



U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
Community Planning and Development

Special Attention of:

CPD Division Directors
State CDBG Grantees

Notice CPD-06-11

Issued: October 24, 2006
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SUBJECT: Guidance on Preparation of the State CDBG Method of Distribution in Accordance with the Final Consolidated Plan Rule dated February 9, 2006.

I. Method of Distribution

This Notice provides policy guidance to states to aid in the preparation of an acceptable Method of Distribution (MOD) for the use of State CDBG funds in accordance with the requirements of 24 CFR 91.320(k)(1)(i) and 24 CFR 570.490(a)(2). These regulations were revised on February 9, 2006, in response to many comments by states that the previous regulations were unclear on what was required to be in the MOD and whether HUD had the right to monitor a state's MOD after the state's Consolidated Plan had been approved. The final rule clearly states that the MOD needs to provide sufficient information so that units of general local government (UGLG's) will be able to prepare responsive applications. The regulation says that the MOD **shall** contain a description of **all** criteria used to select applications from local governments for funding including relative importance of the criteria. The MOD must include a description of how all CDBG resources will be allocated among funding categories and the threshold factors and grant size limits that are to be applied. The final rules also states in 24 CFR 91.320(k)(1)(i) that HUD may monitor the MOD as part of its audit and review responsibilities in order to determine compliance with program requirements.

Section 24 CFR 91.320(k)(1)(ii) of the final rule provides that if the state intends to help UGLG's apply for Section 108 loan guarantee funds, the state must describe the available Section 108 loan guarantee amounts and the selection process in its MOD. Likewise, if the state intends to allow UGLG's to implement community revitalization strategies, the MOD must reflect the state's process and criteria for approving the locality's revitalization strategy.

A state is free to design its MOD according to the state's vision on how CDBG funds should be distributed within the state, consistent with the State CDBG program requirements. HUD has no desire to influence the state's decision-making process. HUD's only interest is to ensure that the state's selection process is clear so that units of general local government will know the criteria the state is using to fund applications.

A major change in the February 9, 2006 Consolidated Plan regulations permits states to provide a summary of their selection criteria in the MOD as long as each of the criteria is summarized and the details are promulgated in application manuals or other official state publications that are widely disseminated to eligible applicants. The selection criteria summary must include a summary of the state's funding thresholds, number of applications allowed per grantee, as well as any grant limits that the state has imposed on the CDBG program. The regulations were changed to recognize the fact that many states use application manuals that provide detailed guidance to potential grantees on how to structure their applications in order to maximize their chances of receiving State CDBG funding and to make it clear that providing the details of the selection process in an application manual is an acceptable process. Use of application manuals can have the effect of streamlining the MOD, as well as allowing the state to make some of the specific decisions on scoring applications at a later time. (Application manuals may also contain extensive materials that are not part of the selection process, such as guidance on how the state expects grantees to administer their grant. This could include guidance on environmental, financial management, relocation and procurement requirements, as well as required certifications, and contract requirements for State CDBG recipients.)

It is important for states to share all selection criteria with units of general local government so that the UGLG will be able to provide a responsive application. For example, if the application guide states that projects with a significant impact will receive 100 points, projects with moderate impact will receive 70 points, projects with low impact will receive 40 points and projects with an insignificant impact will receive 0 points, the state must clearly define the terms significant, moderate, low, and insignificant so that the UGLG's will be able to provide responsive applications. The definitions should include what the state determines impact to be, along with the state's definitions of impact gradation. For example, for a housing rehabilitation project, a state might define significant impact to mean bringing 90-100% of the properties in the target area up to code, moderate impact might mean bringing 70-89% of properties up to code, low impact might mean bringing 50-79% of the properties up to code, and insignificant impact might mean bringing less than 50% of the properties up to code. Another example would be for high impact in a public facilities project to be defined as bringing public water to an area that had not had it in the past, moderate impact would be improving water service and fire protection, by providing a significant increase in the capacity of the system so that it can meet state and federal water and fire protection standards, low impact would be improving a water system for planned future growth over the next 10 years, and insignificant impact would be a project that did not meet any of the aforementioned definitions.

HUD recognizes that states must achieve a balance between the objective and the subjective aspects of their funding process. Even in a selection system that is as objective as possible, states must necessarily make value judgments in establishing how points will be assigned for a given criterion (e.g. how many points should "impact" be worth in the overall rating system, flowing down to what constitutes "significant impact" versus "moderate impact"). HUD is aware that a degree of subjectivity is inherent in some selection systems (e.g. in deciding whether the revitalization of a downtown area is high or medium impact, states can describe what high and medium impact would look like, but ultimately there will be a subjective judgment on the part of the reviewer).

The amount of detail that must be provided in the MOD or application manual will vary with the nature of the state's funding categories, and the application review process used by the state. Less documentation might be needed when there is an open window for economic development funding and the state is willing to give technical assistance throughout the review process to grantees

to help them meet the threshold criteria that is needed for funding, (e.g. provide assistance at a cost of less than \$10,000 per job, and show through financial analysis that the business has a strong chance of being successful). Even less documentation is needed when a state decides to fund all applications that meet a specified threshold, i.e. the state will make grants to abate lead based paint contamination in all units in the target area that contain lead based paint. Competitive application systems such as a competition for water and sewer funding may require more detailed rating and ranking criteria. For example, the criteria should not simply say that leveraging is a factor, as UGLG's would have no way of knowing what the requirements are to receive leveraging points when they submit their funding application. One acceptable scenario would be for the MOD to state that leveraging is defined as a written commitment submitted by the UGLG that states that the entity will supply a specific amount of funds to the project by a date certain. The MOD might further state that the contribution may be either cash or in-kind, and it must be directly related to the project, and be made after the project is approved and has received an environmental release. For projects that meet the leveraging definition, the MOD might state that leveraging is worth up to 20 points of the total of 100, and that applicants with leveraging of 100% or higher will receive 20 points, applicants with 75-99% leveraging will receive 15 points, applicants with 50-74% leveraging will receive 10 points and applicants with below 50% leveraging will receive 0 points.

HUD is not judging the merits or rationale behind the factors that states use to rate and rank applications, just the fact that the factors are clear to potential applicants. To use an extreme example it is allowable for a state to fund applications from UGLG's in the order that the applications were submitted, as long as the state clearly indicates this policy in its MOD and the policy otherwise complies with applicable laws and regulations.

Some states' MODs indicate that higher level officials may review the rating and ranking process before contracts are offered to UGLG's. If the officials are just reviewing the process to ensure that the reviewing team scored projects in accordance with the rating and ranking criteria, there is no requirement to add anything to the MOD. If the officials have the ability to change the rating based on other criteria, (e.g. ensuring that funded projects promote economic development to the greatest extent possible) these criteria, and the weight they will be given, must be shared with the grantees in the MOD and/or the application guide. Language in the MOD stating that "factors to be considered in rating the application include but are not limited to" is unacceptable as UGLG's have no way of knowing what the unstated factors are when the UGLG's are preparing their funding application.

II. Monitoring

Section 91.320(k)(1)(i) states that HUD may monitor the MOD as part of its audit and review responsibilities. HUD uses risk analysis to determine which grantees and programs to monitor. After the HUD field office decides to monitor a specific grantee's program (e.g. CDBG), a decision is made on what area(s) of the program should be monitored. If a field office decides to monitor the state's MOD, the field office will review whether the state is following its MOD as well as whether the MOD meets the requirements of the regulations. During a review of the MOD, the field office will most likely review other state publications that contain information on the state's rating and ranking procedures such as an application manual. Section 91.320(k)(1)(i) of the final rule permits states to provide a summary of the selection criteria, provided that all criteria are summarized and the details are set forth in application manuals or other official state publications that are widely distributed to eligible applicants. If a state chooses to provide the details of its selection criteria in an application manual rather than the MOD, the only way that the Department will be able to review the state's selection criteria is during monitoring. The field office monitor will also want to review the

state's guidance to its reviewers on how to review applications, as well as rating and ranking scoring sheets and other documentation that is used in the rating process. The field office monitor will likely review the state's documentation of its application review and selection process.

Section 570.490(a)(2) provides that the state shall keep records to document its funding decisions reached under its MOD including all the criteria used to select applications from local governments for funding and the relative importance of the criteria (if applicable), regardless of the organizational level (e.g. career staff or political-level officials) at which the final funding decision is made, so they can be reviewed by HUD, the Inspector General, the Government Accountability Office, and citizens. Section 570.493(b) provides that a state's failure to maintain records in accordance with §570.490 may result in a finding that the state has failed to meet the applicable requirement to which the record pertains. Failure to keep proper records on the MOD could result in a finding that the state has failed to follow the MOD requirements of §91.320(k)(1)(i). This reinforces the need for states to have explicit rating and ranking criteria to justify how they are selecting their State CDBG grantees. It is noted that the information collection requirements mandated by §570.490 have been approved by the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501-3520) and assigned OMB control number 2506-0085. In accordance with the Paperwork Reduction Act, HUD may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection displays a currently valid OMB control number.

The purpose of the revision to the MOD requirements is to ensure that the MOD is clear so that UGLG's can prepare responsive CDBG applications to the state and comment on the proposed MOD in the Consolidated Plan. HUD recognizes each state's right to design its MOD to best meet the needs of its citizens residing in the non-entitled areas of the state. The revised Consolidated Plan regulation strikes a balance between providing states with the hallmark flexibility inherent in the CDBG program and requiring states to supply UGLG's with clear guidance on the rating and ranking requirements for the CDBG program.

For any questions about the guidance provided in this memorandum, HUD field staff should contact the State and Small Cities Division on (202) 708-1322; state grantees should contact their HUD Field Offices.