

California Code of Regulations  
Title 25, Division 1  
Chapter 7  
Subchapter 19  
Commencing with Section 8300  
Effective date: July 11, 2010

Section 8300.	Purpose and Scope .....	2
Section 8301.	Definitions.....	2
Section 8302.	Restrictions on Demolition .....	5
Section 8303.	Site Control Requirements.....	5
Section 8304.	Unit Standards.....	6
Section 8305.	Tenant Selection.....	7
Section 8306.	Tenant Recertification.....	8
Section 8307.	Rental Agreement and Grievance Procedure.....	8
Section 8308.	Operating Reserves .....	10
Section 8309.	Replacement Reserves .....	12
Section 8310.	Underwriting Standards .....	13
Section 8311.	Limits on Development Costs.....	15
Section 8312.	Developer Fee .....	15
Section 8313.	Reserved.....	16
Section 8314.	Use of Operating Cash Flow.....	16
Section 8315.	Subordination Policy.....	18
Section 8316.	Leasehold Security.....	20

## Section 8300. Purpose and Scope

- (a) These regulations provide uniform standards and program rules for multifamily rental housing developments assisted by the Department of Housing and Community Development. When expressly incorporated by reference, some or all of the provisions of this Chapter shall apply to: the Joe Serna Junior Farmworker Grant (JSJFWHG) Program (Chapter 7, subchapter 3, commencing with Section 7200); the Multifamily Housing Program (MHP) (Chapter 7, subchapter 4, commencing with Section 7300); and the HOME Investment Partnerships (HOME) Program (Chapter 7, subchapter 17, commencing with Section 8200). These regulations interpret and make specific the following Health and Safety Code Division 31, Part 2 statutes applicable to these programs: Chapter 2 (commencing with Section 50517.5); Chapter 16 (commencing with Section 50896), and Chapter 6.7 (commencing with Section 50675).
- (b) These regulations establish terms, conditions and procedures for funds awarded after the effective date of these regulations.

NOTE: Authority cited: Sections 50406(n); 50517.5(a)(1), (2); 50675.1(c); 50675.11; 50896.3(b), Health and Safety Code. Reference: 50517.5, 50675, 50896, 50896.1, and 50896.3 Health and Safety Code, and 24 CFR part 92.

## Section 8301. Definitions

The following definitions govern this subchapter.

- (a) "Assisted Unit" means a Unit that is subject to the Program's rent and/or occupancy restrictions as a result of the financial assistance provided by the Program, as specified in the Regulatory Agreement.
- (b) "CalHFA" means the California Housing Finance Agency.
- (c) "Commercial Space" means any nonresidential space located in or on the property of a Rental Housing Development that is, or is proposed to be, rented or leased by the owner of the Project, the income from which shall be included in Operating Income.
- (d) "CPI" means the Consumer Price Index for All Urban Consumers, West Region, All Items, as published by the Bureau of Labor Statistics, United States Department of Labor.
- (e) "Debt Service Coverage Ratio" means the ratio of (1) Operating Income less the sum of Operating Expenses and required reserves to (2) debt service payments, excluding voluntary prepayments and non-mandatory debt

service. In calculating Debt Service Coverage Ratio, the Department may include all Operating Income, and may exclude Operating Income that cannot be reasonably underwritten by lenders making amortized loans.

- (f) "Department" means the Department of Housing and Community Development.
- (g) "Developer Fee" means the same as the definition of that term in California Code of Regulations, Title 4, Section 10302.
- (h) "Distributions" means the amount of cash or other benefits received from the operation of a Rental Housing Development and available to be distributed pursuant to Section 8314 to the Sponsor or any party having a beneficial interest in the Sponsor or the Project, after payment of all due and outstanding obligations incurred in connection with the Rental Housing Development. Distributions do not include payments for: deferred Developer Fee up to the limit set forth in Sections 8312, approved partnership and asset management fees, mandatory debt service, approved reserve accounts established to prevent tenant displacement resulting from the termination of rent subsidies, operations, maintenance, payments to required reserve accounts, land lease payments to parties that do not have a beneficial interest in the Sponsor entity, or payments for property management or other services as set forth in the Regulatory Agreement for the Rental Housing Development.
- (i) "Eligible Households" for MHP means "eligible household" as defined in Section 7301, for HOME this term means the same as "low income families" as defined in 24 CFR 92.2, and for JSJFWHG this term means the same as "agricultural household" as defined in Section 7202.
- (j) "Operating Expenses" means the amount approved by the Department that is necessary to pay for the recurring expenses of the Project, such as utilities, maintenance, management, taxes, licenses, and the cost of on-site supportive services coordination, but not including debt service, required reserve account deposits, or other supportive services costs.
- (k) "Operating Income" means all income generated in connection with operation of the Rental Housing Development including rental income for Assisted Units and non-Assisted Units, rental income for Commercial Space, laundry and equipment rental fees, rental subsidy payments, and interest on any accounts, other than approved reserve accounts, related to the Rental Housing Development. "Operating Income" does not include security and equipment deposits, payments to the Sponsor for supportive services (except for funds applied towards the cost of on-site supportive service coordination), or tax benefits received by the Sponsor.

- (l) "Program" means the Department funding program or programs providing assistance to the Project.
- (m) "Project" means a Rental Housing Development, and includes the development, the construction or rehabilitation, and the operation thereof, and the financing structure and all agreements and documentation approved in connection therewith.
- (n) "Regulatory Agreement" means the written agreement between the Department and the Sponsor that will be recorded as a lien on the Rental Housing Development to control the use and maintenance of the Project, including restricting the rent and occupancy of the Assisted Units.
- (o) "Rental Housing Development" means a structure or set of structures with common financing, ownership, and management and which collectively contains 5 or more Units (except that HOME projects may contain fewer than 5 Units.). "Rental Housing Development" does not include any "health facility" as defined by Section 1250 of the Health and Safety Code or any "alcoholism or drug abuse recovery or treatment facility" as defined by Section 11834.02 of the Health and Safety Code. Where a Rental Housing Development is located on non-contiguous parcels, all of the parcels shall be governed by similar tenant selection criteria, serve similar tenant populations and have similar rent and income restrictions.
- (p) "Restricted Unit" means any Assisted Unit and any Unit that is subject to Rent and occupancy restrictions that are comparable to those applicable to Assisted Units. Restricted Units include Units subject to a TCAC regulatory agreement, and all Units subject to similar long-term, low-income or occupancy restrictions imposed by other public agencies.
- (q) "Rural Area" means the same as defined in Section 50199.21 of the Health and Safety Code.
- (r) "Sponsor" means the legal entity or combination of legal entities with continuing control of the Rental Housing Development. Where the borrowing entity is or will be organized as a limited partnership, Sponsor includes the general partner or general partners who have effective control over the operation of the partnership, or, if the general partner is controlled by another entity, the controlling entity. Sponsor does not include the seller of the property to be developed as the Project, unless the seller will retain control of the Project for the period of time necessary to ensure Project feasibility as determined by the Department.
- (s) "TCAC" means the California Tax Credit Allocation Committee.
- (t) "Transitional Housing" means a Rental Housing Development operating under programmatic constraints that require the termination of assistance after a specified time or event, in no case less than 6 months after initial

occupancy, and the re-renting of the Assisted Unit to another eligible participant.

- (u) “Unit” means a residential Unit that is used as a primary residence by its occupants, including efficiency Units, residential hotel units, and units used as Transitional Housing.

NOTE: Authority cited: Sections 50406(n); 50517.5(a)(1), (3); 50675.1(c); 50675.11; 50896.1(a), and 50896.3(b), Health and Safety Code. Reference: Sections 50517.5, 50675, 50675.1(c), 50675.2, and 50896.1(a), Health and Safety Code, and 24 CFR part 92.

### Section 8302. Restrictions on Demolition

Proposed projects involving new construction and requiring the demolition of existing residential Units are eligible only if the number of bedrooms in the new Project is at least equal to the total number of bedrooms in the demolished structures. The new Units may exist on separate parcels provided all parcels are part of the same Rental Housing Development (with common ownership, financing and management).

NOTE: Authority cited: Sections 50406(n); 50517.5(a)(1), (3); 50675.1(c); 50675.11; 50896.1(a), and 50896.3(b), Health and Safety Code. Reference: Sections 50517.5(a)(1), (d)(3); 50675.4; 50675.7; and 50896.1(a) Health and Safety Code, and 24 CFR Section 92.353(a).

### Section 8303. Site Control Requirements

At the time of application, a sponsor must have site control of the of the proposed Project property, in the name of the Sponsor or an entity controlled by the Sponsor, by one of the following means:

- (a) fee title;
- (b) a leasehold interest on the Project property with provisions that enable the lessee to make improvements on and encumber the property provided that the terms and conditions of any proposed lease shall permit, prior to loan closing, compliance with all Program requirements, including compliance with Section 8316;
- (c) an enforceable option to purchase or lease which shall extend through the anticipated date of the Program award as specified in the Notice of Funding Availability;

- (d) a disposition and development agreement with a public agency;
- (e) an agreement with a public agency that gives the Sponsor exclusive rights to negotiate with that agency for acquisition of the site, provided that the major terms of the acquisition have been agreed to by both parties; or
- (f) a land sales contract, or other enforceable agreement for the acquisition of the property.

NOTE: Authority cited: Sections 50406(n); 50517.5(a)(1), (3); 50675.1(c); 50675.11; 50896.1(a), and 50896.3(b), Health and Safety Code. Reference: Sections 50517.5((d)(4)(A), 50675.6, 50675.7(c)(3), and 50896.1(a), Health and Safety Code., 42 U.S.C. Section 5304(b) and 24 CFR Section 92.35(a).

#### Section 8304. Unit Standards

- (a) Restricted Units shall not differ substantially in size or amenity level from non-Restricted Units with the same number of bedrooms, and Units shall not differ in size or amenity level on the basis of income-level restrictions. Restricted Units shall not be segregated from non-Restricted Units, and Units shall not be segregated from each other on the basis of income-level restrictions. Within these limits, Sponsors may change the designation of a particular Unit from Assisted to non-Assisted or from one income-restriction to another over time. For Projects involving rehabilitation or conversion, the Department may permit certain Units to be designated as exclusively market-rate Units where necessary for fiscal integrity and where all other Program requirements are satisfied.
- (b) For the full loan term, the number, size, type, and amenity level of Assisted Units shall not be fewer than the number nor different from the size, type and amenity level described in the Regulatory Agreement.
- (c) For projects assisted by MHP, the number of Assisted Units shall equal the number of Restricted Units to the extent allowed by the requirements of Article XXXIV of the California Constitution.

NOTE: Authority cited: Sections 50406(n); 50517.5(a)(1), (3); 50675.1(c); 50675.11; 50896.1(a) and 50896.3(b), Health and Safety Code. Reference: Sections 50517.5(d)(4)(A), (d)(5), and (e)(2); 50675.1(c); 50675.1(c); 50675.2(b); 50675.7; 50675.8 and 50896.1(a), Health and Safety Code, 24 CFR Sections 92.252(e) and 92.504(c).

## Section 8305. Tenant Selection

- (a) Sponsors shall select only Eligible Households as tenants of vacant Assisted Units, using procedures approved by the Department that include:
  - (1) reasonable criteria for selection or rejection of tenant applications which shall not discriminate in violation of any federal, state or local law governing discrimination, or any other arbitrary factor;
  - (2) prohibition of local residency requirements;
  - (3) prohibition of local residency preferences, except where accompanied by an equal preference for employment in the local area and applied to areas not smaller than municipal jurisdictions or recognized communities within unincorporated areas;
  - (4) tenant selection procedures that include the following components, and that are available to prospective tenants upon request:
    - (A) selection of tenants based on order of application, lottery or other reasonable method approved by the Department;
    - (B) notification to tenant applicants of eligibility for residency and, based on turnover history for Units in the Rental Housing Development, the approximate date when a Unit may be available;
    - (C) notification of tenant applicants who are found ineligible to occupy an Assisted Unit of their ineligibility and the reason for the ineligibility, and of their right to appeal this determination;
    - (D) maintenance of a waiting list of applicant households eligible to occupy Assisted Units and Units designated for various tenant income levels, which shall be made available to prospective tenants upon request;
    - (E) targeting specific special needs populations in accordance with the Regulatory Agreement and applicable laws; and
    - (F) affirmative fair housing marketing procedures as specified in the Affirmative Fair Housing Marketing Plan Compliance Regulations of the United States Department of Housing and Urban Development, (24) CFR part 200.620 (a)-(c), or similar affirmative fair marketing housing plan as approved by the Department.

- (b) Sponsors shall rent vacant units to households with no less than the number of people specified in the following schedule:

*Unit Size    Minimum Number of Persons in Household*

SRO	1
0-BR	1
1-BR	1
2-BR	2
3-BR	4
4-BR	6
5-BR	8

A Sponsor may assign tenant households to Units of sizes other than those indicated as appropriate in the table above if the Sponsor reasonably determines that special circumstances warrant such an assignment and the reasons are documented in the tenant's file. The Sponsor's determination is subject to approval by the Department. Through the Project's tenant selection or management plan, a sponsor may receive advance Department approval of categorical exceptions to the above schedule.

NOTE: Authority cited: Sections 50406(n); 50517.5(a)(1), (3); 50675.1(c); 50675.11; 50896.1(a) and 50896.3(b), Health and Safety Code. Reference: Sections 50517.5(a)(1), (d)(3), (d)(5), (e)(2); 50675.1(c); 50675.8(a)(1); 50896.1(a) Health and Safety Code, and 24 CFR Sections 92.303, 92.350 and 92.351.

Section 8306. Tenant Recertification

- (a) The Sponsor shall annually recertify household size and income for Assisted Units.
- (b) If at the time of recertification, a tenant's household size has changed and no longer meets the occupancy standards pursuant to the previous section, the Sponsor may require the tenant household to move to the next available appropriately sized Unit.

NOTE: Authority cited: Sections 50406(n); 50517.5(a)(1), (3); 50675.1(c); 50675.11; 50896.1(a) and 50896.3(b), Health and Safety Code. Reference: Sections 50517.5(a)(1), (d)(3), (d)(5), (e)(2); 50675.1(c); 50675.8(a)(1); 50896.1(a) Health and Safety Code, and 24 CFR Sections 92.303, 92.350 and 92.351.

Section 8307. Rental Agreement and Grievance Procedure

- (a) All rental or occupancy agreements for Assisted Units are subject to Department approval and shall include:

- (1) provisions requiring good cause for termination of tenancy. One or more of the following constitutes "good cause":
  - (A) failure by the tenant to maintain applicable eligibility requirements under the Program or other eligibility requirements as approved by the Department;
  - (B) material noncompliance by the tenant with the lease, including one or more substantial violations of the lease or habitual minor violations of the lease which:
    - (i) adversely affect the health and safety of any person or the right of any tenant to the quiet enjoyment of the leased premises and related Project facilities;
    - (ii) substantially interfere with the management, maintenance, or operation of the Rental Housing Development; or
    - (iii) result from the failure or refusal to pay, in a timely fashion, Rent or other permitted charges when due. Failure or refusal to pay in a timely fashion is a minor violation if payment is made during the 3-day notice period;
  - (C) material failure by the tenant to carry out obligations under federal, state or local law;
  - (D) subletting by the tenant of all or any portion of the Assisted Unit;
  - (E) any other action or conduct of the tenant constituting significant problems which can be reasonably resolved only by eviction of the tenant, provided that the Sponsor has previously notified the tenant that the conduct or action in question would be considered cause for eviction. Examples of action or conduct in this category include the refusal of a tenant, after written notice, to accept reasonable rules or any reasonable changes in the lease or the refusal to recertify income or household size; or
  - (F) for Transitional Housing, the end of the maximum term prescribed for tenant occupancy by the Program operated in a particular Transitional Housing Project.
- (2) a provision requiring that the facts constituting the grounds for any eviction be set forth in the notice provided to the tenant pursuant to state law;

- (3) notice of grievance procedures for hearing complaints of tenants and appeal of management action; and
  - (4) a requirement that the tenant annually recertify household income and size.
- (b) The Sponsor shall adopt an appeal and grievance procedure to resolve grievances filed by tenants and appeals of actions taken by Sponsors with respect to tenants' occupancy in the Rental Housing Development, and prospective tenants' applications for occupancy. The Sponsor's appeal and grievance procedure shall be subject to Department approval and, at a minimum, shall include the following:
- (1) a requirement for delivery to each tenant and applicant of a written copy of the appeal and grievance procedure;
  - (2) procedures for informal dispute resolution;
  - (3) a right to a hearing before an impartial body, which shall consist of one or more persons with the power to render a final decision on the appeal or grievance; and
  - (4) procedures for the conduct of an appeal or grievance hearing and the appointment of an impartial hearing body.
- (c) Neither utilization of, nor participation in any of the appeal and grievance procedures shall constitute a waiver of or affect the rights of the tenant, prospective tenant, or Sponsor to a trial de novo or judicial review in any judicial proceeding which may thereafter be brought in the matter.
- (d) This section shall not be construed to pre-empt or supercede requirements established by local government which further limit good cause for eviction.

NOTE: Authority cited: Sections 50406(n); 50517.5(a)(1), (3); 50675.1(c); 50675.11; 50896.1(a) and 50896.3(b), Health and Safety Code. Reference: Sections 50517.5(d)(3), (d)(5), (e)(2); 50675.8(a)(1), (a)(2); and 50896.1(a) Health and Safety Code and 24 CFR Section 92.253 and 92.303.

#### Section 8308. Operating Reserves

The Sponsor shall establish an operating reserve for the purpose of defraying potential operating shortfalls arising from unforeseen circumstances, beyond the rent-up period.

- (a) Withdrawals from the operating reserve shall require prior written approval of the Department. Should the Department fail to take action on a request for an eligible withdrawal from the operating reserve within 30 days from documented receipt of the request, that request shall be deemed approved.
- (b) The initial deposit to the operating reserve shall be funded from development funding sources in an amount determined by the Department, which shall be not less than the total of the following: 4 months of projected Operating Expenses (excluding the cost of on-site supportive services coordination), 4 months of required replacement reserve deposits, and 4 months of non-contingent debt service. For projects with tax credits, the requirement shall be 3 months of these items. In setting the initial funding requirement, the Department shall consider factors including, but not limited to the projected level of Project cash flow, the adequacy of the operating budget, Project location, local market characteristics, the number of sites, and Project design.
- (c) Sponsor shall fully replace any withdrawals from the Operating Reserve using available cash flow prior to use of any cash flow to pay deferred Developer Fee, partnership management or similar fees, or Distributions.
- (d) Upon occurrence of both of the following events, the Department may reduce the required minimum balance: (i) operation at a debt service coverage ratio of 1.15 or greater for 5 years; and (ii) operation at an Operating Expense coverage ratio of 1.08, where Operating Expense ratio is defined to equal effective gross income, less required replacement reserve deposits and non-contingent debt service, divided by total Operating Expenses, not including the approved cost of supportive services coordination.
- (e) The Department may agree with other financing sources to allocate authority regarding amounts deposited into or withdrawn from the Operating Reserve, where the Department determines that such arrangement would not jeopardize the fiscal integrity of the Project and the minimum reserve requirements would be maintained. For Projects subject to the HUD Section 811 and 202 programs or receiving a permanent loan from CalHFA, the Department may also defer to the operating reserve requirements of these agencies during the time such projects are regulated by HUD or CalHFA, and not require deposits in the amounts specified in subsection (b).
- (f) Where all Project development funding sources are legally precluded from using their funds to capitalize the operating reserve as required by subsection (b), the Sponsor may fund this account out of Operating Income, provided that cash flow is sufficient to reasonably ensure that the required balance can be accumulated within six years of initial occupancy.

NOTE: Authority cited: Sections 50406(n); 50517.5(a)(1), (3); 50675.1(c); 50675.11; 50896.1(a) and 50896.3(b), Health and Safety Code. Reference: Sections 50517.5, 50675.5(b)(8), and 50896.1(a) Health and Safety Code.

#### Section 8309. Replacement Reserves

The Sponsor shall establish a replacement reserve for the purpose of defraying the cost of infrequent major repairs and replacement of building components that are too costly to be absorbed by the Project's annual operating budget.

- (a) Withdrawals from the replacement reserve shall require prior written approval of the Department. Should the Department fail to take action on a request for an eligible withdrawal from the replacement reserve within 30 days of documented receipt of the request, that request shall be deemed approved.
- (b) The replacement reserve shall be funded from Operating Income or a combination of Operating Income and development sources
  - (1) For new construction or conversion Projects, the initial amount of annual deposits to the replacement reserve account shall be equal to at least 0.6% of estimated construction costs associated with structures in the Project, excluding construction contingency and general contractor profit, overhead and general requirements, unless the Department approves a different amount based on the results of a third-party a reserve study or other reliable indicators of the need for replacement reserve funds over the term of the Program loan.
  - (2) For rehabilitation Projects, the initial amount of annual deposits to the replacement reserve account shall be determined by the Department based on the results of a third-party physical needs assessment or other reliable indicators of the need for replacement reserve funds over the term of the Program loan.
  - (3) The Department may periodically adjust the amount of required deposits to the replacement reserve for a particular Project based on the results of reserve studies or other reliable indicators of the need for replacement reserve funds over time.
  - (4) The Department may agree with other financing sources to allocate authority regarding amounts deposited into or withdrawn from the replacement reserve, where the Department determines that such arrangement would not jeopardize the fiscal integrity of the Project and the minimum reserve requirements would be maintained. For Projects subject to the HUD Section 811 and 202 programs or receiving a permanent loan from CalHFA or the Rural Housing

Service of the United States Department of Agriculture, the Department may also defer to the replacement reserve requirements of these agencies during the time such projects are regulated by HUD, CalHFA or the Rural Housing Service of the United States Department of Agriculture.

NOTE: Authority cited: Sections 50406(n); 50517.5(a)(1), (3); 50675.1(c); 50675.11; 50896.1(a) and 50896.3(b), Health and Safety Code. Reference: Sections 50517.5(d)(1), 50675.5(b)(8), and 50896.1(a) Health and Safety Code.

### Section 8310. Underwriting Standards

In analyzing Project feasibility, the Department shall, at a minimum, utilize the following assumptions and criteria:

- (a) Residential vacancy rates shall be assumed to be 5%, unless a different figure is required by another funding source (including TCAC) or supported by compelling market evidence.
- (b) Vacancy rates for Commercial Space shall be assumed to be 50%.
- (c) Total Operating Expenses (not including property taxes or the approved costs of on-site service coordination) shall not be less than those specifically listed in California Code of Regulations, Title 4, Section 10327 as minimum Operating Expenses (without the reduction allowed by those regulations for bond-financed projects). The Department may project higher Operating Expenses where warranted by the experience of comparable properties and particular building characteristics, such as the nature of the tenant population or the level of rehabilitation. Prior to loan closing, the Department may approve total Operating Expenses that are less than those specified in Section 10327, supra, only if the Project has an extraordinary design feature, such as its own electrical generation system, which results in a quantifiable operating cost savings as documented by a qualified third party.
- (d) All Operating Expenses, including property management fees, shall be within the normal market range, as periodically determined by the Department in surveys or based on costs observed in its portfolio.
- (e) The first year Debt Service Coverage Ratio shall not be:
  - (1) less than 1.10:1 or
  - (2) greater than 1.20:1, except where projected cash flow after debt service and required reserve deposits is equal to or less than 12

percent of operating expenses, or where a higher first year ratio is necessary to meet either the requirements of subsection (h) or CalHFA's standard underwriting requirements.

In applying the requirements of subsections (e)(1) and (e)(2), the annual MHP Program loan payment of 0.42% will be considered debt service. These requirement shall not apply to Projects funded under the HUD Section 811 and 202 programs.

- (f) Balloon payments are not allowed on senior debt, and are allowed on junior debt during the term of the Program loan only where the Department determines that the balloon payment will not jeopardize project feasibility.
- (g) Variable interest rate debt shall be underwritten at the ceiling interest rate, unless the Department determines that using a lower interest rate assumption will not jeopardize project feasibility.
- (h) The Project must demonstrate a positive cash flow for 15 years, using income and expenses increase rate assumptions specified in California Code of Regulations, Title 4, Section 10327. If projected Project income includes rental assistance or operating subsidy payments under a renewable contract, the Department may assume that this contract will be renewed, where the renewal of the rental assistance or operating subsidy is likely.
- (i) Reserved
- (j) Where the Department is providing construction-period financing, the minimum budgeted construction contingency shall be 5 percent of construction costs for new construction projects and 10 percent of construction costs for rehabilitation and conversion projects.

NOTE: Authority cited: Sections 50406(n); 50517.5(a)(1), (3); 50675.1(c); 50675.11; 50896.1(a) and 50896.3(b), Health and Safety Code. Reference: Sections 50517.5(d)(2), (e)(2); 50675.7(b)(3), and 50896.1(a), Health and Safety Code, and 24 CFR Section 92.252.

### Section 8311. Limits on Development Costs

- (a) Project development costs must be reasonable compared to development costs for other similar developments of modest design in the general area of the Project.
- (b) Builder overhead, profit and general requirements shall be limited in accordance with California Code of Regulations, Title 4, Section 10327.
- (c) Property acquisition prices shall not exceed appraised value, except where the increment above appraised value is fully covered by junior public agency financing that carries no mandatory debt service.
- (d) Proposed Project sites shall not require site development work that is significantly more costly than that typical for other similar projects in the local market area, unless either:
  - (1) the proposed site acquisition cost together with the site development costs are less than the cost of a typical site together with typical site development costs in the Project's market area; or
  - (2) there are no other sites available in the market area with a lower combined cost.

NOTE: Authority cited: Sections 50406(n); 50517.5(a)(1), (3); 50675.1(c); 50675.11; 50896.1(a) and 50896.3(b), Health and Safety Code. Reference: Sections 50517.5(a)(1), (c)(2), (e)(2); 50675(a); 50675.4((b)(2), (c)(1); 50675.5, and 50896.(1)(a), Health and Safety Code

### Section 8312. Developer Fee

- (a) Developer Fee shall not exceed the amount calculated in accordance with subsections (1), (2) or (3) below, with the exception of LIHTC Projects which shall also be subject to subsection (b). The per unit amounts will be adjusted in thousand dollar increments in accordance with changes in the CPI when, following the year 2000, the CPI has indicated the next full thousand dollar increment has been reached.
  - (1) For new construction Projects and Projects where the contract for the rehabilitation work equals or exceeds \$25,000 per unit:
    - (A) For the first 30 Units, \$20,000 per Unit.
    - (B) For each Unit in excess of 30, \$7,500 per Unit.
  - (2) For other Projects involving acquisition and rehabilitation where the contract amount for the rehabilitation work, excluding contractor

profit and overhead, equals or exceeds \$7,500 per Unit and is less than \$25,000 per unit:

- (A) For the first 30 Units, \$9,000 per Unit.
  - (B) For each Unit in excess of 30, \$4,500 per Unit.
- (3) For all other Projects, \$2,000 per Unit.
- (b) For LIHTC Projects, Developer Fee payments shall not exceed the lesser of \$1,200,000 or the maximum amount that may be included in eligible basis pursuant to California Code of Regulations, Title 4, Section 10327. If the Developer Fee limit established pursuant to this subsection exceeds that established in subsection (a) above, the difference shall be deferred and payable from operating cash flow pursuant to Section 8314(a)(1)(A).
  - (c) Deferred Developer Fee is payable out of cash flow pursuant to Section 8314. For LIHTC Projects, the amount of the deferred Developer Fee is also subject to the limits on deferred developer fee in the TCAC regulations and any applicable federal statutes or regulations.
  - (d) The dollar value of any capital contribution of funds or real property made by the Sponsor or an affiliate, as approved by the Department, for Project development costs shall increase the Developer Fee limit by the dollar value of the capital contribution.

NOTE: Authority cited: Sections 50406(n); 50517.5(a)(1), (3); 50675.1(c); 50675.11; 50896.1(a) and 50896.3(b), Health and Safety Code. Reference: Sections 50517.5(a)(1), (c)(2), (e)(2); 50675.5(b)(5); 50675.8(a)(5); and 50896.1(a), Health and Safety Code.

Section 8313. Reserved

Section 8314. Use of Operating Cash Flow

- (a) Operating income remaining after payment of approved operating expenses, reserve deposits and mandatory debt service shall be applied in the following priority order:
  - (1) First, towards payment of any:
    - (A) approved deferred Developer Fee, pursuant to Section 8312; and
    - (B) asset management, partnership management and similar fees, to the extent such fees are specified under the terms of

financing from a local public entity and reasonable in comparison to fees paid in other similar developments in the Department's portfolio. Where there is no standard specified under local public entity financing, or there is no local public entity financing, the Department shall allow the payment of asset management fees in an amount not to exceed \$12,000 per year.

- (2) Second, 50 percent to the Sponsor as Distributions and 50 percent to the Department as payments on the Program loan.
  - (A) If the terms of other public agencies' financing also require payments from remaining cash flow, the Department may agree to share what would otherwise be its 50 percent share of available cash flow with the public agencies in amounts proportional to the agencies' respective loan amounts.
  - (B) To be consistent with the terms of other public agency loans, the Department may agree to set the percentage payable to the Sponsor at an amount less than 50 percent.
  - (C) For projects with income from project-based Section 8 or similar project-based rental assistance that is not underwritten by other Project lenders, the Department may reduce the Sponsor's share to an amount equivalent to the amount they would receive if one of the other lender's loan amount was based on an income stream that included the income from the rental assistance.
- (b) A Sponsor may not accumulate Distributions from year to year. A Sponsor may deposit all or a portion of permitted Distributions into a Project account for distribution in subsequent years. These future Distributions shall not reduce the otherwise permitted Distribution in those subsequent years.
- (c) Payment of Distributions, deferred Developer Fee, asset management fees, partnership management and similar fees shall be permitted only after the Sponsor submits a complete annual report and operating budget, and the Department determines that the report and budget demonstrate compliance with all Program requirements for the applicable year. Circumstances under which no Distributions, deferred Developer Fee, asset management fees or partnership management and similar fees shall be paid include:
  - (1) when written notice of default has been issued by any entity with an equitable or beneficial interest in the Project;
  - (2) when the Department determines that the Sponsor has failed to comply with the Department's written notice of any reasonable

requirement for proper maintenance or operation of the Rental Housing Development or use of Project income;

- (3) if all currently required debt service, including mandatory payments on the Program loan, and Operating Expenses have not been paid;
  - (4) if the replacement reserve account, operating reserve account, or any other reserve accounts are not fully funded pursuant to Sections 8308 and 8309 and the Regulatory Agreement.
- (d) Distributions attributed to income from Commercial Space and non-Restricted Units shall not be subject to limits pursuant to this section.

NOTE: Authority cited: Sections 50406(n); 50517.5(a)(1), (3); 50675.1(c); 50675.11; 50896.1(a) and 50896.3(b), Health and Safety Code. Reference: Sections 50517.5(a)(1), (c)(2), (e)(2); 50675.8(a)(5); 50896.1(a).

#### Section 8315. Subordination Policy

- (a) The Department may execute and cause to be recorded a subordination agreement subordinating the Department's lien so long as the subordination does not increase the Department's risk beyond that contemplated in the Program loan or grant commitment, as may be amended from time to time, and so long as the subordination would further the interest of the Program. However, and except for Projects assisted by the U.S. Department of Housing and Urban Development under the Section 811 or Section 202 programs, the Department shall not enter into a subordination agreement or other agreement that contains any of the following:
- (1) Any limitation of, or condition on, the Department's exercise of its remedies including, but not limited [to] issuing a notice of default based on a breach under the Department's loan documents, including a default based solely on a breach of the senior lienholder's documents.
  - (2) An agreement that the senior lienholder's acceptance of a deed in lieu of foreclosure would result in the senior lienholder taking title to the Rental Housing Development free and clear of the Department's lien(s).
  - (3) An agreement permitting any modification or supplement of the senior lienholder's lien without the prior written consent of the Department except an agreement that permits a senior lienholder to make advances to: (i) cure a default under a lien with a higher priority than the Department's lien; (ii) pay delinquent taxes on the security property; (iii) pay delinquent hazard or liability insurance

premiums for the security property; or (iv) to protect the health and safety of the tenants.

- (4) An agreement that would require the Department to undertake additional obligations to any party.
- (b) The Department's lien(s) shall not be subordinated to the liens of a local governmental entity unless the total local governmental assistance to the Project is more than twice the amount of the Department's total assistance to the Project (including both loans and grants).
- (c) As used in this section:
- (1) "Department's lien" means a deed of trust, regulatory agreement, or other agreement securing payment or performance under an award of Program funds that has been recorded in the office of the recorder of the county in which the Rental Housing Development is located.
  - (2) "Lien of a local government entity" means a recorded deed of trust, regulatory agreement, reversion, or other recorded agreement securing payment or performance, or a covenant running with the land that affects the maintenance, use, operation, or occupancy of the Rental Housing Development. Except that covenants in favor of a community redevelopment agency regarding the use, maintenance, operation, or transferability of a Rental Housing Development including rent limitations or income restrictions on tenants, or prohibiting discrimination, shall not constitute liens subject to the requirements of this section.
  - (3) "Total local government assistance" means the sum of the principal amounts of loans and grants made by the local government entity plus other direct project costs paid for by the local governmental entity and approved by the Department including, but not limited to, costs of site preparation, demolition, environmental remediation, and land acquisition. The value of assistance in the form of land write-downs or donations shall be limited to the cost paid by the public agency to acquire the land, less any sales proceeds paid to the agency; or in the case of a leasehold, the cost paid by the public agency less the present value of projected lease payments.

NOTE: Authority cited: Sections 50406(n); 50517.5(a)(1), (3); 50675.1(c); 50675.11; 50896.3(b), Health and Safety Code. Reference: 50517.5 (d)(4)(D), 50675(e), 50675.1(b), 50675.6(d), 50896, 50896.1, and 50896.3 Health and Safety Code

## Section 8316. Leasehold Security

- (a) In any Project where the Sponsor proposes to control the Project land through a long-term ground lease, either:
- (1) the Regulatory Agreement and other Program documents shall be recorded against both the Sponsor's interest in the Project and the fee interest in the land, and the lease shall have a term remaining at the time of recordation at least equal to the term of the Program loan or grant; or
  - (2) if the Regulatory agreement and other Program documents are not recorded against the Project's fee interest, the ground lease shall be subject to the Department's approval, must not be subject to any other mortgages on the fee interest, and shall contain, or be amended to contain, provisions which:
    - (A) establish a remaining term of at least ninety (90) years from the date the Department documents are recorded, provided that the Department may accept a lesser term, not less than 65 years, when the lessor is a public agency;
    - (B) ensure the validity of the lien of the Program loan and/or grant documents on the lease;
    - (C) ensure that the lease permits the Project to satisfy all Program requirements and permit the Department to enforce the provisions of the Program loan and/or grant without restriction;
    - (D) expressly consent to the lessee's assignment of the lease to the Department without further consent of the lessor, and permit the Department, after acquisition of the leasehold property, to transfer or assign the lease to a third party without consent of the lessor.
    - (E) provide that the lessor does not have the right to terminate the lease or accelerate the rent upon lessee's breach without first giving the lessee and the Department reasonable notice and opportunity to cure within a reasonable period;
    - (F) provide that no termination, modification or amendment to any terms of the lease shall be effective without the written consent of the Department, and any attempt to take such actions would be void without the Department's consent;
    - (G) require that, in the event of destruction of any improvements on the land, neither the lessor nor the lessee shall terminate

the lease if and so long as the lessee or Department pursues reconstruction of the improvements with reasonable diligence;

- (H) provide that the Department shall not have any liability for the performance of any of the obligations of lessee under the lease until the Department has acquired the leasehold interest, and then only in accordance with the terms of the lease and only with respect to obligations that accrue during the Department's ownership of the leasehold interest;
  - (I) provide that neither the lessor nor the lessee, in the event of bankruptcy by either, will take the benefit of any provisions in the United States Bankruptcy Code that would cause the termination of the lease or otherwise render it unenforceable in accordance with its terms;
  - (J) provide that the leasehold interest will not merge into the fee in the event that the lessee acquires the reversionary interest in the Project; and
  - (K) provide that acquisition of the leasehold property by the Department will not result in a termination of the leasehold; and upon such event, obligate the lessor to enter into a new lease having a term at least as long as the term remaining on the lease prior to acquisition by the Department and on substantially the same terms and conditions.
- (b) Where the lessee and lessor are related or affiliated parties, the Program loan and/or grant documents shall be recorded against both the Sponsor's interest in the Project and the fee interest in the land.
- (c) The Department may modify or waive the requirements of subparagraph (a)(2) where the lessor is a public agency that demonstrates that it is prohibited by law from meeting the requirements and the Department determines that there remains adequate security for the Program loan.

NOTE: Authority cited: Sections 50406(n); 50517.5(a)(1), (3); 50675.1(c); 50675.11; 50896.3(b). Reference: 50517.5 (d)(4)(A), 50675.7, 50896.1, and 50896.3 Health and Safety Code.