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HUD Section 108 Loan Guarantee Program: An Overview

The Section 108 Loan Guarantee program (Section 108) is one of several Department of Housing and Urban Development (HUD) programs designed to support local community and economic development activities. It is a source of flexible financing for which grantees of the Community Development Block Grant (CDBG) can carry out large-scale projects, by pledging current and future CDBG for a guaranteed loan. HUD considers Section 108 loan guarantee applications on a noncompetitive, rolling basis. Private lenders finance Section 108 loans with a "full faith and credit" guarantee by the federal government.

The Section 108 program shares similar programmatic structure and flexibility with the CDBG program. These factors may position Section 108 as a useful tool for community and economic development as local governments face an uncertain financial future and shifting community development priorities. For instance, Section 108 funds can be used for activities related to long-term disaster recovery or for resilience against future disasters. Section 108 may also emerge as a useful tool for local governments recovering from the economic effects of the Coronavirus Disease 2019 (COVID-19) pandemic.

This In Focus describes availability of and access to program financing, summarizes the Section 108 program structure, discusses annual principal loan amount maximums, and outlines some policy considerations.

Availability of Financing

Section 108 funds are made available to CDBG recipients on an ongoing basis, allowing participating communities to apply for funds anytime during the year. Typically, the qualified loan amount is five times greater than a CDBG grantee's annual allocation (minus any outstanding loan balances), which allows borrowers to maximize program funds for projects that would not necessarily be feasible within a given CDBG program year.

Program Structure and Administration

Like CDBG, the Section 108 program derives its authority from Title I of the Housing and Community Development Act of 1974 (42 U.S.C. §5301 et seq.). CDBG eligibility and program requirements are also generally applicable to Section 108. For more information on CDBG, please see CRS Report R43520, *Community Development Block Grants and Related Programs: A Primer*, by Joseph V. Jaroscak.

Eligible Entities

CDBG entitlement communities, insular areas, and states (on behalf of nonentitlement communities) are eligible to leverage their annual CDBG allocations for Section 108 financing. Recipients of Section 108 loans may execute planned activities directly, or relend the funds to a third party, including private companies, to carry out the eligible activities.

Eligible Activities

All eligible activities must meet one of the three national objectives of the conventional CDBG program:

1. principally benefit low- and moderate-income (LMI) persons;
2. aid in the prevention or elimination of slums or blight; or
3. meet an urgent need by addressing conditions that pose a serious and immediate threat to the health and safety of residents.

As is the case with CDBG program funds, 70% of a borrower's Section 108 loan funds must meet the objective of principally benefitting low- and moderate-income persons. Section 108 activities must also comply with program requirements outlined in 24 C.F.R. § 570 Subpart M, as well as CDBG rules and crosscutting federal regulations (e.g., Davis-Bacon).

The majority of eligible Section 108 program activities fall into one of four broad categories:

1. economic development;
2. public facilities and infrastructure;
3. housing rehabilitation; and
4. debt servicing and related fees.

Though broadly similar, eligible Section 108 activities are somewhat more constrained than CDBG. Unlike CDBG, Section 108 funds cannot be used for public service activities, nonfederal cost share, or long-term planning activities.

Application Process

Prior to submission of a Section 108 application, eligible communities are required to make a draft available for public comment, hold a minimum of one pre-submission public hearing, and address any comments provided (24 C.F.R. §570.704). This process must comply with a local citizen participation plan, developed by the public entity applying for Section 108 funds. This plan may be consistent with the participation plan required in the HUD consolidated planning process. Communities then finalize and submit their application for review and approval by HUD (24 C.F.R. §570.704).

The relevant HUD Field Office and HUD Financial Management Division review Section 108 applications simultaneously. If the application clears review, the Deputy

Assistant Secretary for Grant Programs considers it for approval. In general, HUD attempts to review and approve an application within 45 days, barring any delays associated with programmatic or financial aspects of the application.

Applicants are required to pledge current and future CDBG allocations as a primary form of security for a Section 108 loan. Additional pledges of collateral are required for loans with repayment periods of 10 or more years, or at the discretion of HUD, as outlined in program regulations (24 C.F.R. §570.705(b)(3)).

Funding Process

Upon approval of a Section 108 Loan Guarantee application, HUD generates loan documents and coordinates with the recipient on any necessary revisions. Typically, Section 108 loans are financed initially through an interim variable rate product. Periodically, HUD releases public offerings for permanent financing of Section 108 loans, once a sufficient aggregate amount in loan guarantees has been awarded.

Loan Terms and Repayment

Section 108 loans can be repaid over periods of up to 20 years. Repayment structures may vary depending on the individual project and borrower. The interest rates for Section 108 interim loans are based on the adjusted three-month London Interbank Offered Rate, or LIBOR. Interest rates for loans funded by a public offering are fixed, and are based on U.S. Treasury borrowing rates.

Although borrowers use CDBG grant funds as collateral for Section 108 guaranteed loans, they do not necessarily use the grant funds to pay off the loans. CDBG program activities related to Section 108 loan repayment represented 1.9% of overall program expenditures in FY2020. In many cases, borrowers use Section 108 project revenues or other local resources to pay these costs.

Planning and Program Monitoring

Section 108 borrowers are required to include information on planned activities in their HUD consolidated plans and annual action plans. Additionally, participants must submit annual performance evaluation reports consistent with CDBG program reporting requirements. Like CDBG, borrowers report funding status and accomplishments in HUD's Integrated Disbursement and Information System, or IDIS.

Total Principal Amounts and Credit Subsidies

Typically, Congress sets the maximum level of Section 108 loan commitments in annual appropriations legislation. Over the past five years, the Section 108 principal maximum set by Congress has been $300 million.

If the overall amount of loan commitments reaches or exceeds 50% of the maximum loan commitment amount, HUD can set additional limits on any new individual guarantee amounts (42 U.S.C. 5308(k)(2); 24 C.F.R. §570.705).

In 2015, HUD amended program regulations to allow for the collection of fees from Section 108 borrowers as a credit subsidy for loan guarantees, in lieu of annual appropriations. Since FY2016, Congress has included language in annual appropriations legislation directing the Secretary to set the amounts for credit subsidy fees.

Policy Considerations

As currently administered, the Section 108 program provides communities with access to financing to support large-scale community or economic development projects. Program participants leverage current and future CDBG allocations as the primary asset against which to borrow for such projects, which may generate revenue or enhance local amenities and opportunities.

Although the Section 108 program provides access to flexible community development financing, there may be factors limiting its feasibility as an option for some potential borrowers. HUD reporting indicates that fewer than half of the current eligible state and local governments have borrowed under the Section 108 program since its inception. Past HUD analysis has indicated that potential borrowers may have concerns over the perceived risk of pledging CDBG funds as collateral and its effect on project feasibility. Congress may consider identifying and examining potential barriers for some communities in utilizing Section 108 financing.

Additionally, Congress may wish to identify potential options to enhance access and increase participation in the Section 108 program. In the 1990s, Congress funded and HUD administered competitive Economic Development Initiative (EDI) grants to provide flexible funding for Section 108 to enhance the viability and security of their financed projects. Competitive EDI grants were used for a variety of purposes including establishing reserve funds or covering a range of project costs. HUD has cited an unpublished analysis of EDI from the University of Louisville, suggesting that EDI grants improved Section 108 project feasibility and revenue generation. Congress may consider reauthorizing the competitive EDI program, or other programmatic options that could increase liquidity for borrowers and improve the feasibility of potential Section 108 projects.

On the other hand, creation or reauthorization of additional programs may not be necessary due to the Section 108 program's inherent flexibility. HUD informs Section 108 borrowers of the ability to blend loan funds with other federal resources for community development such as Low-Income Housing Tax Credits, New Markets Tax Credits, and Opportunity Zone tax incentives. Congress may consider options to increase awareness and enhance coordination of such resources to optimize the use of federal resources for large-scale community development projects.

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