**Uniform Multifamily Regulations**

**Title 25, California Code of Regulations**

**Proposed Amendments to Division 1, Chapter 7, Subchapter 19**

**Amend § 8300. Purpose and Scope, as follows:**

 (a) These regulations provide uniform standards and program rules for multifamily rental housing developments assisted by the Department of Housing and Community Development.

(b) When expressly incorporated by reference, some or all of the provisions of this Chapter shall apply to Department programs, including: the Joe Serna Junior Farmworker Housing 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), the TOD Housing Program (operated under guidelines); the AB 1699 Loan Restructuring Program (operated under guidelines); the Veterans Housing and Homelessness Prevention (VHHP) Program (operated under guidelines); and the Affordable Housing and Sustainable Communities (AHSC) Program (operated under guidelines). These regulations interpret and make specific the following ~~Health and Safety Code Division 31, Part 2~~ statutes applicable to these programs: Health & Safety Code Division 31, Part 2, Chapter 2 (commencing with Section 50517.5), Chapter 16 (commencing with Section 50896), ~~and~~ Chapter 6.7 (commencing with Section 50675) and Chapter 3.9 (commencing with Section 50675); Health & Safety Code Division 31, Part 13, commencing with Section 53560; Public Resources Code Division 44, Part 1, commencing with Section 75200; and Military and Veteran’s Code Division 4, Chapter 6, Division 3.2, commencing with Section 987.001.

(c) ~~These regulations establish terms, conditions and procedures for~~ All amendments to these regulations shall apply to funds awarded under a Notice of Funding Availability or other funding announcement issued after the effective date of ~~these regulations~~the subject amendments.

(d) Amendments to these regulations shall also apply to Projects with existing Department loans or grants when the respective borrower or recipient thereof requests and is granted by the Department a subordination to new senior debt, or upon obtaining new tax credits for the Project.

(e) For Projects where the closing of the Department’s loan occurred prior to the effective date of the most recently amended version of these regulations, Sponsors may voluntarily elect to have the following provisions of the most recently amended version of these regulations apply prospectively:

(1) Subsections 8314(1)(B) and 8314(c), regarding asset management fees.

(2) Subsections 8314(e). (f) and (g), regarding supportive services costs.

The amended versions of these provisions shall apply only after the Sponsor obtains consents from other funding sources, as required by the Department, and after execution and recordation of such amendments to Department loan documents as the Department may require. The Department shall publish uniform instruments for this purpose, and these instruments shall not be subject to change or negotiation; Sponsors must agree to their exact terms.

(f) Sponsors may voluntarily elect to have the most recently amended version of these regulations apply, either in their entirety or as specified in subdivision (e), where the closing of the Department’s loan occurs after the effective date of the recent amendments.

(g) Except as specified in subdivisions (e) and (f), in all cases where the amended regulations apply, they shall apply in their entirety. No piecemeal or partial application of selected provisions shall be allowed.

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.

**Amend § 8301. Definitions, as follows:**

 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 or that is required by the Department to be deposited into a reserve account to defray scheduled operating deficits.

(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) “Native American Lands” means real property located within the State of California that meets both the following criteria: it is trust land for which the United States holds title to the tract or interest in trust for the benefit of one or more tribes or individual Indians, or is restricted Indian land for which one or more tribes or individual Indians holds fee title to the tract or interest but can alienate or encumber it only with the approval of the United States; and the land may be leased for housing development and residential purposes under federal law.

(~~j~~k) "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 supportive services that the Sponsor is obligated to provide under their TCAC regulatory agreement, case management and on-site supportive services coordination, but not including debt service, required reserve account deposits, or other supportive services costs.

(~~k~~l) "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~~m) "Program" means the Department funding program or programs providing assistance to the Project.

(~~m~~n) "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~~o) “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~~p) "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~~q) “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~~r) "Rural Area" means the same as defined in Section 50199.21 of the Health and Safety Code.

(~~r~~s) “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~~t) “TCAC" means the California Tax Credit Allocation Committee.

(~~t~~u) "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~~v) “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.

**Amend § 8302.** **Restrictions on Demolition, as follows:**

(a) 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)~~.

(b) The Department may approve exceptions to subdivision (a) where it determines that such exceptions will substantially improve the livability of the remaining units. For example, it may approve a reduction in the number of single room occupancy (SRO) units where necessary to add private cooking and bathing facilities.

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).

**Amend § 8303. Site Control Requirements, as follows:**

Section 8303. Site Control Requirements and Scattered Site Projects

(a) 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~~1) fee title, which, for tribal trust land, may be evidenced by a title status report or an attorney’s opinion regarding chain of title and current title status;

(~~b~~2) 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~~3) 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~~4) a disposition and development agreement with a public agency;

(~~e~~5) 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~~6) a land sales contract, or other enforceable agreement for the acquisition of the property.

(b) If the Project has multiple non-contiguous sites, the configuration of those sites must satisfy all provisions of the statutes governing the applicable Department funding program or programs, and meet the following additional requirements:

(1) all of the developments on the various sites must have a single owner and property manager;

(2) if there is any debt with required payments that has a deed of trust recorded in a position senior to the Department loan, the debt and associated security instruments must be the same for all sites; multiple senior lenders are not allowed;

(3) there must be a single annual report and annual audit of project operations covering all sites;

(4) the Department must be secured against all sites, with lien priority relative to local public agency lenders and use of cash flow available for residual receipts loan payments determined in accordance with Section 8315 of these regulations; and

(5) The Department must be named on insurance policies covering all sites, with coverage meeting Department requirements.

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).

**Amend § 8305. Tenant Selection, as follows:**

(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 may include priority status under a local coordinated entry (also known as centralized or coordinated assessment, or coordinated access) system established pursuant to federal regulations governing the Continuum of Care Program (including 24 CFR 578.7) and 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, and that do not result in applicants waiting in a physical line;

(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) With the exceptions noted below, 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 |

Exceptions:

(1) persons of different generations are not required to share a bedroom;

(2) children of opposite sex five years and older are not required to share a bedroom;

(3) live-in aides may be allocated a separate bedroom; and

(4) for units covered under Housing Choice Vouchers or project-based Section 8 rental assistance contracts, Sponsors may defer to the local housing authority’s determination of appropriate unit occupancy.

A Sponsor may assign tenant households to Units of sizes other than those indicated as appropriate in the table and exceptions listed 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 additional 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.

**Amend § 8308. Operating Reserves, as follows:**

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

### 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.

### 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.

### 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.

### 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.

### 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 or Native American Housing Assistance and Self Determination Act 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).

### 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.

**Amend § 8309.** **Replacement Reserves, as follows:**

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

#### For new construction or conversion Projects submitting applications in 2016, the initial amount of annual deposits to the replacement reserve account shall be equal to at least the lesser of 0.6% of estimated construction costs associated with structures in the Project, excluding construction contingency and general contractor profit, overhead and general requirements or $600 per unit. For projects submitting applications, after 2016, the initial amount of annual deposits shall be $600 per unit increased by the change in CPI since 2016.~~,~~ ~~unless~~ However, the Department may 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~~ the initial 20 years of operation.

#### 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~~ the initial 20 years of operation. In its initial underwriting, in the absence of an approved physical needs assessment or other reliable indicators of the need for replacement reserve funds, the Department may assume that the initial amount of annual deposits shall be $600 per unit, for applications submitted in 2016, and $600 increased by the change in CPI since 2016, for applications submitted in subsequent years.

#### 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.

#### 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, 202 or Native American Housing Assistance and Self Determination Act 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.

**Amend § 8310. Underwriting Standards, as follows:**

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% unless the Department determines that at least one of the following two conditions apply, in which case it may assume a rate of 25%:

 (1) the Sponsor demonstrates to the satisfaction of the Department all of the following four items:

(A) the Project is located in an urbanized area with substantial similar commercial space nearby;

(B) the Project’s specific location and layout makes it highly suitable for prospective tenants; and

(C) the projected rental rate does not exceed the average for competitive properties; and

(D) the vacancy rate for competitive properties is low, and is expected to remain low, taking into account the impact of planned new competitive developments; or

(2) the Commercial Space has either been pre-leased to a new, highly creditworthy tenant or tenants for a term of not less than five years, or is subject to an existing lease with a highly creditworthy tenant or tenants that extends at least five years past the projected date of construction completion.

(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 a higher first year ratio is necessary to:

 (A) project~~ed~~ first year cash flow after debt service and required reserve deposits ~~is~~ equal to ~~or less than~~ 12 percent of operating expenses ~~or,~~;

 (B) ~~where a higher first year ratio is necessary to~~ meet ~~either~~ the requirements of subsection (h);

(C) meet CalHFA’s standard underwriting requirements; or

(D) project a positive cash flow over 20 years, using the assumptions specified in subdivision (i).

 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 requirements shall not apply to Projects funded under the HUD Section 811 and 202 programs,~~ The Department may modify these requirements for Projects receiving operating or rental subsidies structured to allow for breakeven operation, or for operation at a level of cash flow that differs from that resulting from application of these requirements.

(f) Balloon payments are not allowed on senior debt, except as follows:

(1) for existing Department-funded Projects undergoing rehabilitation without new Department funding; or

(2) where the Department’s regulatory agreement is recorded senior to all other lender liens.

In both cases, the Sponsor demonstrates to the Department’s satisfaction that the Project will generate sufficient income, and income obtained through refinancing, to be able to pay the balloon payment when due.

(g) Balloon payments ~~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~~h) 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~~i) Senior debt yield maintenance charges or prepayment penalties applicable after the fifteenth anniversary of the recordation of the senior loan (or conversion of the senior loan from construction to permanent financing) shall not exceed one percent of the outstanding senior loan balance.

(~~h~~j) 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~~k) ~~Reserved~~For projects using low income housing tax credits, the agreements between the ownership entities must allow the Sponsor or an entity directly controlled by the Sponsor to acquire, at the end of the fifteen year tax credit compliance period, either all of the assets of the ownership entity, including the real estate, fixtures, personal property and any cash accounts, or the entire interests of the investor entity and any other interests not already controlled by the Sponsor, at a price that minimizes the risk that the acquisition will require an outlay of cash, and without reserves being spent prematurely, as determined by the Department. This requirement may be satisfied through a purchase option that clearly allows the Sponsor or an entity controlled by the Sponsor to acquire all of the assets of the owner at a price equal to the greater of:

(1) an amount equal to the then fair market value of the Project plus the fair market value of any cash accounts (net of current liabilities) associated with the Project; or

(2) the amount of outstanding debt on any amounts owed by the ownership entity related to the Project, including any loans made by the Sponsor or entity controlled by the Sponsor, plus all unpaid amounts required to be paid to the investor under the partnership documents, not including taxes arising from the acquisition transaction.

If the purchase price is set at fair market value, this value shall be established through an appraisal approved by the Department.

(~~j~~l) 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.

**Amend § 8312. Developer Fee, as follows:**

(a) For projects not utilizing low income housing tax credits, 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 that $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 utilizing low income housing tax credits, Developer Fee payments shall not exceed the ~~lesser of $1,200,000 or the maximum~~ sum of:

(1) the amount that ~~may~~could be included in eligible basis for a 9% competitive tax credit application~~s~~, pursuant to California Code of Regulations, Title 4, Section 10327;

(2) 15% of the tax basis for non-residential costs included in the Project, consistent with Section 10327;

(3) for 4% tax credit projects, any deferred Developer Fee (payable exclusively from operating cash flow), allowed in eligible basis under TCAC regulations; and ~~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)~~ (4) ~~T~~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.

**Amend § 8313. Reserved, as follows:**

Section 8313. ~~Reserved~~ Miscellaneous

(a) Where the requirements of federal funding for a Project (including direct federal loans but excluding federal loan guarantees) would cause a violation of the requirements to these regulations, the Department may modify these requirements as minimally necessary to ensure program compatibility.

(b) If actual total development costs are less than those approved by the Department at construction loan closing, and to the extent allowed under TCAC regulations. the Department loan amount shall be reduced by an amount not less than the difference between projected and actual costs multiplied by the ratio of the Department’s loan amount to the total amount of public agency loans with required payments that do not exceed 0.42% per year. If a reduction would conflict with TCAC or CDLAC regulations, the funds that would have been applied towards this reduction in the absence of such conflict shall be used to reduce tenant rents or for other tenant benefits, as approved by the Department.

(c) The Department may permit the ultimate borrower or recipient of Department funds to be a special purpose entity formed and controlled by the Sponsor if and only if the Sponsor can demonstrate to the satisfaction of the Department all the following criteria:

1. The Sponsor will remain as equally liable to the Department as the special purpose entity with respect to the specific performance of the obligations of the loan or grant documents;
2. The Sponsor shall not intentionally or in effect limit or abrogate its legal liability to the Department by utilizing the special purpose entity; and
3. There shall be no more than two corporate entities between the Sponsor and the special purpose entity in the corporate control and organizational structure(s). For the purposes of this item, “corporate entity” may include a corporation, limited liability company, business trust, limited partnership, or general partnership. For the purposes of determining “control,” the Department shall utilize the standards promulgated by the State Franchise Tax Board.

**Amend § 8314. Use of Operating Cash Flow , as follows:**

(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:

##### approved deferred Developer Fee, pursuant to Section 8312; and

##### 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~~$30,000 per year for 2016 through 2020. This limit shall be increased every five years in accordance with changes in the CPI for the five-year period ending one year prior to the effective date of the increase. For example, the limit for 2021 through 2025 shall be $30,000 multiplied by the percentage change in the CPI from January 1, 2016 to December 31, 2020.

(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 (or, if a public agency has either donated land to the Project, or is providing the land through a ground lease, the Department loan amount and the total local government assistance, as defined in Section 8315 of these regulations). If a public agency loan requires mandatory payments (beyond payments from remaining cash flow) exceeding 0.42 percent per annum, the Department shall discount the amount of the public agency loan to reflect its net present value over the term of the loan, net of the required payments.

(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) Unpaid asset management, partnership management and similar fees may accrue for a period not to exceed three project fiscal years following the year during which they are earned. Payment of these accrued fees shall not reduce otherwise permitted payments. 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.

(~~c~~d) ~~Distributions attributed to income from Commercial Space and non-Restricted Units shall not be subject to limits pursuant to this section.~~ 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.

(e) For 2016, the following limits shall apply to costs paid as Operating Expenses for supportive services that the Sponsor is obligated to provide under their TCAC regulatory agreement, case management and supportive service coordination:

(1) $4,080 per unit per year for supportive housing restricted to individuals or families experiencing chronic homelessness, as defined consistent with Health and Safety Code Section 50675.14;

(2) $3,060 per unit per year for supportive housing that is not restricted to individuals or families experiencing chronic homelessness as defined pursuant to Health and Safety Code Section 50675.14;

(3) $1,051 per unit per year for other units restricted to households with incomes not exceeding 30 percent of area median income; and

(4) $765 per unit per year for all other units.

 These maximum amounts shall be increased each year after 2016 at the rate of two percent per year.

(f) For supportive housing, as defined pursuant to Health and Safety Code Section 50675.14, and upon approval by the Department, Sponsors may establish a reserve to cover unexpected shortfalls in revenues to pay for resident services coordination and case management costs. This reserve may be funded through project cash flow available after funding Operating Expenses and other required reserves, or through development sources. The maximum balance shall not exceed three times the per unit per year limits specified in subsection (e).

(g) Resident service coordination and case management costs include the costs of providing tenants with information on and referral to social, health, educational, income support and employment services and benefits, coordination of community building and educational activities, and individualized needs assessment and individualized assistance with obtaining services and benefits. They may include salaries, benefits, contracted services, telecommunication expenses, travel costs, supplies, office expenses, staff training, maintenance of on-site equipment used in services programs, such as computer labs, incidental costs related to resident events, and other similar costs approved by the Department.

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).

**Amend § 8315. Subordination Policy, as follows:**

(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:

#### 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.

#### 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).

#### 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.

#### 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. If a public agency loan requires mandatory payments (beyond payments from remaining cash flow) exceeding 0.42 percent per annum, the Department shall discount the amount of the public agency loan to reflect its net present value over the term of the loan, net of the required payments.

(d) The Department's lien(s) shall not be subordinated to the liens of a lender affiliated with an entity that has an ownership interest in the Project unless the lender has both:

(1) a Community Reinvestment Act rating of “Outstanding,” or has a rating of “Satisfactory” instead of “Outstanding” based on factors unrelated to their performance as a housing lender in California; and

(2) a Standard and Poor’s rating of “A-“ or higher.

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

**Amend § 8316. Leasehold Security, as follows:**

(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, regulatory agreement, use restrictions or equivalent instruments on the fee interest, and shall contain, or be amended to contain, provisions which:

##### 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;

##### ensure the validity of the lien of the Program loan and/or grant documents on the lease;

##### 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;

##### 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.

##### 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;

##### 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;

##### 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;

##### 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;

##### 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;

##### 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

##### 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) If any other regulatory agreement , use restriction or equivalent instrument is recorded against the fee, the Department’s regulatory agreement must also be recorded against the fee.

(~~b~~c) 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~~d) To the extent consistent with the statutes and regulations or guidelines governing the Program, ~~T~~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, or where the Project will be located on Native American Lands and there is a legal prohibition on meeting these 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.