SENATE COMMITTEE ON HOUSING
Senator Scott Wiener, Chair
2023 - 2024 Regular

Bill No: AB 515 **Hearing Date:** 7/10/2023
Author: Ward
Version: 7/3/2023 Amended
Urgency: No **Fiscal:** Yes
Consultant: Mehgie Tabar

SUBJECT: Housing programs: financing

DIGEST: This bill authorizes the Department of Housing and Community Development (HCD) to approve the payoff of an HCD loan in whole or part, prior to the end of its term, and the extraction of equity from a development for purposes approved by HCD.

ANALYSIS:

Existing law:

1) Allows HCD to approve an extension of an HCD loan, the reinstatement of a qualifying unpaid matured loan, the subordination of an HCD loan to new debt, or an investment of tax credit equity under various older HCD rental housing finance programs.

2) Allows HCD to approve an extension of a loan, the reinstatement of a qualifying unpaid matured loan, or the subordination of an HCD loan to new debt or an investment of tax credit equity if it determines that the project will have after rehabilitation of repairs, a potential remaining useful life equal to or greater than the term of the restructured loan.

3) Allows HCD to charge a monitoring and transaction fee to cover its costs for loan extensions and transactions, and requires developer fee limitations to be consistent with specified laws and regulations, including those set by the California Tax Credit Allocation Committee (CTCAC).

4) Provides that HCD may subordinate its loan to refinance existing senior debt only as necessary for project feasibility and to reimburse borrower advances for predevelopment costs, recent capital improvements, and recent operating deficits.

5) Includes, in Multi-family Housing Program (MHP) Regulations, issued by HCD, the following prohibitions:

   a) Prohibits a property owner from encumbering or pledging Rental Housing Development, or any interest therein or portion thereof, or allow any lien, charge, or assessment against the Rental Housing Development without the prior written approval of HCD.
   b) No loan may be paid off prior to maturity without the prior written consent of HCD in its sole discretion, which consent shall be subject to conditions deemed necessary to ensure compliance with the Program requirements.

6) The Loan Portfolio Restructuring Program (LPRP) includes the following prohibition on cash payments to program sponsors:

   a) Prohibits project sales from involving a cash payment to the selling party, or to any party related to or affiliated with the selling, nor can property owners cash out their equity.

This bill:

1) Authorizes HCD to approve the payoff of an HCD loan in whole or part, prior to the end of its term, and the extraction of equity from a development for purposes approved by HCD.

2) Prohibits the extension, reinstatement, subordination, payoff, extraction, or investment, as specified, if it would result in a rent increase for tenants of a development over the annual adjustment to the tenants' rents under HCD's regulatory agreement.

3) Authorizes HCD to charge additional fees, as necessary, to cover its costs for processing restructuring transactions, and would provide that the monitoring fees continue until the end of the term of HCD's regulatory agreement, as specified.

4) Limits developer fees to the amount allowed by the CTCAC and to 25% of actual rehabilitation costs, as applicable.

5) Authorizes HCD to waive specified requirements in the regulatory agreement if the loan is paid off, including requiring occupancy and financial reports and governing the use of operating income and reserves for the development.

COMMENTS:

1) *Author's Statement.* "Affordable housing developers are challenged with accessing enough funds to break ground and develop essential, affordable

housing. Often, they have to access various sources of funds, including loans from the Department of Housing and Community Development (HCD). However, when affordable housing developers access these loans, they are locked in and do not have any flexibilities. Under existing law, HCD has the authority to approve any prepayment of affordable housing loans; however, HCD has indicated that it will not currently approve any adjustments to its loans. Allowing affordable housing projects to sell or refinance HCD loans will provide additional funds for the development of desperately needed affordable homes in California. AB 515 will require, under certain conditions, HCD to allow the sales and refinancing of HCD financed properties, unlocking millions of dollars by allowing repayments or partial repayments of HCD loans. Any sale or refinancing of HCD loans would include an agreement that the affordable housing development remains affordable for the duration of the original loan period, ensuring the preservation of affordable housing."

2) *Affordable Housing Finance.* The state finances affordable multifamily rental housing using a combination of loans, tax credits, and private activity bonds. Unlike market rate housing, affordable housing does not have the cash-flow from rents to support traditional financing.

   Affordable housing is provided to tenants whose household income is below the area median income (AMI). To qualify, very low-income tenants must make 60% or less of the AMI and lower-income tenants must make only 80% or less of AMI. Tenants in affordable housing are only required to pay 30% of their income toward rent, so the state provides enough long term subsidy to reduce the overall debt service on a development. HCD loans serve as the permanent financing that comes in once a development is complete to take out the predevelopment and construction loans a developer took on to construct the development. HCD loans are secured with a lien in first position on the property. Developments are also subject to a 55-year recorded regulatory agreement which runs with the project. If a developer pays off an HCD loan before the covenants expire, the regulatory agreement is not extinguished and the developer must continue to provide the units at an affordability rent for the length of the regulatory agreement to lower-income tenants.

3) *HCD Prepayments and Equity Withdrawals.* Developers with older HCD loans would like the option to sell developments with MHP loans and pay off the loans or to refinance the loans to take cash out to rehabilitate a development or re-deploy the funds to develop more affordable housing. This would generate millions of dollars to create new affordable housing at no additional cost to the state. According to the sponsors, HCD objects to the sale of properties if the sale involves payment of surplus proceeds to the property owner or the local participating city and prohibits prepayment of MHP loans altogether. Given the

scarcity of funds available for the development of affordable housing and the overall low supply, HCD may have concerns that anything that could jeopardize existing affordable housing is too great of a risk.

MHP regulations suggest that HCD does have some discretion to allow for prepayment and limited ability to allow for a refinance of a loan (*i.e.*, if necessary to maintain or improve the fiscal integrity of a project, to maintain affordable rents, or to decrease rents).

HCD also administers the LPRP. This program was appropriated $332.5 million to preserve and rehabilitate existing HCD-funded developments, including those with MHP loans. To qualify, developments must have expired regulatory agreements or the regulatory agreements must be set to expire by 2032. The LPRP does not allow cash payments to the developer or any cash-out of their equity except if the cash payment is held in a restricted account and contributed to the project during the development period and remains with the project as permanent funding.

This bill would require HCD to allow prepayment of any loans related to housing or housing projects administered by HCD if all of the following conditions are met: the project can continue to cover the debt-service coverage ratio of 1.15 and demonstrates positive cash flow for 15 consecutive years; any new debt is subordinate to HCD's lien and regulatory agreement; HCD's regulatory agreement remains in place for the project for its remaining term; and HCD continues to receive monitoring fees to ensure compliance with the existing regulatory agreement.

The bill specifies that any equity that a developer withdraws from a development must be reinvested back into the development or invested into additional deed-restricted housing for lower-income households. MHP provides permanent loans to serve as long term equity to reduce the debt-service on affordable housing developments to allow for lower rents. This bill is important because HCD should have discretion over how much equity a developer can take out of a project because it will impact rents levels for the length of the 55-year regulatory agreement, as well as the amount of equity available to maintain the development.

FISCAL EFFECT: Appropriation: No Fiscal Com.: Yes Local: No

POSITIONS: (Communicated to the committee before noon on Wednesday, July 5, 2023.)

SUPPORT:

California Council for Affordable Housing (Sponsor)
California Housing Consortium
California Housing Partnership Corporation

OPPOSITION:

None received.

-- END --