvement in expanding economic opportunities for low-and moderate-income households within its NSRAs in past five years;
    - Indicators that measure the NSRA's viability for redevelopment and the entity's ability to implement effective strategies to improve economic opportunity and livability within the NSRA;

- Funds will be awarded as follows:

    - Grants will be allocated as a percentage of a grantee's formula grant;
    - Grantees with higher scores shall receive a larger percentage of bonus funds than those with lower scores;
    - No grantee shall receive a bonus grant greater than 50% of its formula grant;
- Funds must be used in NSRAs for activities that expand economic opportunity; funds may be used to create affordable housing if this is part of the grantee's strategy to expand economic opportunity.

Grantees would not actually apply for these grants; HUD would analyze eligibility and scoring criteria through data collected in the Integrated Disbursement Information System (IDIS). The theory behind this bonus fund is to incentivize grantees to achieve certain

outcomes by rewarding them, but without limiting the kinds of activities that can be undertaken with formula funds.

Unfortunately, the funding for this program comes out of the CDBG formula; it is not a separate program. The proposed FY 2007 appropriation for this bonus fund is $200 million. We are strongly opposed to the diversion of limited formula funds for this purpose.

Program Elimination

The final element of HUD's "reform" proposal is the elimination of three programs: Section 108 Loan Guarantees, the Brownfields Economic Development Initiative (BEDI), and the Rural Housing and Economic Development programs. The rationale for this program elimination is that most of the activities can be carried out with CDBG funds, with the exception, of course, of the tremendous leveraging opportunities that the Section 108 program provides.

Section 108 provides cities and counties with a source of financing for large scale affordable housing, economic development, and public facilities projects. The program allows CDBG grantees to leverage a portion of their CDBG entitlement grants to undertake projects on a scale that can transform neighborhoods. Section 108 funding is often the catalyst to entice private sector funding to distressed neighborhoods in need of revitalization. In 2005, HUD approved 55 Section 108 project applications. Of the $336 million total that was approved, $194.7 million went to economic development projects that created or retained 9,922 jobs, $212.7 million supported housing rehabilitation projects, and $119.2 million went to public facility and improvement projects. This activity would not be possible if communities had to rely solely on their annual entitlement grants.

Section 108 loans are often coupled with Brownfields Economic Development Initiative (BEDI) grants to spur the reclamation of brownfields. BEDI grants can be used to pay predevelopment costs of a Section 108 project, and the can also be used as a loan loss reserve to write down interest rates, or establish a debt service reserve. Both of these programs complement and enhance CDBG; they don't duplicate CDBG. They should not be terminated.

CDBG Funding

Finally, we wish to comment on formula funding for CDBG. We complement the Chairman and members of the Subcommittee for their leadership in preserving CDBG, at HUD, during the previous session of the 109th Congress. The price paid for this victory was a heavy one, with formula funding cut from the FY 2005 level of $4.1 billion to $3.71 billion. This was on top of the $200 million cut in FY 2005.

Earlier this year, our organizations, along with two others, surveyed our members to quantify the impact of the cuts to the formula grant portion of the program from FY 2004 to FY 2006. Here is what we found:

- 5,064,408 fewer low- and moderate-income persons would be served nationwide as a result of cuts to the CDBG program from FY 2004 to FY 2006.

- 5,588 fewer businesses would be assisted, 14,881 fewer jobs would be created, and 3,345 fewer jobs would be retained.

- 5,843 fewer households would be assisted through homebuyer assistance activities, including a total of 2,533 first-time homebuyers, and 1,828 minority households.

- 255,569 elderly and 391,823 children would fail to receive public services that are routinely funded with CDBG funds, such as meals on wheels, improvements to nursing homes, child care, and after school enrichment programs.

- 253,187 fewer persons with special needs would be served, along with 196,150 fewer homeless persons.

- 1,251 new city and county public improvement projects would be cancelled or delayed, such as street and sidewalk improvements, water and sewer systems, fire stations, public facilities, and the remediation of environmental contamination.

Survey respondents included grantees in 43 states and the Commonwealth of Puerto Rico; representing 30 percent of all CDBG formula grantees, including 68 percent of all state programs and 28 percent of all entitlement cities and counties.

We were very pleased that H.R. 5576 passed by the House earlier this month contains a $200 million increase in CDBG formula grants to $3.9 billion for FY 2007. We thank the members who voted for this important increase. We will continue our efforts in the Senate to achieve a significant increase in formula grants at part of its version of the FY 2007 Transportation, Treasury, and Housing and Urban Development appropriations bill.

Thank you.