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DATE: September 8, 2015

TO: Tax Credit Stakeholders

FROM: Mark Stivers, Executive Director

SUBJECT: Proposed Revisions to Selected Sections of the July 16, 2015 Proposed Regulation Changes with Initial Statement of Reasons

The staff of the California Tax Credit Allocation Committee (TCAC) wishes to substantially revise and seek new public comments on certain sections of the regulation changes proposed on July 16, 2015. In this document, staff summarizes and responds to comments on these selected sections that were received by the close of the initial comment period on August 31, 2015. Staff also provides and explains the revised regulation change proposal for each section. The "back end" provisions of the July 16 Proposed Regulation Changes (described below) are addressed as a group due to the intertwined nature of the comments and the sections. The initially proposed changes are shown in red with single-underlined additions and single strikeout deletions. The additional changes or deletions suggested by the revision are signified by double-underlined additions and double strikeout deletions and highlighted in yellow.

TCAC staff invites new public comments on these selected revised sections only. Interested persons wishing to express their views on these revised proposed regulation changes may submit written comments to TCAC by 5:00 pm on Wednesday, September 30. Please see the public notice for additional information regarding public comments on these revised proposed regulation changes.

Staff will respond to this second round of comments in the Final Statement of Reasons (FSOR) to be issued prior to the meeting at which the Committee will consider the complete package of proposed regulation changes. Staff may propose further revisions to these revised sections in the FSOR.

Staff will not accept new comments regarding sections of the initially proposed regulation changes that are not revised by this document. Staff will respond in the FSOR to those

comments received by the August 31 deadline. Staff is still reviewing comments to those non-revised sections and may withdraw or propose revisions to those sections as well in the FSOR.

Summary of Proposed Changes

1. Revise the proposal to address 15-year capital needs upon sale or refinance. **See description on page 11 and revised proposed changes in Section 10320(b) (Page 15), Section 10302 (Page 14), Section 10320(c) (Page 18), and Section 10327(d)(3)-(5) (Page 21).**

2. Withdraw those proposals relating specifically to projects with at least 50% of the units receive rental assistance. **See Sections 10337(a) (Page 21), Section 10320(b) (Page 15), and Section 10320(c) (Page 18).**

3. Withdraw the proposal to exclude the value of the welfare exemption from the appraised value of a property and withhold approvals of sales and stand-still agreements unless the sale or refinance value is consistent with this requirement. **See Section 10322(h)(9)(A) (Page 19), Section 10320(b) (Page 15), and Section 10320(c) (Page 18).**

4. Include a proposal to require contribution of a share of net equity from a Transfer Event to a sponsor-held trust account for affordable housing. **See description on page 13 and revised proposed changes in Section 10337(a) (Page 21), Section 10302 (Page 14), Section 10320(b) (Page 15), Section 10322(i)(20) (Page 20), and Section 10325(c)(3)(M) (Page 20).**

5. Provide 9% competitive points only to rehabilitation projects for irrigation with reclaimed water, greywater, or rainwater and require new construction projects to irrigate with such sources unless waived. **See Section 10325(c)(6)(F) (Page 24) and Section 10325(f)(7)(L) (Page 39).**

6. Propose various changes to the 9% tax credit tiebreaker. **See Section 10325(c)(10) (Page 25).**

7. Provide greater specificity to the requirement to consult with energy efficiency experts early in the project design process to identify and consider cost-effective energy efficiency or generation measures beyond those required. **See Section 10325(f)(7)(A) (Page 36).**

8. Apply California Building Code accessibility standards to rehabilitation projects in general but require them to provide 4% communications accessible units in accordance with Chapter 11(B). **See Section 10325(f)(7)(K) (Page 38).**

9. Revise the exclusion of costs related to leasing offices, parking facilities, or landscaping from the minimum rehabilitation thresholds. **See Section 10325(f)(10) (Page 39) and Section 10326(g)(7) (Page 43).**

10. Revise the bedroom requirements for large family projects. **See Section 10325(g)(1)(A) (Page 41).**

11. Revise the unit mix and size requirements for special needs projects. **See Section 10325(g)(4) (Page 41).**

12. Revise the threshold basis limit increase for threshold basis boost for structured parking. **See Section 10327(c)(5)(A) (Page 45).**

Back End Provisions

The initially proposed regulation changes included various proposals related to distributions from project sale or refinancing during the regulatory period or appraisal values. These included:

- With respect to new projects, prohibit any distribution from refinancing or sale proceeds to an owner unless all rehabilitation work determined by a capital needs assessment to be necessary within 15 years is completed within one year. **Section 10337(a)(2), page 71.** TCAC shall not approve a change of ownership or stand still agreement unless the owner agrees to amend the regulatory agreement accordingly and set aside adequate funding for the rehabilitation. **Section 10320(b)(2), page 8 and (c)(1), page 10.** The costs of any rehabilitation items left uncompleted shall be excluded from basis if an owner resyndicates. **Section 10327(d)(3), page 67.**

- With respect to existing projects that seek to resyndicate and from which sale or refinance proceeds have been distributed to owners over the previous 15 years, exclude from basis the costs of rehabilitation determined to be necessary by a 15-year capital needs assessment, up to the cumulative amount of proceed distributions. **Section 10327(d)(4), page 67.**

- If a resyndication provides for the distribution of sale proceeds to a seller, exclude from basis the costs of rehabilitation determined to be necessary by a 15-year capital needs assessment. **Section 10327(d)(5), page 67.**

- For new projects in which at least 50% of the units receive rental assistance, generally limit the cumulative distribution from refinancing and sale proceeds over the most recent 15-year period such that the distributions do not exceed the difference between the value of the property based on tax credit rent limits and the debt encumbering the property. **Section 10337(a)(3), page 71.** TCAC shall not approve a change of ownership or stand still agreement unless the owner demonstrates compliance with this limitation. **Section 10320(b)(3), page 8 and (c)(2), page 10.**

- Require that an appraisal exclude the value of the property tax welfare exemption unless the owner can demonstrate that the welfare exemption was reflected in the purchase price when the current owner initially acquired the project. **Section 10322(h)(9)(A)(iii), page 11.** TCAC shall not approve a change of ownership or a stand still agreement related to a refinance unless this requirement is satisfied. **Section 10320(b)(4), page 8 and (c)(3), page 10.**

Many commenters commented on these provisions in the aggregate or to proposals that were contained in multiple sections. As a result, staff will respond to these comments in the aggregate and summarize the various revisions in the aggregate. The revised language for each section, however, will be shown under that specific section.

Comments on Back End Sections:

One commenter stated that the back end proposals are terrific and big and urged TCAC to not be shy about pursing this opportunity.

One commenter commended protecting the integrity of the program and its policy goals over the life of the project.

One commenter supported the limits on distributions for Section 8 properties and excluding the value of the welfare exemption from an appraisal. The commenter supported with reservations the proposals to exclude from basis the costs of rehabilitation when distributions have been made and requiring capital needs improvements to be completed in one year.

One commenter supported the prohibition on distributions unless the rehabilitation work is completed and for projects with rental assistance. This will discourage sales for substantial profits and the potential loss of this important housing stock. The commenter, however, opposed excluding the cost of rehabilitation from basis.

One commenter said he was greatly encouraged by the back end changes as his public organization is dismayed by the pressure from limited partners to capture year 15 equity that could go to rehabilitation. Limited partners are capitalizing the welfare exemption and assuming that new tax credits will fund rehabilitation needs. Likewise, they are capitalizing Section 8 assistance, which puts tremendous pressure on public entities who are skeptical about committing public resources to such projects.

One commenter stated that the valuable public-private partnership model does not mean government regulation is unnecessary. The commenter understands the rationale to limit equity takeouts, ensure complete rehabilitations of properties, and limit distributions coming from tax credit equity. The industry is under scrutiny, and it should ensure that the benefits of the tax credit program accrue to tenants and the communities they live in.

One commenter supported the efforts to ensure property needs and residents are the first priority in future resyndications and to ensure that excess proceeds (whether from a Section 8 overhang or the welfare exemption) remain in affordable housing. The commenter voiced a commitment to identifying practical ways to implement these protections.

One commenter agreed with the concept of meeting rehabilitation needs before equity is distributed but urged exclusion of limited partner buyouts, repayment of general partner equity contributions or loans to buy out limited partners, and general partner loans to the project for initial feasibility or to cover operating deficits. The commenter does not support the Section 8 proposal as written and is concerned that reducing sales prices by the value of the welfare exemption negatively affects acquisition basis. The commenter encouraged TCAC to consider other ways to protect the value of the welfare exemption.

One commenter supported efforts to ensure that the benefit of the welfare exemption is directed to tenants but expressed concern that using the appraisal approach is likely to lead to significant abuse and difficulty in implementation.

One commenter strongly supported efforts to address extraordinary windfall distributions on sales, refinancings, and resyndications. Distributions in excess of a reasonable return should be reinvested in affordable housing stock via a trust fund mechanism. The commenter strongly supports ensuring long-term capital needs are financed first before distributions but does not

support reductions to basis. TCAC should not look at past distributions. The commenter also agrees that the welfare exemption should be better directed towards rent reductions but does not believe limiting appraised values are the best approach.

One commenter supported the general policy recommendation to ensure adequate funding for rehabilitation upon sale as a reasonable expectation. The commenter believes the welfare exemption is a slippery slope that may present future impacts to the ability to provide affordable housing and opposed making changes in this regard.

One commenter stated that equity take outs are definitely an issue to discuss and address. Projects with 100% Section 8 assistance are the most challenging examples. That said, it is difficult to regulate to the lowest common denominator. The commenter suggested that more thought go into the proposals.

One commenter stated that tax credit projects have proven over time to be safe investments and that therefore it is unnecessary to allow undue reward to investors and developers. He further states that the expectation of back end capital appreciation is unlikely to be a key factor in an investor's decision making process as the tax credits and losses comprise their return. Likewise, developer fees are sufficient to secure developer participation in the program. Moreover, there is a clear public purpose to ensuring that an owner consider the condition of the property when seeking sale or refinance distributions. The commenter suggested a requirement that an owner conduct a physical needs assessment prior to TCAC approval of a sale or refinance and that the identified short term work be funded and completed with cash distributions or resyndication proceeds up to the amount of the proposed distribution. The on-going owner should fund the identified longer term work with a project reserve or trust account.

One commenter understands the concerns about equity distributions and agrees that rehabilitation needs should be met first but believes the current proposals are impractical, will create significant unintended consequences, and may prevent sales when the tenants would be best served by new ownership. The commenter also opposes reducing sales prices by the value of the welfare exemption as this reduces acquisition basis which is critical.

One commenter said it is imprudent to cash out the welfare exemption, as property taxes provide much-needed funds for schools, counties, and city services.

One commenter suggested that instead of limiting sale prices the regulations could require sellers to contribute the value TCAC seeks to maintain for the project into a seller-held trust fund that would benefit affordable housing generally.

Two commenters, including one organizational commenter, generally supported the overall objectives of maintaining equity to ensure responsible rehabilitation and preservation of the public investment but were not convinced that the proposed language is the best way to get there. The commenter does support requiring a capital needs assessment (CNA) at sale or refinance and capitalizing 2-year needs and ensuring adequate on-going reserve contributions. The commenter supports efforts to ensure the welfare exemption is directed to tenants but opposes using the appraisal process to do so as it will lead to abuse and difficulty in implementation.

One organizational commenter agreed that policies should prevent developers from taking windfall profits at sale or refinancing which leaves development resources depleted and tenants vulnerable. The proposal, however, severely limits mission-oriented developers from using proceeds to meet needs at other properties. Allowing some of the value to meet these needs

should be allowed. The commenter urged TCAC to consider the financial implications of the welfare exemption proposal to ensure we do not restrict capital flows.

One commenter supported the effort to ensure that the program does not incentivize private financial benefit at the expense of public subsidies or the quality of housing but argued that the proposals create an uncertain regulatory burden and should be withdrawn until further detail can be provided. Ensuring that capital needs are met is understandable but altering the nature of a real estate transaction is fraught with complications. Removing the welfare exemption from appraisals will make it more difficult to resyndicate to address rehabilitation needs.

One commenter stated that it's important to let the market set sales prices but urged staff to look at the HUD Section 236 escrow process, which requires a seller to escrow certain sales proceeds for future affordable housing development. This rewards owners for a job well done while also promoting more development.

One organizational commenter, endorsed by another commenter, concurred with the stated policy goal that equity generated by tax credit investment should benefit the rehabilitation of the project but stated that the proposed regulation goes too far and negatively impacts the public-private partnership that is integral to the LIHTC program. The commenter suggested the following revisions:

- On transfers of ownership at the end of the 15-year federal compliance period, the short term and long term rehabilitation needs be addressed (excluding transfers of limited partner interests), as determined by a capital needs assessment.
- TCAC impose the same standard for qualifying buyers for transfers of ownership as that on new tax credit applicants to ensure that affordable housing developers and market rate "yield" buyers are held to the same standards in terms of management/ownership capacity and experience.
- Beyond the capital needs assessment requirement, there be no limitations on the distribution of proceeds for projects awarded tax credits prior to January 1, 2016 since owners could not have reasonably planned for such limitations in their prior decision-making.

This same organizational commenter, endorsed by another commenter, concurred that there are some HUD projects with a Section 8 overhang that may have led to high value over time but opposed the proposal to limit distributions related to the value of a rental assistance overhang because it would prevent the vast majority of HUD projects that need significant rehabilitation from being acquired by affordable housing developers, leading to the loss of very low-income HUD-subsidized housing or significant disrepair in that housing stock because owners lack the incentives to maintain the properties. The commenter stated that this issue should be dealt with at the federal level and additional time should be spent to address it in a more comprehensive way.

This same organizational commenter, endorsed by another commenter, strongly opposed the proposed changes related to the welfare exemption because it would endanger the utility of and could result in additional attacks on the exemption. Exclusion of the exemption from value would have significant impacts on the financing of affordable housing and make it more difficult for existing owners to rehabilitate properties after purchasing the tax credit investor's interest at the end of the 15-year federal compliance period.

One commenter stated that the development community does not understand the intent of public policy benefit of the back end changes and that it undermines the theme of increasing the production of affordable housing. He suggested that TCAC commission a working group and start from scratch on these proposals.

Two commenters urged TCAC to defer the recommended changes relating to limiting the distribution of sale and refinance proceeds. The commenter understands the concerns TCAC raises but believes this is a terribly complicated matter with potential unintended consequences that needs further vetting.

One commenter stated that limitations on distributions and appreciation will push out the most prudent developers, including the commenter, because a business model driven by fees is precarious. He stated that regulating capital needs assessments is redundant with conditions already monitored by the capital markets, creating inefficiency and possibly disputes. He added that the proposed changes regarding rent caps and underwriting tax exemptions and Section 8 contracts will make it more difficult for developers to be competitive.

One commenter strongly opposed all of these back end proposals.

One commenter believes that the back end proposals will make it difficult or impossible to resyndicate and renovate existing properties with 4% credits and will chase away 4% projects in general.

One commenter stated that the proposed changes that limit the equity take out of existing tax credit projects will have serious, negative consequences on the disposition of the tax credit portfolio, including: 1) new affordable tax credit product will dry up because the limited reward will not be worth the risk; 2) the current at-risk inventory will be driven into the hands of yield buyers; 3) tax credit prices will fall; and 4) resyndication applications will all but cease as owners sell to yield buyers or wait out the use agreement.

One commenter stated that TCAC's interference with market forces will undermine the dynamics of the public-private partnership and eliminate core incentives to produce and maintain affordable housing. Developers make long-term commitments that require substantial economic resources. If the proposals eliminate the developer's potential for any back end appreciation, it will make it difficult for developers to meet guarantee obligations as there will be no possibility of repayment. Currently, a developer's profit from one project often offsets losses from another project. Under the proposal, one underperforming project could drive the sponsor out of business. Lastly, the commenter stated that the proposals fail to differentiate between distributions to investors and developers and therefore penalizes developers who must buy out investors. Many developers will choose to sell their projects rather than resyndicate under the proposed rules.

One commenter stated that the proposal limiting back end value for projects with rental assistance will prohibit him from competing on the front end with market-rate, yield driven buyers. This would be a costly mistake.

One commenter stated that the back end proposals undermine the entire premise under which the tax credit program was developed. It's all sticks and no carrots. The commenter believes that the program is supposed to be self-regulated by the market and that such radical change is a big mistake.

One commenter expressed his shock and anger and stated that the proposed back end changes will force him to sell to yield investors. The commenter is not opposed to the rehabilitation requirement in concept, but it is not palatable in its current form and needs much more work.

One commenter stated that more thought is needed on the back end provisions. The reward for taking huge financial risks is the potential back end payday, and the good deals offset losses on the bad deals. The proposals disincentivize participation in the program generally.

One commenter stated that the back end provisions significantly impact a project's ability to resyndicate and that the Section 8 concerns in particular may be shortsighted. He is not interested in California being a guinea pig on these issues.

One commenter expressed shock at the back end propels and recommended starting with a fresh slate.

One commenter stated that resyndication buyers are having difficulty competing with yield buyers and that the proposed back end changes disincentivize tax credit buyers even more. Resyndication brings in committed owners, lenders, and often local oversight. Resyndication also greens a building and brings in services. Yield buyers run a project lean.

One commenter urged that staff not take the back end provisions to Committee before they are fully vetted as the current proposals would lead to the biggest unintended consequences of all time. The policy of meeting rehabilitation needs is a good one but needs refinement. There are true debt issues related to the appraisal provision. The limitations on equity distributions related to the Section 8 overhang only deal with sales and refinances, so owners would take cash out annually. Staff needs to look at the consequences of equity limitations.

One commenter welcomed accountability features to improve maintenance and sustainability but opposed the more radical features that interfere with the fundamental nature of the program's public-private partnership. Under this program, the benefits and risks were to be borne by the developer, and value generated by wise management was reserved for the developer. The proposals infringe on the benefits of ownership, creating disincentives to production and making affordable housing developers less competitive in the market. In addition, the proposals fail to distinguish between distributions to developers and to investors. Excluding the value of the welfare exemption at sale or refinance is illegal as applied to existing projects and, as prospectively applied, is inconsistent with legislative intent and reduces the reliability of the exemption in the eyes of lenders and investors. With respect to the capital needs assessment provisions, the commenter suggested that TCAC only require rehabilitation work identified in a capital needs assessment associated with the tax credit reservation to be completed during the compliance period. If a developer fails to complete rehabilitation work promised in one TCAC application, then the owner shall fund the uncompleted repairs in the event of a resyndication.

One commenter said that the back end provisions have unintended consequences for lenders. The retroactive nature of the proposed back end provisions undermine the high level of trust in government that California currently benefits from. Projects are already on hold, and future projects will be discouraged.

One commenter expressed concern that the back end changes would risk his family's investment in affordable housing. In addition, the buyout of limited partners needs to be considered for exemption as something beyond the control of the developer.

One commenter opined that the current equity take outs are a result of a historic current moment but that the changes will have a long-term impact that will change the risk/reward dynamic and chill participation in the program.

One commenter stated that TCAC should be careful about changes to the risk/reward dynamic. The proposals will make resyndication difficult, advantaging yield buyers. Using equity is often the way to buy out investors.

One commenter stated that the proposed back end changes are counterproductive to the development of affordable housing and that existing projects will suffer dire consequences.

One commenter stated that 15-year capital needs can be a large figure. Reducing distributions by this amount will greatly reduce the motivation to develop new projects. In addition, the back end proposals generally will motivate owners to continue ownership indefinitely and make it very difficult for even these owners to access renovation funds through refinance or resyndication, resulting in decreased maintenance over time. Ultimately, the proposals may drive private sector partners away from the program.

One commenter stated that the back end proposals are troubling because they significantly curtail the economic incentives for private parties to participate in the tax credit program, favor yield buyers, and disincentivize an owner to operate and maintain the project in an efficient and engaged manner. As an alternative, the commenter supported creating a reasonable limit on the distribution of equity in a sale or refinancing if the distribution would leave the project without sufficient reserves or cash flow to address future capital needs. The commenter further suggested exempting mixed income projects with less than 40% tax credit units from any back end limitations.

One commenter opposed the proposed back end changes. He believes that profit taking, even in large numbers, is not contrary to the intent of the tax credit and Section 8 programs. Congress believed that incentives were necessary to attract private capital to affordable housing and therefore presented developers significant business opportunities, including the possibility of cash proceeds upon sale. The proposals frustrate Congress' intent and hinder the production of affordable housing. The proposal related to Section 8 properties will act as a material disincentive to HUD owners using the tax credit program for rehabilitation and undercut years of work to harmonize HUD programs with the tax credit program. The commenter further believes the welfare exemption provisions are unconstitutional and unfairly ignore the value of debt leveraged by the exemption.

One commenter believes the back end changes are inconsistent with the public-private partnership model.

One organizational commenter, endorsed by another commenter, believes the back end changes will reduce traditional private financing available for affordable housing, decreasing production. The 15-year capital needs requirements will frustrate resyndication, discourage buyers from maintaining properties, and encourage them to perform the least amount of rehabilitation possible. The Section 8 limitations will impair preservation by making projects infeasible. Excluding the value of the welfare exemption will erode lenders' collateral and impact a lender's ability to underwrite this benefit as net income, reducing loan proceeds.

One commenter stated TCAC's ability to require permission for transfers and changes in partnership interests is unclear based on the current regulatory agreement. With respect to the

welfare exemption provisions, the commenter states that the proposal raises a question of an unconstitutional taking. In addition, it artificially and retroactively alters consideration of expenses without regard to income, ignoring debt supported by the exemption. In addition, the change will likely change the terms under which lenders will offer credit, creating large financing gaps, and make it more difficult to get needed legal opinions. Owners will hold and have an incentive to defer maintenance. Applicants may opt out of the welfare exemption and use more tax credits and public financing. The commenter urges that changes not stall transactions that were negotiated in good faith under the existing regulations.

This same commenter stated, with respect to the Section 8 proposal, that it would stop owners from seeking to improve the property, reduce the ability of owners to finance services and other amenities, and add a special disadvantage to resyndicating properties, instead encouraging owners to opt out of Section 8, forever reducing affordability.

This same commenter, with respect to the 15-year CNA provisions, stated that focusing on resyndicated properties creates a bias for rehabilitation properties not currently in the tax credit program. This will also incentivize owners to sell to yield buyers and parties not seeking new tax credits, reducing demand for an already underutilized resource. TCAC should instead encourage resyndications. Lastly, the commenter feels that the 15-year CNA requirements for non-resyndicated properties are unnecessary and duplicative of lender practices. More troubling is requiring all 15 years' worth of repairs in one year.

One commenter stated that the distribution limits on Section 8 properties will encourage owners to opt out and discourage them from selling to preservation buyers. The proposal does not benefit the state of California in any way, and developers and investors who undertake the risks in these projects should not be penalized. Limiting the appraisal value will reduce basis, making it harder to renovate properties, increasing the likelihood of gentrification. The commenter also opposed the 15-year CNA requirements because they will encourage the developer to convert the property to market rate and fervently opposed the welfare exemption provisions as an affordable housing developer would then have to pay more for the project than it would a market rate project.

One commenter strongly opposed the Section 8 and welfare exemption provisions. The Section 8 proposal is a seizure of private property, removes incentives to participate in the tax credit program, and results in sales to yield buyers who will opt out of Section 8. The welfare exemption proposal upends legislative intent and puts the entire tax abatement program at risk. Lenders and investors may stop assuming the abatement in underwriting.

One commenter was very concerned about the back end proposals because it is difficult to know the severity of the impact on developers and investors, though the initial reaction is grave. The program has developed a good balance between risk and reward. Stripping away the reward, which is not overly generous in 98% of cases, will certainly have negative repercussions.

One commenter urged further study of the back end limitations related to Section 8 developments and the exclusion from valuation of the welfare exemption. The commenter questions the concerns about the welfare exemption and worries it could open a can of worms. The commenter also opposed limiting distributions beyond maintenance need and excluding from basis longer-term rehabilitation needs.

One commenter generally agreed with ensuring funding for the 15-year rehabilitation needs at sale or refinance but suggested applying it to projects receiving credits after January 1, 2016, not

excluding uncompleted rehabilitation from basis, and differentiating between short and long term capital needs. The commenter had strong concerns about excluding the value of the welfare exemption as it could have serious impacts on financing and could work against the rehabilitation of property at the 15-year mark. The commenter also had concerns about the Section 8 proposal as it may chill acquisition of these properties by affordable housing developers. California should not move forward without HUD involvement on this issue.

One commenter opposed the back end provisions as unconstitutional. The welfare exemption provision is not contemplated in the current regulatory agreement, interferes with investment-backed expectations, and will decrease value by at least $13,000 per unit.

One commenter stated he will not likely develop new housing units, especially mixed income projects, with 4% tax credits if the back end regulations are approved as written. With respect to the 15-year rehabilitation provisions, the commenter said there is no incentive for an owner to maintain a property if there are no benefits upon sale or refinance, that lenders will already require a new owner to complete immediate repairs and set aside appropriate reserves, and that developers should receive distributions to compensate them for risks. With respect to the welfare exemption, a buyer will have to assume the exemption in order to effectively compete in bidding. Lastly, the commenter suggested that the distribution limits should only apply to projects with at least 50% affordable units to encourage mixed-income projects.

One commenter urged that TCAC hold all the back end items over for continued study as they favor yield buyers and may impede resyndications.

Two commenters opposed excluding welfare exemption value from an appraisal as this will significantly reduce basis. One commenter also opposed limiting the value of Section 8 properties as this will risk losing the properties to yield buyers.

One commenter understood the impetus for the back end proposals but expressed concern that they would negatively impact the ability to buy out investors and address rehabilitation needs. Of particular concern are the reductions to basis for certain rehabilitation costs or from reducing the value of Section 8 properties. The commenter suggested a higher rehabilitation standard for these properties, requiring that proceeds be used to pay off public lenders, or requiring additional affordability, green features, reserves, or services.

One commenter strongly opposed the back end provisions, stating that they are unacceptable to existing affordable housing owners and will discourage them from reinvesting, rehabilitating, and refinancing their properties or developing new properties. The proposal will not increase the supply of affordable housing but will encourage owners to sell to yield buyers. Excluding the value of the welfare exemption will cause immediate write downs of existing values, cause lenders and investors to highly discount or be unwilling to underwrite the property tax exemption, and cause unintended tax and legal issues detrimental to all stakeholders.

Response to Comments:

While some commenters acknowledged the issues the back end proposals sought to address, given the intense interest and the often strong concerns and opposition raised to the specific back end changes proposed, staff essentially has gone back to the drawing board. Staff is withdrawing or significantly revising each back end proposal as discussed below.

Addressing 15-year Capital Needs upon Sale or Refinance

Given that every project financed through the tax credit program received significant public resources and is subject to a long term affordability covenant with the Committee, the Committee has a significant interest in ensuring that each project remains habitable and in good repair. As the tax credit program continues to mature, and the age of tax credit financed projects continues to grow, addressing the long-term habitability of tax credit projects is increasingly important. Staff continues to believe that if value in a tax credit financed project is being monetized due to a sale or refinancing event, it is appropriate that a portion of the monetized value be used to ensure that the short and long term capital needs of the project are addressed. Staff believes that the approach set forth in the proposed revisions addresses the Committee's need to ensure that tax credit projects remain habitable and in good repair without unduly burdening owners of tax credit projects and without unduly impairing the ability of owners of tax credit projects to realize and distribute gain upon the appreciation of a tax credit project, which staff acknowledges to be an important incentive to program participation.

While often disagreeing with the specifics of the initial proposals related to this issue, there was a greater level of support for the concepts embodied by this back end proposal than any other. Staff convened a working group that expressed general support for requiring that capital needs be addressed upon sale or refinance of both existing and future tax credit projects and provided advice on specifics.

The most common concerns expressed by commenters on the specifics of the 15-year capital needs proposals were the following:

- With respect to existing tax credit projects, the provision excluding basis related to 15-year capital needs upon resyndication is only relevant to buyers who wish to resyndicate and therefore will advantage yield buyers. An even playing field is needed.
- The requirement to complete all 15-year capital needs within one year of the sale or refinance necessitates the unnecessary early replacement of items that are still in good repair.
- The prohibition on using resyndication proceeds to pay for all 15-years' worth of repairs identified in the capital needs assessment reduces basis and may make many projects infeasible for resyndication.

The proposed revisions to address each of these issues to a large extent do so by applying the revised rehabilitation requirements to all existing projects, not just those seeking resyndication or a new award of tax credits; by allowing longer-term repairs to be made as needed, as opposed to within one year; and by requiring that only uncompleted short term work items be funded at resyndication through a capitalized reserve that is not basis eligible.

Section 10320(b) of the existing regulations provides that the ownership of any existing Tax Credit project may not be transferred (including the transfer of certain interests within an owner of a Tax Credit project) without the prior written approval of the Executive Director. The proposed additions of Sections 10320(b)(2) through 10320(b)(4) provide guidance as to when the approval of the Executive Director can and cannot be withheld in connection these transfers that are also "Transfer Events," as defined in the proposed Section 10302(pp). These new provisions also expand the approval rights of the Executive Director to include certain refinancing transactions and certain transfers of limited partnership interests in the owner of a tax credit project that are included in the definition of a Transfer Event. Given that the economic ownership interest in many tax credit projects are transferred through the sale of the partnership

interests of the project owner (rather than an actual sale of the project), expanding the approval rights of the Executive Director to cover the transfer of limited partner interests in certain circumstances closes an existing loophole in the approval rights set forth in Section 10320(b). Approval rights over certain refinancing transactions are appropriate given that increased leverage on a project may subject the project's existing tax credit regulatory agreement to greater risk of termination upon foreclosure.

Sections 10320(b)(2) through 10320(b)(4) require that as a condition precedent to the approval of certain Transfer Events, the owner of a Tax Credit project must (i) perform a capital needs assessment of the project to determine the short and long term capital needs thereof and (ii) covenant to the Committee that the short term capital needs will be performed within two years of the Transfer Event and that the owner will establish sufficient capital reserves to cause the long term capital needs of the project to be addressed. These requirements shall be waived if the Transfer Event does not result in a distribution of equity from the project.

The additions to Section 10302 define various terms used in these provisions. The changes to Section 10320(c) clarify that the execution of a stand-still agreement that involves a Transfer Event is subject to the provision of Section 10320(b)(2) through (4). The change to Section 10337(a)(2) specifies in new regulatory agreements that approval of all Transfer Events is required. The changes to 10320(b)(1) delete obsolete language but make no substantive change.

As a result of these changes, staff is withdrawing the proposed changes to Sections 10327(d)(3) through (5) that reduced basis at resyndication.

Withdraw Proposal Related to Limiting Distributions from Projects with Rental Assistance

Staff is withdrawing those back end proposals relating specifically to projects with at least 50% of the units receiving rental assistance (Section 10337(a)(3), Section 10320(b)(3), and Section 10320(c)(2)). Staff will continue discussions with the U.S. Department of Housing and Urban Development (HUD) regarding actions HUD may wish to take to ensure that Section 8 markup revenues contribute to the operation and maintenance of the project.

Withdraw Proposal Related to `Excluding the Value of the Welfare Exemption from Appraised Value

Staff proposes to withdraw the proposal to exclude the value of the welfare exemption from the appraised value of a property and withhold approvals of sales and stand-still agreements unless the sale or refinance value is consistent with this requirement (Sections 10322(h)(9)(A)(iii), 10320(b)(4), and 10320(c)(3)).

Proposal to Require Contribution of a Share of Net Equity to a Trust Account

Staff remains concerned about equity take-outs from certain projects that are in part made possible by public subsidies and other incentives that are meant for the production and preservation of affordable housing. While staff acknowledges that it is important for sponsors, lenders, and investors to rely on these subsidies for the initial underwriting of a project, staff feels it is also important to preserve some of the additional financial benefit that sponsors may

realize at sale or refinance associated with these subsidies. Staff further acknowledges the importance of project sponsors remaining incentivized to protect and preserve their affordable housing portfolio by allowing sponsors to enjoy the economic benefits of successful operations and appreciation over time.

The proposed regulation change applies only to projects that receive a tax credit reservation on or after January 1, 2016 and is only effective in the event that additional project equity is available after a project's rehabilitation needs are accommodated pursuant to the proposed Section 10320(b)(2) described above.

The proposed change in Section 10337(a)(3) adds a section to the regulatory agreement requiring a sponsor at the time of a future Transfer Event, as defined, to contribute a portion of the net project equity to a sponsor-held trust account. The contribution is the lesser of 60% of net equity or a limit related to the property's change in assessed value from between placed in service and the Transfer Event.

> **Example:** The Equity Share Portion is the lesser of two numbers: 1) 60% of the net equity; and 2) the limit.
>
> The formula for the limit on the amount of the Equity Share Portion is:
>
> $$\frac{1\% \times [\text{sales price or the assessed value on the date of refinancing} - \text{assessed value in the year the building was placed in service}]}{\text{capitalization rate}}$$
>
> If the difference in assessed valuations were $5,000,000 and the capitalization (cap) rate were 5%, the limit would equal $1 million.
>
> If the net equity in the project were $2 million, the 60% number would be $1.2 million, so the Equity Share Portion would be the smaller $1 million limit.
>
> If the net equity in the projects were $1 million, the 60% number would be $600,000, so the Equity Share Portion would be the smaller $600,000.

The funds in the trust account may be used to fund a variety of affordable housing activities, including the production of new affordable housing. In lieu of funding a trust account, a sponsor may elect to direct the required contribution to the Department of Housing and Community Development or reduce regulated project rents by an annualized amount of the required contribution (the required contribution amount multiplied by the cap rate for the Transfer Event) TCAC shall not approve a transfer event unless these requirements are satisfied.

The proposed change in Section 10325(c)(3)(M) allows negative points for failure to obtain approval for a transfer event.

Section 10302

Revised Proposed Change:

Add the following definitions to Section 10302:

(cc) "Net Project Equity" shall mean the total sale or refinancing proceeds resulting from a Transfer Event less the payment of all obligations and liabilities of the owner, including any secured and unsecured related and third party debt thereof (including, without limitation, repayment of deferred developer fees and repayment of any advances made by a partner to fund operating and/or development deficits).

(ff) "Qualified Capital Needs Assessment" shall mean a capital needs assessment for a property subject to a Transfer Event dated within one hundred eighty (180) days of the proposed Transfer Event which (i) meets the requirements of (a) the Fannie Mae Multifamily Instructions for the PNA Property Evaluator or (b) Standard Guide for Property Condition Assessments: Baseline Property Condition Assessment Process (ASTM Designation E 2018-08) and (ii) clearly sets forth (a) the capital needs of the project for the next two (2) years (the "Short-Term Work") and the projected costs thereof, and (b) the capital needs of the project for the subsequent thirteen (13) years (the "Long Term Work") and the projected contributions to reserves that will be needed to accomplish that work.

(pp) "Transfer Event" shall mean (i) a transfer of the ownership of a project, (ii) the sale or assignment of a partnership interest in a project owner and/or (iii) the refinancing of secured debt on a project. The following shall not be deemed a Transfer Event: (i) the transfer of the project or a partnership or membership interest in a project owner in which the debt encumbering the project is not increased, refinanced or otherwise modified, (ii) the refinancing of project debt which does not increase the outstanding principal balance of the debt other than in the amount of the closing costs and fees paid to the project lender and third parties as transaction costs, (iii) the replacement of a general partner by a limited partner upon the occurrence of a default by a general partner in accordance with the partnership agreement of the project owner, (iv) a transfer pursuant to a foreclosure or deed in lieu of foreclosure to a non-related party, or (v) a "Subsequent Transfer" pursuant to Section 10320(b)(4)(B) hereof.

Section 10320(b)

Revised Proposed Change:

(b) ~~Tax Credits and ownership transfers.~~ Approvals required by this Section 10320(b) shall not be unreasonably withheld if all of the following requirements, as applicable, are satisfied:

(1) No allocation of the Federal or State Credits, or ownership of a Tax Credit project, may be transferred without prior written approval of the Executive Director. ~~Said approvals that comply with the following provisions shall not be unreasonably withheld.~~ In the event that prior written approval is not obtained, the Executive Director may assess negative points pursuant to section 10325(c)(3)(M), in addition to other remedies.

~~(1) The following requirements apply to all ownership or Tax Credit transfers requested after January 31, 2014.~~

(~~1~~A) Any transfer of project ownership (including changes to any general partner, member, or equivalent responsible party), or allocation of Tax Credits shall be evidenced by a written agreement between the parties to the transfer, including agreements entered into by the transferee and the Committee.

(~~2~~B) The entity replacing a party or acquiring ownership or Tax Credits shall be subject to a "qualifications review" by the Committee to determine if sufficient project development and management experience is present for owning and operating a Tax Credit project. Information regarding the names of the purchaser(s) or transferee(s), and detailed information describing the experience and financial capacity of said persons, shall be provided to the Committee. Any general partner change during the 15-year federal compliance and extended use period must be to a party earning equal capacity points pursuant to Section 10325(c)(2)(A) as the exiting general partner. At a minimum this must be three (3) projects in service more than three years, or the demonstrated training required under Section 10326(g)(5). Two of the three projects must be Low Income Housing Tax Credit projects in California. If the new general partner does not meet these experience requirements, then substitution of general partner shall not be permitted.

~~(2) Any transfer of project ownership (including the sale or assignment of a partnership interest) subject to the requirement to Section 10337(a)(2) shall not be approved unless the owner who shall own the property after the sale agrees to amend the regulatory agreement to meet the requirements of that section and has, in the determination of the Executive Director, set aside adequate funding to meet the rehabilitation requirement.~~

~~(3) Any transfer of project ownership (including the sale or assignment of a partnership interest) subject to the limit on cumulative distributions of refinancing and sale proceeds described in Section 10337(a)(3) shall not be approved unless the seller, transferor, or assignor demonstrates to the satisfaction of the Executive Director that the limitation has been satisfied. The amount of debt encumbering the property and the amounts of cumulative distributions over the most recent 15 year period shall be specified within an audited statement accompanying any request for approval of a change of ownership.~~

~~(4) For purposes of approving a change in ownership (including the sale or assignment of a partnership interest) for value, the applicant shall submit an appraisal consistent with the requirements of Section 10322(h)(9). Unless a waiver has been granted pursuant to Section 10322(h)(9)(A)(iii), CTCAC shall not approve a change of ownership if the sales price or valuation exceeds the appraised value.~~

(2) In addition to any applicable requirements set forth in Section 10320(b)(1), all Transfer Events shall be subject to the prior written approval of the Executive Director. In the event that prior written approval is not obtained, the Executive Director may assess negative points pursuant to section 10325(c)(3)(M), in addition to other remedies. The Executive Director shall approve a Transfer Event if each of the following conditions have been satisfied.

(A) Prior to a Transfer Event, the owner of the project shall submit to the Executive Director a Qualified Capital Needs Assessment. In the case of a Transfer Event in which a third-party lender is providing financing, the Qualified Capital Needs Assessment shall be commissioned by said third-party lender.

(B) The entity which shall own the project subsequent to the Transfer Event (the "Post Transfer Owner") shall covenant to the Committee (the "Capital Needs Covenant") that the Post Transfer Owner (and any assignee thereof) shall:

(i) set aside at the closing of the Transfer Event adequate funds to perform the Short Term Work (the "Short Term Work Reserve Amount");

(ii) perform the Short Term Work within two (2) years from the date of the Transfer Event;

(iii) make deposits to reserves as are necessary to fund the Long Term Work, taking into account any balance in replacement reserve accounts upon the conclusion of the Transfer Event beyond those required by clause (i). Notwithstanding the foregoing, the Post Transfer Owner shall have no obligation to fund any reserve amount from annual operations to the extent that the funding of the reserve causes the project to have a debt service coverage ratio of less than 1.00 to 1.00. In calculating the debt service coverage ratio for the purposes herein, the property management fee shall not exceed the greater of (a) 7% the project's effective gross income, or (b) such amount approved by HUD or USDA, as applicable. Any property management fee in excess of these limitations shall be subordinate to the funding of the required reserves and shall not be considered when calculating the debt service coverage ratio; and

(iv) complete the Long Term Work when required, or prior thereto, pursuant to the Qualified Capital Needs Assessment.

(C) The requirements of Section 10337(a)(3), if applicable, are satisfied.

The Executive Director may waive or modify the requirements of this Section 10320(b)(2)(A) and (B) if the owner can demonstrate that the Transfer Event will not produce, prior to any distributions of Net Project Equity to parties related to the sponsor, developer, limited partner(s) or general partner(s), sufficient Net Project Equity to fully fund the work contemplated by the Qualified Capital Needs Assessment. There shall be a presumption that a Transfer Event has insufficient Net Project Equity (and the requirements of this Section 10320(b)(2)(A) and (B) shall be waived) if no Net Project Equity from the Transfer Event is distributed to parties related to the sponsor, developer, general partner(s) or limited partner(s) of the owner.

(3). The Capital Needs Covenant shall at all times be subordinate to any deed of trust given to any third party lender to a project. The owner of a project subject to a Capital Needs Covenant shall certify compliance with the terms of said Capital Needs Covenant to CTCAC annually for the term of the Capital Needs Covenant on a form to be developed by the Executive Director. Failure to comply with the terms of the Capital Needs Covenant may subject the owner to negative points and/or a ban on buying or receiving future properties.

(4). If a project seeks to receive a new reservation of 9% or 4% tax credits concurrently with a Transfer Event or during the time that the project is subject to a Capital Needs Covenant, the following provisions shall apply:

(A) The underwriting for the new reservation of 9% or 4% credits shall include a capitalized replacement reserve in an amount equal to the cost of any Short Term Work which will not be performed as of the date of the syndication of the new 9% or 4% tax credits reserved for the project.

(B) After the Transfer Event giving rise to the covenant required pursuant to Section 10320(b)(2)(B) (the "Initial Transfer"), if the project will be subsequently transferred in connection with the closing of the new reservation of 9% or 4% credits (a "Subsequent Transfer"), any increase in acquisition price (if the Initial Transfer was a sale) or the project valuation (if the Initial Transfer was a refinancing) between the Initial Transfer and the Subsequent Transfer which is attributable to a reduction in the amount of annual deposits into the replacement reserve account from those required pursuant to Section 10320(b)(2)(B)(iii)

because all or a portion of the Long Term Work will be performed in connection with the new reservation of 9% or 4% credits, must be evidenced in the form of (i) a seller carryback note or (ii) a general partner equity contribution.

(C) Upon the closing of the syndication of the new 9% or 4% credits reserved for the project, the Capital Needs Covenant shall automatically terminate without any further action of the project owner and/or the Committee.

The Executive Director shall have the authority to waive or modify the requirements of this Section 10320(b)(4) if the owner can demonstrate to the reasonable satisfaction of the Executive Director that the requirements of Section 10320(b)(4) would be overly burdensome or would not be in the best interest of the project. This Section 10320(b)(4) shall not be applicable to any project with an existing tax credit regulatory agreement with a remaining term of five (5) or less years.

Section 10320(c) and (d)

Additional Comments Received:

One commenter opposed limiting the Executive Director's discretion to waive, modify, or alter the terms of the stand-still policy.

Response to Comments:

With respect to the proposal to codify TCAC's current policy on subordinations and stand-still agreements, staff finds the comment urging greater flexibility compelling. Staff has revised the language to specifically allow for subordination to restructured public loans and to give the Executive Director the authority to permit other subordinations as appropriate.

Revised Proposed Change:

(c) CTCAC shall initially subordinate its regulatory contract to a permanent lender but thereafter shall not subordinate existing regulatory contracts to acquisition or refinancing debt, except in relation to new Deeds of Trust for rehabilitation loans, ~~or~~ FHA-insured loans, restructured public loans, or as otherwise permitted by the Executive Director. At the request of the owner, CTCAC shall enter into a stand-still agreement permitting the acquisition or refinance lender 60 days to work with the owner to remedy a breach of the regulatory contract prior to CTCAC implementing any of the remedies in the regulatory contract, except that ~~as follows:~~ CTCAC shall not enter into a stand-still agreement related to a Transfer Event unless the conditions of Section 10320(b)(2) have been satisfied. If CTCAC enters into a stand-still agreement related to a Transfer Event, Sections 10320(b)(3) and (b)(4) shall apply to the project.

~~(1) If the project is subject to the limit on distributions of refinancing and sale proceeds described in Section 10337(a)(2), the stand-still agreement shall not be approved unless the owner agrees to amend the regulatory agreement to meet the requirements of that section and has, in the determination of the Executive Director, set aside adequate funding to meet the rehabilitation requirement.~~

~~(2) If the project is subject to the limit on cumulative distributions of refinancing and sale proceeds described in Section 10337(a)(3), the stand still agreement shall not be approved unless the owner demonstrates to the satisfaction of the Executive Director that the limitation has been satisfied. The amount of debt encumbering the property and the amounts of cumulative distributions over the most recent 15 year period shall be specified within an audited statement accompanying any request for execution of a stand still agreement.~~

~~(3) For purposes of approving a stand still agreement related to a refinancing in which proceeds will be distributed to an owner, the applicant shall submit an appraisal consistent with the requirements of Section 10322(h)(9). Unless a waiver has been granted pursuant to Section 10322(h)(9)(A)(iii), CTCAC shall not approve a the stand still agreement unless the appraised value used by the lender for purposes of establishing the loan to value ratio is less than or equal to the appraised value submitted to CTCAC. The lender shall certify that this requirement has been met.~~

(~~c~~d) False information. Upon being informed, or finding, that information supplied by an applicant, any person acting on behalf of an applicant, or any team member identified in the application, pursuant to these regulations, is false or no longer true, and the applicant has not notified CTCAC in writing, the Committee may take appropriate action as described in H & S Code Section 50199.22(b) and in section 10325(c)(3) of these regulations. Additionally the Executive Director may assess negative points to any or all members of the development team as described in Section 10322(h)(5).

Section 10322(h)(9)(A)

Revised Proposed Change:

(A) Rehabilitation applications. An “as-is” appraisal prepared within 120 days before or after the execution of a purchase contract or the transfer of ownership by all the parties by a California certified general appraiser having no identity of interest with the development’s partner(s) or intended partner or general contractor, acceptable to the Committee, and that includes, at a minimum, the following:

(i) the highest and best use value of the proposed project as residential rental property;
(ii) the Sales Comparison Approach, and Income Approach valuation methodologies except in the case of an adaptive reuse or conversion, where the Cost Approach valuation methodology shall be used;
(iii) the appraiser’s reconciled value except in the case of an adaptive reuse or conversion as mentioned in (ii) above. ~~The value shall exclude the value of the property tax welfare exemption, except that an existing project may request a waiver to this provision if it can demonstrate to the satisfaction of the Executive Director that the welfare exemption was considered and reflected in the purchase price when the current owner initially acquired the project~~;
(iv) a value for the land of the subject property “as if vacant”;
(v) an on site inspection; and
(vi) a purchase contract verifying the sales price of the subject property.

Except as described below, the "as if vacant" land value and the existing improvement value established at application, as well as the eligible basis amount derived from those values shall be used during all subsequent reviews including the placed in service review, for the purpose of determining the final award of Tax Credits. For tax-exempt bond-funded properties receiving credits under Section 10326 only or in combination with State Tax Credits, the applicant may elect to forego the appraisal required pursuant to this Section 10322(h)(9) and use an acquisition basis equal to the sum of the third party debt encumbering the seller's property, which may increase during subsequent reviews to reflect the actual amountacquisition basis may increase with CTCAC's approval where (a) the sales price is no more than the sum of the assumed third-party debt on the property and other third party debt on the property that is required to be paid down or paid off, and (b) a third-party appraisal consistent with Section 10322(h)(9) supports the updated purchase price.

Section 10322(i)(20)

Reason:

The proposed Section 10337(a)(3) uses current and past assessed values to calculate an equity share portion of net remaining value. In order to make this calculation, TCAC needs to collect assessed values from the year the building is placed in service or as soon thereafter as the valuation is available. This provision requires submittal of the baseline assessed valuation with the place in service package or within 30 days of receipt by the owner.

Proposed Change:

(20) A project's placed in service application shall include the project's property tax statement for the year the property is placed in service, if available. If the owner receives the statement after the submission of the placed in service application, the owner shall provide CTCAC with the statement within 30 days of receipt.

Section 10325(c)(3)(M) and (U)

Reason: These proposed change provides an enforcement mechanism for the requirement in Section 10320(b)(2) to obtain prior written approval of all Transfer Events and the requirement in Section 10337(a)(3)(B) to expend funds in a trust account only for specified purposes.

Proposed Change:

(M) failure to properly notify CTCAC and obtain prior approval of Transfer Events, general or limited partner changes, transfer of a Tax Credit project, or allocation of the Federal or State Credit;

(U) failure, after a notice and cure period, to comply with a requirement of the regulatory agreement or of a covenant entered into pursuant to Section 10320(b)(2)(B) or Section 10337(a)(3)(B).

Section 10327(d)(3)-(5)

Revised Proposed Change:

~~(3) If a project subject to the requirements of Section 10337(a)(2) seeks a new reservation of Tax Credits (i.e. resyndication), the costs of any rehabilitation work determined by the capital needs assessment conducted at the time of the sale or refinancing to be necessary to be undertaken within 15 years and that remain uncompleted on the date of application shall be excluded from eligible basis.~~

~~(4) If a project that is not subject to the requirements of Section 10337(a)(2) seeks a new reservation of Tax Credits (i.e. resyndication) and has distributed refinancing and/or sale proceeds to any owner or previous owner over the last 15 year period, the costs of any rehabilitation work determined by the application's capital needs assessment to be necessary to be undertaken within 15 years, up to the cumulative amount of refinancing and/or sale proceeds distributed to any owner or previous owner over the last 15 year period, shall be excluded from eligible basis. The capital needs assessment shall be ordered by an investor or by a first mortgage or public lender who will have a loan outstanding after the resyndication. The history of cumulative distributions over the most recent 15 year period shall be specified within an audited statement accompanying the application.~~

~~(5) If an application seeking a new reservation of Tax Credits (i.e. resyndication) provides for the distribution of sale proceeds to a seller, except in the form of a seller carryback note with a term of at least 55 years, the costs of any rehabilitation work determined by the application's capital needs assessment to be necessary to be undertaken within 15 years shall be excluded from eligible basis. The capital needs assessment shall be ordered by an investor or by a first mortgage or public lender who will have a loan outstanding after the resyndication.~~

Section 10337(a)

Revised Proposed Change:

(a) Regulatory Agreement. All recipients of Tax Credits, whether Federal only, or both Federal and State, are required to execute a regulatory agreement, as a condition to the Committee's making an allocation, which will be recorded against the property for which the Tax Credits are allocated, and, if applicable, will reflect all scoring criteria proposed by the applicant in the competition for Federal and/or State housing Credit Ceiling.

(1) For all projects receiving a reservation of competitive 9% federal tax credits on or after January 1, 2016 for which all general partners will be Qualified Nonprofit Organizations, the partnership agreement shall include a Right of First Refusal ("ROFR") for one or more of the nonprofit general partners to purchase the project after the end of the 15-year federal compliance period. The price to purchase the project under this ROFR shall be the minimum

price allowed under IRC Section 42(i) plus any amounts required to be paid to the tax credit investors that remains unpaid for approved Asset Management Fees and required payments under the limited partnership agreement for tax credit adjusters that remain outstanding at the time of the sale. The applicant shall demonstrate compliance with this requirement prior to the issuance of the 8609 forms.

(2) For all projects receiving a reservation of 4% and 9% federal tax credits on or after January 1, 2016, the regulatory agreement shall require written approval of the Executive Director for any Transfer Event. ~~prohibit any distribution from refinancing or sale proceeds to an owner or owners unless all rehabilitation work determined by a capital needs assessment to be necessary to be undertaken within 15 years from the date of sale or refinancing shall be completed within one year of the date of sale or refinancing. The capital needs assessment shall be ordered by a first mortgage or public lender who shall have a loan outstanding after the sale or refinancing.~~

~~(3) The regulatory agreement for projects that receive a reservation of 4% or 9% federal tax credits on or after January 1, 2016 and in which at least 50% of the units are subject to a continuing state or federal project-based rental assistance contract shall limit the cumulative allowed distribution from refinancing and sale proceeds permitted to an owner or owners, and/or to a previous owners as a payoff of a seller carryback note, over the most recent 15-year period of ownership. For purposes of calculating the limitation amount, the total distributions shall be reduced by the percentage of non-Tax Credit units in the project and shall not include any amount that is financed with a seller carryback note with a term of at least 55 years. If the rental assistance rents exceed the TCAC rent limits on the date of sale or refinancing, the cumulative distribution permitted (after funding the rehabilitation required as a result of the 15-year capital needs assessment pursuant to paragraph (2)) shall not exceed the difference between the value of the property based on tax credit rent limits and the debt encumbering the property, as determined by a CTCAC-ordered appraisal.~~

(3) For all projects that receive a reservation of 4% or 9% federal tax credits on or after January 1, 2016 and which include at least 50% Tax Credit units, the regulatory agreement shall require all of the following:

(A) If a Transfer Event, after application of Sections 10320(b)(2) through (4) and prior to any distributions to parties related to a sponsor, developer, limited partner, or general partner, produces Net Project Equity, then the Equity Share Portion of this remaining Net Project Equity shall be deposited into a trust account for the provision of rental housing units affordable to and serving households earning no more than 60% of the area median income.

The Equity Share Portion shall be 60% of this remaining Net Project Equity, but no more than 1% of the difference between the sales price or the assessed value on the date of refinancing, as applicable, and the assessed value in the year the building was placed in service, divided by the cap rate used in the appraisal conducted in conjunction with the Transfer Event.

(B) The parties shall make the required deposit into the trust account to be held by the seller or refinancer or a related entity, and the proposed holder of the trust account shall enter into a covenant with TCAC to expend funds in the account only for the following purposes related to providing rental housing units affordable to and serving households earning no more than 60% of the area median income that will be subject to a governmental regulatory agreement with a remaining term of at least 15 years:

I. New construction.
II. Rehabilitation with or without acquisition, provided that the acquisition price is not paid to a related entity.
III. Land banking, provided that construction starts on eligible units within 5 years. If construction does not start within 5 years, the property shall be sold and net proceeds returned to the trust account, unless the Executive Director approves an extension.
IV. Capital needs of existing properties.
V. Property operating losses not related to increases in fees to a related entity.
VI. Continue resident services beyond the time period committed in a CTCAC or CDLAC application.
VII. Unrelated third party predevelopment expenses.
VIII. The buydown of debt on a property that maintains the cash flow after debt service in accordance with the limitations described in Section 10327(g)(7) as shown in an audited financial statement.
IX. The capitalization of an operating reserve within a project subject to an existing project-based Section 8 or other rental assistance contract to maintain tenant rents for the longest possible time in the event of a loss of rental assistance.
X. The payment of taxes associated with the proceeds deposited into the trust account.
XI. Another use approved by the Executive Director.

The holder of the trust account annually shall report on a form prescribed by CTCAC on deposits of funds to and use of funds from the trust account and certify that such uses are in compliance with the requirements of this section.

(C) In lieu of funding the trust account required in subsection (A) above, the parties to the Transfer Event may elect to (i) reduce targeted rents in each succeeding year of the regulatory period by an amount equal to the Equity Share Portion multiplied by the capitalization rate used in the appraisal conducted in conjunction with the Transfer Event, in which case the post-Transfer Event owner shall agree to amend the regulatory agreement accordingly, or (ii) donate the Equity Share Portion to the California Department of Housing and Community Development for provision of rental housing units affordable to and serving households earning no more than 60% of the area median income.

(4) Where a Project is receiving renewable project-based rental assistance or operating subsidy:

(~~1~~A) the Sponsor shall in good faith apply for and accept all renewals available;

(~~2~~B) if the project-based rental assistance or operating subsidy is terminated through no fault of the owner, the property owner shall notify CTCAC in writing immediately and shall make every effort to find alternative subsidies or financing structures that would maintain the deeper income targeting contained in the recorded CTCAC regulatory agreement. Upon documenting to CTCAC's satisfaction unsuccessful efforts to identify and obtain alternative resources, the owner may increase rents and income targeting for Rent Restricted Units above the levels allowed by the recorded regulatory agreement up to the federally-permitted maximum. Rents shall be raised only to the extent required for Financial Feasibility, as determined by CTCAC. Where possible, remedies shall include skewing rents higher on portions of the project in order to preserve affordability for units regulated by TCAC at extremely low income targeting. Any necessary rent increases shall be phased in as gradually as possible, consistent with maintaining the project's Financial Feasibility. If housing Special Needs populations, the property owner shall attempt to minimize disruption to existing households, and transition to non-Special Needs households only as necessary and upon vacancy whenever possible.

Other Provisions

Section 10325(c)(6)(F)

Initially Proposed Regulation Change:

Allow points for the use of rainwater, greywater, or recycled water for irrigation.

Comments received:

TCAC Committee Member Betty Yee recommended that the regulations require irrigation only with reclaimed water, greywater, or rainwater (excepting water used for Community Gardens) in new construction projects and allow competitive points only for rehabilitation projects. The current drought and the possibility of on-going drier conditions in California as a result of climate change make it imperative to pursue all possible water saving measures.

One commenter stated that achieving 100% of irrigation needs with non-potable water may be challenging and that having this as the metric may have the unintended consequence of dissuading applicants from pursuing this option. The commenter suggested providing points for projects meeting at least 90% of the irrigation need under normal conditions.

One commenter pointed out that the points for non-potable water use benefits projects with high irrigation needs though projects are increasingly turning to drought tolerant landscaping or have little to no green space.

One commenter stated that using greywater in existing buildings is more difficult than in new developments and should garner more points.

One commenter supports the promotion of water efficiency but raised concerns that some projects would be ineligible. Urban infill projects can have no landscape areas that require irrigation. In addition, not all jurisdictions allow irrigation with reclaimed water, greywater, or recycled water. The commenter suggested a minimum square footage of irrigated landscape area to ensure desired outcomes.

Response to comments:

Staff proposes to allow competitive points for irrigating with reclaimed water, greywater, or rainwater only for rehabilitation projects and make this a minimum construction standard for new construction projects pursuant to Section 10325(f)(7)(L) below.

Because the language of the existing regulations refers to "normal conditions," staff believes that requiring offset of 100% of irrigation needs still accounts for unanticipated future conditions.

Revised Proposed Change:

(HF) Water efficiencyRehabilitation projects:

Irrigate only with reclaimed water, greywater, or rainwater (excepting water used for Community Gardens) 3 points

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Section 10325(c)(10)

Initially Proposed Regulation Change:

Alter the public funds factor of the tiebreaker to count leveraged soft resources, including public or private soft loans and land donations from unrelated entities (and land donations from related entities on a case by case basis). Count operating and rental subsidies from the California Department of Health Care towards the public funding numerator increase. Multiply the leveraged soft resources factor of the tiebreaker by a size factor. Alter the credit efficiency factor in the tiebreaker by adding back leveraged soft resources that supplant eligible basis. Allow TCAC to use its own appraisals to establish donated land values.

Comments Received:

General

One commenter stated that the tie breaker changes were a good effort in general but that she'd like to see more distinction of projects through the scoring system than through the tiebreaker.

One commenter urged TCAC to think smaller about tiebreaker changes as these proposals could have a big impact and turn the tiebreaker on its head.

One commenter stated that changes to the final tiebreaker that would reduce the competitiveness of more deeply-targeted income- and rent-restricted projects would not be good public policy and seems inconsistent with the federal law that requires preference for projects serving the lowest income tenants.

One commenter urged consideration of a tiebreaker incentive for market-rate units as HUD, under its Rental Assistance Demonstration Program, is increasingly requiring the inclusion of non-subsidized units. The current tiebreaker penalizes this.

One commenter expressed serious concerns that the proposed tiebreaker methodology would establish the opportunity for abuse and encouraged TCAC to leave the tie-breaker as is until a new methodology can be developed and fully vetted for unintended consequences, fairness, and equity.

Two commenters, including one organizational commenter, supported the current tiebreaker and advocated no change.

One commenter suggested basing the tiebreaker on public benefit rather than financing structure.

Two commenters stated that the adjustments to the tiebreaker move in the right direction but do not go nearly far enough to balance the benefits of public funding with cost-efficient development. The commenters suggested rewarding cost efficient development on the same basis as public funds.

One commenter suggested using small, incremental additions (such as one or two percentage points) to the tiebreaker to incentivize larger projects and other policy goals.

One commenter opposed the changes to the tiebreaker in their current form.

Two commenters urged inclusion of San Francisco and Los Angeles operating subsidies to the list of enumerated subsidies that will count towards the tiebreaker as these have been accepted in the past.

One commenter appreciated the intent to lessen the weight of public funding and incorporate other factors related to cost effectiveness and production but stated that the proposed changes are difficult to interpret and apply and have an unclear impact on the intended policy goals.

Two commenters preferred a phased approach to accommodate projects in the pipeline.

One commenter suggested eliminating the divide by three portion of the credit reduction factor or creating a tiebreaker without soft public funds to better reward cost efficiency. The tiebreaker should encourage increasing supply, closing financial gaps, reducing project costs, and increasing equity.

One commenter said the three proposed changes are welcome but will do little to increase production or discourage the "waste" of public subsidies currently incentivized. The commenter suggested applying the size factor to the entire tiebreaker, not just the public funds factor, and removing the divide by three provision of the credit reduction factor.

Expansion of public funds to soft leverage category

Nine commenters supported including leveraged soft resources towards the tiebreaker. One suggested more specificity to avoid shenanigans and urged TCAC to monitor the use of this provision and make future adjustments as needed. One suggested more clearly defining the terms of private soft loans and expressed concern about the advantage seller carryback loans would enjoy.

One commenter strongly supported private entity resources in the tiebreaker as a way to encourage creativity and resourcefulness but requested further guidance on what will constitute legitimate soft resources from a non-public entity.

One commenter supported including the value of private land donations within the tiebreaker. He stated that this change will end the current unfair advantage that housing authorities enjoy for land they donate. The commenter, however, opposed the application of the 10-year rule to private donations and urged that all private donations count.

One commenter questioned the wisdom of requiring a 10-year hold period for donated land.

One commenter supported any conceivable change that will allow land donations from unrelated entities, with certain qualification.

Three commenters supported the inclusion of leveraged soft resources in the tiebreaker as a way to increase the supply of affordable housing. The commenter stated that owners of existing real estate, who may include owners of affordable housing, may be interested in donating land to increase the number of units. Requiring the prior approval of the Executive Director for donations of land from related parties will ensure that this provision is used in bona fide donation situations.

Two organizational commenters stated it makes sense to allow funds from unrelated non-public entities but urged more clarification and controls. One suggested strengthening the identity of the contributing party so that the party's enforcement responsibility is more clearly understood.

One commenter expressed concern that allowing private funds opens the door to abuse and suggested that the source of the funds be documented and independently verified by TCAC staff both at application and placed in service as truly arms-length.

Two commenters opposed counting soft loans and grants from unrelated non-public entities as too difficult to administer and creating too much potential for manipulation.

One commenter likewise expressed strong concern that counting soft loans from unrelated entities will create unintended consequences as developers seek to convert deferred developer fee to soft loans through shenanigans. Deferred developer fees are a necessary financial cushion to a project, and encouraging the overleverage of projects will risk underwater projects.

Two commenters asked that funds from the U.S. Department of Justice's National Mortgage Settlement be excluded from the tiebreaker. They stated that the proposed change provides an unwarranted benefit to a small group of lenders obligated to make loans with these funds, as the current language would consider them private soft funds.

Two commenters, including an organizational commenter, appreciated the effort to balance the competition but believe that allowing private loans to count as soft leverage is problematic and will result in applicants taking advantage. Allowing private sources needs to be done in a transparent and controlled manner.

One organizational commenter opposed adding private soft loans until TCAC can identify a way to ensure their legitimacy.

Two commenters were concerned about counting private funds until there is a clear and workable definition of "unrelated."

One commenter asked for examples of when land donations from related entities may be approved.

One commenter asked for clarification that tribal funds be considered public funds.

Size factor

One commenter supported the size factor.

One commenter appreciated the effort to incentivize large projects as the current tiebreaker incentivizes smaller projects.

One commenter supported the proposed size factor as long as the results are assessed going forward to remedy any unintended consequences. Cost efficiency and economies of scale must be balanced against quality, developing not just in low-cost locations, and meeting special needs.

One commenter supported incentivizing larger, new construction projects as the need for a larger supply of decent, affordable housing in Indian Country cannot be overstated.

One organizational commenter applauded the proposed addition of the size factor but pointed out that the size factor would not be necessary if the two current factors were equally weighted.

One commenter supported the size factor but recommended that the advantage for larger projects be capped at 100 units.

One organizational commenter, endorsed by another commenter, appreciated the proposal's attempt at placing less emphasis on bringing a high amount of public funds to a small number of units but opposed making the proposed change at this time and instead urged a longer effort to

develop a tiebreaker formula that specifically focuses on variables that would more effectively meet the public policy goal of increasing production of affordable housing.

Another organizational commenter stated that the size factor unfairly punishes smaller developments, making it more difficult for rural communities to compete.

One commenter opposed the size factor, stating that economies of scale are by no means universal and discouraging medium-size infill developments is counter to the need for transit-oriented developments, deconcentrated poverty, sensitivity to community scale, and the realities of achieving public approvals. Only the most massive projects will be funded, effectively redlining cities where sites are unavailable or large projects unlikely to be approved. The effect will be more pronounced in the set-asides. The commenter suggested instead a 1% tiebreaker reduction for projects smaller than 40 units and no boost for large projects.

One commenter asked TCAC to reconsider the application of a size factor until the unintended consequences are better understood. He stated that the size factor will indirectly encourage more SRO and senior housing types. For example, for a specific 1.5 acre parcel available to the developer, he could build 51 units of family housing, 62 units of senior housing, or 87 units of SRO housing. The SRO housing type would increase the size factor applied to the project by 30%. In addition, the size factor would permanently disadvantage small projects that have already received their entitlements, possibly forcing developers to abandon these projects which have been in the pipeline.

One commenter stated that that the size factor creates an unfair advantage for acquisition and rehabilitation projects in rural areas because new construction projects are limited to 80 units while rehabilitation projects have no size limit.

Five commenters opposed the inclusion of the size factor because it will disadvantage smaller projects that have more benefit even if they cost more. They may serve special needs, the chronically homeless, or help achieve fair share goals. One added that impacted areas with few large sites are disadvantaged and that special needs projects are often smaller in order to overcome opposition.

Ten commenters, including two organizational commenters, stated that the size factor will hurt infill, TOD, and special needs projects. Five added that the size factor discourages projects in higher income communities where entitling large projects is more difficult and disadvantages projects from regions with small allocations when they compete in the set-asides. If a size factor is pursued, three of these commenters urged TCAC to lessen the impact, make the factor additive rather than a multiplier, and use a different measure than units. One argued that costs have leveled off, making slight cost savings not worth the negative impact on smaller projects. Two urged that any changes be phased in over time to protect pipeline projects.

One commenter expressed concern about the proposals to incentivize large projects because small projects have important policy outcomes and developers already have incentives to maximize project size. Moreover, in the city where this developer works, projects of 50 units or less are exempt from discretionary approvals, which reduces time and cost. She also stated that a size factor based solely on units will disadvantage large family projects and could fuel much smaller units. One- and two-bedroom units in large family projects will be disincentivized. The commenter recommends having no size factor but, if one is to exist, recommends first basing it on bedroom count and second reducing the benchmark from 70 to 35 units.

One commenter suggested making smaller additions or subtractions to the tiebreaker for project size, as opposed to using a multiplier.

One commenter stated that the size factor formula is extreme. A nudge for larger projects may not be bad, but it should not be disproportionate. He also stated that encouraging larger projects may undermine the other proposals to increase affordable housing in opportunity areas where projects tend to be smaller.

One commenter urged elimination of the size factor. As an urban developer, her projects all use density bonus law and are still under 70 units. If a size factor is maintained, she urged basing it on the number of bedrooms, not units.

One commenter suggested using 100 or 150 in the denominator of the size factor to make the regulations more consistent.

One commenter feels that the size factor unfairly punishes smaller and rural communities that are best served by smaller developments. Many such communities also cannot secure the resources to support large developments. The commenter suggested a size factor based on a 50-unit benchmark in the rural set-aside.

One commenter opposed inclusion of the size factor because smaller, more difficult infill projects may have attributes that outweigh an overly simplified size calculation. The proposal also favors development in outlying areas where land is more abundant. The commenter encouraged TCAC to consider a sliding scale for developers' fees instead.

Two commenters, including one organizational commenter, strongly opposed the size factor as it systematically discriminates against special needs projects competing in the geographic set-aside or other non-special needs set-asides.

One commenter opposed the size factor since it would render smaller projects less competitive.

One commenter opposed the size factor because the majority of sites identified in housing elements do not accommodate 70 units, so penalizing jurisdictions with smaller sites poses a serious impediment to their ability to meet their affordable housing objectives. In addition, this proposal promotes concentration of low-income families contrary to HUD policy. It is better to have two scattered site 35 unit project than one 70 unit project. The commenter suggested as an alternative or augmentation that projects benefit by achieving or exceeding the maximum density of a site.

One commenter stated that the size factor creates an unfair advantage for cities that have more resources to fund larger projects and that are less built out. The commenter suggested setting a floor of 30 units and rewarding projects with lower costs on a per unit or per bedroom basis. At a minimum, the commenter urged grandfathering projects that have already applied to TCAC and latter phases of a phased project.

One commenter opposed the size factor because it is more difficult to develop large properties in densely populated urban and suburban counties. This will also benefit smaller units at the expense of large family developments and discourage phasing.

One commenter opposed the size factor because it is discriminatory against high-income locales where housing is hard to locate and dense urban communities with few large parcels. The policy also is inconsistent with HUD policy to deconcentrate poverty to which Rental Assistance Demonstration projects are subject. The commenter also questions whether larger projects truly

are more cost effective and states that the proposal also seems at odds with TCAC's own policy shift to encourage more special needs housing.

One commenter supported promoting more unit production but does not think this is the best approach. The proposal would allow larger projects with less soft resources to achieve higher tiebreaker scores than projects with more leveraged soft resources and lower per unit total development costs. The commenter suggested extra points for projects that are below established cost benchmarks.

Credit efficiency factor

One commenter supported the change to the efficiency factor.

One commenter, endorsed by a second, stated that the emphasis on public funding in the current tiebreaker overweights public funds at the expense of cost effectiveness, drives public funding from the 4% program, and hurts smaller jurisdictions that lack access to public funds. The commenter urged TCAC to foster conservation of public funds at all levels and equally weight the public funding and credit efficiency factors in the tiebreaker.

One commenter opposed the proposed change to the credit efficiency factor, arguing that it will have unintended consequences of reducing the incentive for voluntary basis reduction and thereby result in more credits requested per project and fewer projects.

Five commenters stated that the proposed change to the credit efficiency factor will disadvantage SRO and special needs projects because the lower rents make them unable to carry higher amounts of hard financing. Two of these commenters added that applicants often must reduce basis to fall within the threshold basis limits and the amount of credits available in a region. These commenters suggested adding back only any reduction in eligible basis beyond the reductions to meet the threshold basis limits and credit availability. Two other commenters recommended dividing the amount added back by 3.

One commenter stated that adding public funds back to the credit efficiency ratio eliminates the penalty for higher costs in this factor. As a result, cost efficiency will have a lesser impact than the current formula, which is a step in the wrong direction.

One commenter believes the proposal should not reward projects that carry move private hard debt. Any factor under the control of the developer will be driven to extreme levels. In this case, it will drive lower operating expenses that are inappropriate.

One organizational commenter opposed the change and suggested that TCAC only add back any reduction beyond reductions to meet threshold basis limits and to fit the credit request within the amount available in a region.

One commenter suggested adding back only a portion of the soft resources to reduce the weighting of this change.

Health Care Services rental subsidies

Three commenters supported including California Department of Health Care Services rental subsidies to the list. Two of these suggested also adding Los Angeles County Department of Health Services subsidies and Veterans Housing and Homeless Prevention Program operating subsidies as well.

TCAC appraisal

One commenter supported TCAC having its own appraisal authority, provided the process is timely and transparent.

One commenter suggested creating a standard for when TCAC would order its own appraisal, such as when a reduction of 15% in the donated land valuation would alter project rankings.

Five commenters, including an organizational commenter, suggested that TCAC commission appraisal reviews rather than second appraisals for land donations. Two appraisers will often come to different value conclusions. A reviewer would only develop an independent opinion if the original appraisal were inappropriate or misleading. Two commenters suggested that applicants should have sufficient time to respond to any findings. Two of the commenters stated that if TCAC prefers ordering its own full appraisal then guidance is needed on when and how TCAC would do so.

One commenter understood the concern about inaccurate appraisals but requested greater clarification on the circumstances, timing, and process involved in obtaining a second appraisal. Given the layered and tightly timed funding process, it is essential that timing impacts are articulated. It is also important to articulate how final values will be established when there are differing appraisals. As an alternative, the commenter suggested that TCAC may wish to provide additional guidance to achieve greater standardization.

One commenter strongly disagreed with this proposal. While the commenter understood the concern, he stated that developers base their risk and feasibility standards, and therefore their predevelopment exposure, on early appraisals. TCAC's review would need to happen long before application submittal in order to avoid disruption to the developer's risk assessment. As an alternative, the commenter suggested that TCAC revisit its appraiser guidelines and/or require some level of appraiser certification.

Two commenters, including an organizational commenter, found this change troublesome. It is not clear when TCAC would exercise the authority. The cost and timing of the review could have detrimental impacts, and the process for reconciling differences is not well defined.

One commenter opposed having TCAC order second appraisals because it could be a slippery slope resulting in protracted appeals and legal battles.

One commenter opposed this proposal as an additional layer of review for projects that have already received appraisals consistent with all of TCAC's policies on appraiser certification, qualification, and standing.

Three commenters, including an organizational commenter, opposed this change because it would introduce too much uncertainty too late in the process without any opportunity for remedy.

One commenter opposed this provision because the applicant uses the appraisal to gauge competitiveness, and a change in tiebreaker score would result in the applicant investing time and resources under a false pretense. More rigorous standards or requiring TCAC approval of appraisers would be a better approach.

One commenter discourages TCAC from using its own appraisals as it is duplicative and not cost effective. At a minimum, the proposal needs more clarification and specificity on how TCAC will implement this.

One commenter opposed TCAC ordering a second appraisal as it creates uncertainty and unnecessary risk for applicants and their partners. TCAC could establish stricter metrics to guide appraisals in advance of submittal.

Response to Comments:

Expansion of public funds to soft leverage category

Staff agrees with the comment that resources provided pursuant to the U.S. Department of Justice's National Mortgage Settlement should not count as soft leverage as that would give a business advantage to lenders subject to the settlement. Staff has revised the language to exclude such funds from benefit in the tiebreaker.

Staff continues to believe that non-public land donated to a project should be held by the donor for some period of time prior to the donation in order to prevent abuse. Staff agrees, however, that 10 years is a long time and may disqualify many legitimate land donations. In an effort to balance these two objectives, staff proposed to reduce the seasoning requirement to 5 years.

While staff continues to believe that encouraging soft resources from unrelated private entities will benefit the program overall, staff also shares the concerns expressed by some commenters that this proposal may lead to abuse. Staff proposes to add language prohibiting the source of the private soft leverage from having received any benefit from a related party to the project. Staff also proposes defining a related party for purposes of this section as a member of the development team or a Related Party, as defined in the TCAC regulations, to a member of the development team. In addition, staff will monitor the use of private soft resources and make adjustments to the regulations in the future if necessary to mitigate or eliminate abuse.

Size factor

While staff maintains its interest in promoting larger projects that on average are more cost effective, staff concurs that small projects can provide important public benefits and may be the only option in infill areas, smaller communities, and communities that may be resistant to affordable housing.

In addition, it occurs to staff that cost effectiveness is not so closely related to size in rehabilitation projects as in new construction projects. Moreover, rehabilitation projects cannot change their size, and by encouraging portfolio applications for the rehabilitation of existing affordable housing developments, the proposed regulation changes would give these portfolio projects an inherent advantage from the size factor.

In an attempt to better balance these objectives and concerns, staff revises its size factor proposal to provide an increase to the soft leverage ratio only for projects containing 50 or more new construction units. Smaller projects and rehabilitation projects would receive no increase but also no penalty. In addition, staff proposes to revise the size factor formula to represent ¼ of the difference between the proposed number of new construction units and a hypothetical project of 50 new units. Staff reduced the benchmark from 70 units to 50 units in order maintain the disincentive for project downsizing for a larger subset of projects. Staff reduced the weighting of the size factor from ½ to ¼ of the difference to reflect the lower benchmark (which results in a higher multiplier) and to respond to comments that the originally proposed size factor was too strong.

While this revised proposal does advantage larger new construction projects over all rehabilitation projects, staff believes this offsets the advantage rehabilitation projects currently enjoy from counting assumed existing public loans towards the tiebreaker. In the first round of 2015, rehabilitation projects had an 85% success rate. New construction projects had only a 50% success rate. Staff believes that the revised size factor moves a step closer to creating a more even playing field between new construction and rehabilitation and incentivizes larger, more cost-efficient new construction projects.

In response to comments that the size factor will disadvantage various types of smaller projects that provide important public benefits, staff points out that the reduced size factor is one component of the total tiebreaker and unlikely to outweigh the advantage of public funds. Special needs projects in particular often have high public fund commitments and often benefit from the rental assistance increase. Moreover, special needs projects have their own set-asides that ensure a significant amount of credits to those projects. In addition, staff will monitor the outcomes of the next funding rounds to assess the impacts of this change.

In response to concerns that basing the size factor on units will push developers to propose more SRO and senior projects that can accommodate more units on a parcel, staff points out that the housing type goals for SRO, senior, and special needs projects are limited, such that developers moving to that project type to improve their tiebreaker score will take on a large risk that credits will be oversubscribed for these housing types. Staff does share the concern, however, that developers will be incentivized to provide fewer bedrooms in large family projects. For that reason, staff is suggesting a change to Section 10325(g)(1)(A) to require at least 25% of units in large family projects to be 2-bedroom units.

Credit efficiency factor

In response to a question at a public hearing, staff proposes to clarify that Tranche B loan proceeds will not be added back to the credit efficiency factor as other public funds are.

Staff acknowledges that ignoring credit reductions that are supplanted by public funds will disadvantage projects that cannot support much private debt. Staff points out, however, that SRO and special needs projects have their own set-asides and benefit in the tiebreaker by the counting of Tranche B loan proceeds, the increase for rental assistance, and the high weighting for public funds. Staff believes that such projects will continue to score well in spite of the change to the credit efficiency factor.

Staff also acknowledges that the change will disincentivize voluntary basis reductions. It is staff’s experience, however, that most voluntary basis reductions, including those to fall within the threshold basis limits or the amount of credits available in a region, are the result of public fund contributions filling the gap created by the reduction. Staff continues to believe that deemphasizing, at least in this small way, the leverage of one public resource with another and eliminating the double counting of public funds is a good policy.

As for the comment that the change to the credit efficiency factor lessens the impact of cost efficiency, staff points out that a project’s soft leverage ratio will increase with reduced project costs and that the soft leverage factor is weighted three times the credit efficiency factor.

While incentivizing hard financing may lead to pressures to reduce operating expenses, TCAC has minimum operating expense requirements, and lenders and investors will maintain an interest in ensuring that projects are properly operated and maintained.

Health Care Services rental subsidies

Staff is resistant to naming local sources of operating and rental subsidies as the list could become unmanageable. TCAC has and will continue to recognize other forms of operating and rental subsidies as appropriate.

TCAC Appraisal

Staff agrees with the comments that an appraisal review is more appropriate than a full second appraisal. Such a review would provide TCAC with a professional opinion as to the reasonableness of the original's work but only provide a second value if the first appraisal were considered inconsistent with recognized appraisal standards.

Staff also agrees that establishing criteria under which TCAC would seek a review would be helpful. Staff proposes that, at a time when TCAC has an appraiser under contract, it shall order a review if a 15% reduction in the value of the donated land and improvements would change an award outcome.

TCAC will only seek a review of an appraisal when it relates to the value of donated land for purposes of the tiebreaker. Because the donation is by definition free, a change in the value will only affect the tiebreaker scoring and not a project's financials. While developers do make decisions based on projected scoring and tiebreakers, TCAC reduces scores and tiebreakers regularly when a project's self-score fails to meet TCAC standards. As a result, staff continues to believe that reviewing appraisals related to donated land is important to ensure the integrity of the competition.

Revised Proposed Change:

(10) Tie Breakers

If multiple applications receive the same score, the following tie breakers shall be employed: For applications for projects within single-jurisdiction regional competitions only (the City and County of San Francisco and the City of Los Angeles geographic apportionments), the first tiebreaker shall be the presence within the submitted application of a formal letter of support for the project from either the San Francisco Mayor's Office of Housing or the Los Angeles Housing + Community Investment Department respectively. Within those cities, and for all other applications statewide, the subsequent tiebreakers shall be as follows:

First, if an application's housing type goal has been met in the current funding round in the percentages listed in section 10315, then the application will be skipped if there is another application with the same score and with a housing type goal that has not been met in the current funding round in the percentages listed in section 10315; and

Second, the highest of the sum of the following two ratios:

(A) Leveraged soft resources~~Committed permanent public funds~~, as described ~~in Section 10325(c)(1)(C)~~below, defraying residential costs to total residential project development costs~~, with the resulting figure multiplied by a size factor. The size factor shall equal fifty percent plus the total number of units divided by 140 (50% + (total units/140))~~. Except where a third-party funding commitment is explicitly defraying non-residential costs only, ~~public funds~~leveraged soft resources shall be discounted by the proportion of the project that is non-residential. ~~Permanent~~

~~funds~~Leveraged soft resources shall be demonstrated through documentation including but not limited to ~~public~~ funding award letters, committed land donations, or documented project-specific local fee waivers.

Leveraged soft resources shall include all of the following:

(i) public funds, as described in Section 10325(c)(1)(C).
(ii) soft loans that meet the criteria described in Section 10325(c)(1)(C) (except that terms shall be of at least 55 years), or grants, from unrelated non-public entities that are not covered by subparagraph (i) and that do not represent Financing available through the National Mortgage Settlement Affordable Rental Housing Consumer Relief programs. The entity providing the soft loans or grants shall not have received any benefit from a related party to the project
(iii) the value of donated land and improvements that are not covered by subparagraph (i), that meet the criteria described in Section 10325(c)(1)(C), and that are contributed by an unrelated entity (unless otherwise approved by the Executive Director), so long as the contributed asset has been held by the entity for at least ~~10~~ 5 years prior to the application due date. ~~The numerator of this ratio may include permanent funding committed by a Community Foundation or a charitable foundation where a public body appoints a majority of the voting members . Additionally the numerator may include the value of land and improvements contributed by an unrelated organization formed under Internal Revenue Code Section 501(c), so long as the contributed asset has been held by the organization for at least 10 years prior to the application due date. Such foundation or organization contributions must be in the form of a grant or residual receipts loan. Local land~~
Land donations include land leased ~~from a public entity, or permitted foundation or organization~~ for a de minimis annual lease payment. CTCAC may contract with an appraisal reviewer and, if it does so, shall commission ~~and use its own~~ an appraisal review if a 15% reduction in ~~to determine~~ the value of land and improvements contributed to a project would change an award outcome. If the appraisal review finds that the conclusions of the submitted appraisal are inconsistent with the data reported and with other generally known information, CTCAC shall use the value established by the appraisal reviewer.
(iv) For purposes of this section, a related party shall mean a member of the development team or a Related Party, as defined in Section 10302(gg), to a member of the development team.

Permanent funding sources for this tiebreaker shall not include equity commitments related to the Low Income Housing Tax Credits.

The numerator of projects with public operating- or rental-subsidies may be increased by 25 percent (25%) of the percentage of proposed tax credit assisted units benefitting from the subsidy. Such subsidies must be received from one or more of the following programs: Project Based Section 8; PRAC (Section 202 and 811); USDA Section 521 Rental Assistance; Shelter Plus Care; McKinney Act Supportive Housing Program Grants; Native American Housing Block Grant (IHBG); California Mental Health Services Act operating subsidies; California Department of Health Care Services; and Public Housing Annual Contributions contracts. Applicants seeking scoring consideration for other public sources of operating- or rent-subsidies must receive written Executive Director approval prior to the application due date.

The numerator of projects of 50 or more newly constructed units shall be multiplied by a size factor equal to seventy five percent plus the total number of newly constructed units divided by 200 (75% + (total newly constructed units/200)).

(B) One (1) minus the ratio of requested unadjusted eligible basis to total residential project development costs, with the resulting figure divided by three. For purposes of this tiebreaker paragraph only, requested unadjusted eligible basis shall be increased by the amount of any reduction to eligible basis that is less than or equal to the amount of leveraged soft resources, as described above but exclusive of donated land value and the amount of private "tranche B" loans underwritten based upon rent differentials attributable to rent subsidies, committed to the project.

Section 10325(f)(7)(A)

Initial Proposed Change:

With respect to energy efficiency, require building to code for new construction. Maintain 10% improvement requirement for rehabilitation projects generally at the project level and expand the lookback period for recent energy efficiency improvements to 5 years, including government programs. Require applicants to consult with the design team and energy efficiency experts early in the project design process to identify and consider cost-effective energy efficiency or generation measures beyond those required.

Comments Received:

Ten commenters, including one organizational commenter, supported relaxing the minimum construction standards related to sustainable building.

One commenter supported the requirement for applicants to consult with energy efficiency experts to identify efficiency measures beyond those required.

One commenter strongly urged that TCAC maintain some requirement for projects to exceed existing building codes for energy efficiency. Without a higher standard to meet, the proposed requirement for applicants to meet with the design team and energy efficiency experts is no different than a conventional kick-off meeting and will not lead to any efficiency improvements. Moreover, the proposed design meeting requirement does not define what the meeting should consist of and how its outcomes should be documented to TCAC. This may result in additional process costs with no additional benefit.

Two commenters requested that TCAC provide guidance on minimum qualifications for energy experts, documentation required, and the approval process.

One commenter agreed with the consultation requirement provided that compliance is evidenced by an applicant or architect certification and not a costly third party report or certification.

One commenter opposed the energy expert consultation requirement because the work and benefits are unclear and it could be a costly endeavor before the project is ready to move forward. The commenter also opposed the requirement to use the Sustainable Building Method Workbook to document compliance with CDLAC points.

One commenter opposed having TCAC monitor sustainability commitments for CDLAC, stating that CDLAC requirements should be monitored by CDLAC. The commenter added that this TCAC documentation will add to production time and expense.

Response to Comments:

Staff continues to believe that requiring new construction projects to build to California's most-stringent in the nation energy efficiency codes achieves important efficiency benefits and makes more projects financially feasible. Staff concurs, however, that more definition is warranted on what the consultation requirement should entail.

With respect to the comments regarding TCAC enforcing CDLAC sustainability commitments, TCAC is the entity that reviews 4% projects at placed in service and already confirms compliance with items in a CDLAC resolution. It would be duplicative for CDLAC to review applications at that time as well.

Revised Proposed Change:

(A) Energy Efficiency. ~~New construction buildings shall be thirty percent (30%) better than the 2008 Energy Efficiency Standards (California Code of Regulations, Part 6 of Title 24) including heating, cooling, fan energy, and water heating but not the following end uses: lighting, plug load, appliances, or process energy. Alternatively, new construction buildings may meet the 20 percent (20%) Zero Net Energy (ZNE) standard established in Section 10325(c)(6)(B)(ii).~~ New construction and rehabilitation applicants shall consult with the design team and ~~energy efficiency experts~~ a certified HERS rater or CABEC certified 2013 Certified Energy Analyst early in the project design process to evaluate a building energy model analysis and identify and consider cost-effective energy efficiency or generation measures beyond those required by this subsection. The application to CTCAC shall describe the measures recommended by the energy analyst and which options were incorporated into the project. In addition, a~~A~~ll rehabilitated buildings shall have improved energy efficiency above the modeled energy consumption of the building(s) based on existing conditions documented using the Sustainable Building Method Workbook's CTCAC Existing Multifamily Assessment Protocols and reported using the CTCAC Existing Multifamily Assessment Report template. Rehabilitated buildings shall document at least a 10% post-rehabilitation improvement over existing conditions energy efficiency ~~achieved for each building~~ achieved for the project as a whole, except that Scattered Site applications shall also document at least a 5% post-rehabilitation improvement over existing conditions energy efficiency achieved for each site. In the case of projects in which energy efficiency improvements have been completed within ~~two~~ five years prior to the application date pursuant to a public or regulated utility program or other governmental program that established existing conditions of the systems being replaced using a HERS Rater, the applicant may include the existing conditions of those systems prior to the improvements. Furthermore, ~~all~~ rehabilitation applicants must submit a completed Sustainable Building Method Workbook with their preliminary reservation application unless they ~~are not seeking competitive points under Section 10325(c)(6)(B),(E), or (G), and~~ are developing a project in accordance with the minimum requirements of Leadership in Energy & Environmental Design (LEED) or GreenPoint Rated Program. In addition, all applicants who will receive points from CDLAC pursuant to Sections 5230(k)(7),(9), or (10) of the CDLAC regulations must submit a completed Sustainable Building Method Workbook with their preliminary reservation application.

Section 10325(f)(7)(K)

Initial Proposed Change:

Apply the 10% mobility/4% communications accessibility requirement to new construction projects only.

Comments Received:

Thirteen commenters, including two organizational commenters, agreed with limiting the 10%/4% accessibility requirements to new construction. One stated he has found the higher standards to be cost prohibitive for many rehabilitation projects. Another stated that the change ensures accessibility without placing an undue burden on existing buildings with existing conditions.

One commenter strongly opposed applying the 10%/4% accessibility requirements only to new construction. A 50% reduction in accessible units has an enormous and detrimental impact on people with mobility and sensory disabilities, a population greatly at risk of homelessness. This change would have meant 310 fewer accessible units in 2014 and will mean that 95% of TCAC funded units will be completely unavailable. The commenter points out the existence of the waiver provision for cases where costs are excessive and argues that there is therefore no need to eliminate the obligation generally. Furthermore, cost concerns do not impact sensory disability accessibility requirements, which should remain at 4%.

One commenter opposed maintaining the 10%/4% standard for new construction, suggesting that all projects remain at code to reduce costs.

Response to Comments:

The originally proposed change applied the 10% mobility and 4% communications accessible unit requirement only to new construction projects. The intent, in essence, was to defer to the building code's standards for rehabilitation units. It occurs to staff, however, that the current regulations also set a higher bar for mobility accessibility in rehabilitation projects than does the building code. The current regulations require compliance with Chapter 11(B), whereas Chapter 11(A) of the building codes otherwise may apply. In TCAC's experience, this difference often requires the moving of walls, including load bearing walls, and other expensive structural modifications. Staff believes that applying the building code standards to rehabilitation projects will best balance accessibility with project feasibility. As a result, staff revises the proposed change to apply the entire paragraph as it relates to mobility accessibility, including the Chapter 11(B) requirement, only to new construction projects. However, staff does propose to maintain the 4% communications accessible requirement for rehabilitation projects as those present few cost concerns.

Revised Proposed Change:

(K) All new construction tax credit recipient projects shall adhere to the provisions of California Building Code Chapter 11(B) regarding accessibility to privately owned housing made available for public use. Tax credits shall be viewed as invoking those requirements as applicable, including ~~except that new construction projects shall include~~ a minimum of ten percent (10%) of the units with mobility features~~,~~ and four percent (4%) with communications features. All rehabilitation projects shall provide a minmum of 4% of the units with communications features consistent with California Building Code Chapter 11(B). ~~These Accessible~~ units shall, to the

maximum extent feasible and subject to reasonable health and safety requirements, be distributed throughout the project consistent with 24 CFR Section 8.26.

Section 10325(f)(7)(L)

Comments received:

TCAC Committee Member Betty Yee recommended that the regulations require irrigation only with reclaimed water, greywater, or rainwater (excepting water used for Community Gardens) in new construction projects, rather than allowing competitive points. The current drought and the possibility of on-going drier conditions in California as a result of climate change make it imperative to pursue all possible water saving measures.

Response to comments:

Staff proposes for new construction projects to remove the competitive points for irrigating with reclaimed water, greywater, or rainwater pursuant to Section 10325(c)(6)(F) and instead make this a minimum construction standard. Staff also proposes waiver authority for cases in which the system will be unnecessary as a result of de minimus landscaped areas or drought-tolerant landscaping that does not require irrigation.

Revised Proposed Change:

(L) New construction projects shall include systems sufficient to irrigate only with reclaimed water, greywater, or rainwater (excepting water used for Community Gardens) under normal conditions. At placed in service, the project architect shall certify that reclaimed water, greywater, or rainwater systems have been installed and are functioning properly to meet this requirement. The Executive Director may waive this requirement if the system will be unnecessary as a result of de minimus landscaped areas or drought-tolerant landscaping that does not require irrigation.

Section 10325(f)(10)

Initial Proposed Change:

Discount costs of leasing offices, parking facilities, or landscaping from the minimum rehabilitation thresholds.

Comments Received:

One commenter understands the desire behind the change but argued that parking and landscaping have real capital needs and that improvements benefit the residents. The exclusion of these particular costs seems arbitrary, creates a new compliance burden, and should be withdrawn.

Two commenters, including one organizational commenter, supported these changes but asked for consideration of drought tolerant landscaping, tot lots, and other recreational amenities.

Two commenters opposed the exclusion from threshold of costs related to leasing offices, parking facilities, and landscaping. One stated that prescribing a rigid standard for what should be included in threshold may prevent applicants from developing the most impactful scope of work to address the unique needs of the project.

One commenter opposed the exclusion of the costs of leasing offices, parking facilities, and landscaping from the minimum rehabilitation threshold because it will incentivize owners to ignore these needs. The commenter suggested that TCAC instead consider limiting these costs to a percentage of the total rehabilitation cost.

Five commenters opposed this change as the entire project benefits the residents. One said the increase in the threshold accomplishes much of the same goal. Two added that is it ironic that the proposed changes to the scoring reward use of non-potable water for irrigation but that this change deters improving the efficiency of existing landscaping. Two suggested allowing $3500-$10,000 per unit of these costs to count towards the threshold.

One commenter believes this proposal goes too far by dictating what rehabilitation is needed and urged TCAC to let developers, lenders, and investors decide.

Response to Comments:

Nothing in the proposed change disallows improvements to leasing offices, parking facilities, and landscaping. In addition, the proposed change does not exclude the costs of leasing offices, parking facilities, and landscaping from basis, just from the calculation of the minimum rehabilitation threshold. As a result, owners will still have a large incentive (i.e., tax credit equity and a higher basis on which the developer fee is calculated) to renovate these facilities when warranted.

The intent of the proposed change is to ensure that these are not the primary repairs and that repairs to structures and units receive adequate attention. Nonetheless, upon further reflection staff believes it is appropriate for some amount of costs associated with leasing offices, parking facilities, and landscaping to count towards the minimum rehabilitation threshold. Staff has revised the proposal to allow up to $4000 per unit in leasing office, parking, and landscaping costs for 9% projects to count towards the threshold. The focus on rehabilitating structures and units remains.

Revised Proposed Change:

(10) Projects applying for competitive Tax Credits and involving rehabilitation of existing buildings shall be required to complete, at a minimum, the higher of $40,000 in hard construction costs per unit or 20% of the adjusted basis of the building pursuant to IRC Section 42(e)(3)(A)(ii)(I). ~~Notwithstanding Section 10302(u), for purposes of meeting this threshold, hard construction costs shall not include~~ At least $36,000 in hard construction costs per unit shall be for rehabilitation costs other than the costs of rehabilitation for leasing offices, parking facilities, or landscaping.

Section 10325(g)(1)(A)

Initial Proposed Change:

Reduce the 3-bedroom requirement for large family housing to 25%.

Comments Received:

Seventeen commenters, including three organizational commenters, applauded reducing the percentage of three-bedroom units to 25%. One suggested further reducing the required percentage to 20% to better reflect current market demand. Three of these commenters suggested establishing a minimum number of two-bedroom units in large family projects to ensure that they do not consist solely of one- and three-bedroom units.

One commenter expressed concern about reducing the three-bedroom percentage because large family projects already don't primarily serve single parent families with two children. The market will not provide three bedroom units, so TCAC should provide relief.

Response to Comments:

Staff concurs with the comments that the regulations should establish a minimum number of two-bedroom units in large family projects to ensure that projects do not consist solely of one- and three-bedroom units. Staff proposes to set the requirement for 2-bedroom units in large family projects at 25%. This change also addresses some of the comments related to the size factor of the tiebreaker. Some commenters expressed concern that basing the size factor on units would push developers to provide the smallest units possible. Establishing a minimum requirement for 2-bedroom units in large family projects will protect against this outcome.

Revised Proposed Change:

(A) At least ~~thirty~~ twenty-five percent (~~30~~25%) of the Tax Credit units in the project shall be three-bedroom or larger units, and at least twenty-five percent (25%) of the Tax Credit units in the project shall be two-bedroom units, ~~with the remaining units configured based on the demand established in the basic threshold requirements~~ except that for projects qualifying for and applying under the At-risk set-aside, the Executive Director may grant a waiver from this requirement if the applicant shows that it would be cost prohibitive to comply;

Section 10325(g)(4)

Initial Proposed Change:

Eliminate the requirement for special needs projects to meet an additional housing type and clarify the minimum construction standards for non-special needs units.

Comments Received:

Five commenters appreciated the elimination of the requirement for special needs projects to meet a second housing type. One added that the unit mix and size requirements are reasonable,

provided there is waiver ability for SRO hotels whose existing configurations may not meet these requirements.

Three commenters, including one organizational commenter, supported the proposal for special needs projects to qualify as a second housing type but recommended that the proposed requirements for non-special needs units apply only to projects that restrict 50-75% of units for special needs.

One commenter supported this change but urged clarification of what circumstances may warrant a waiver.

One commenter strongly supported removal of the second housing type requirement but would like to see the unit mix requirement removed or better understand the circumstances under which a waiver would be approved.

One commenter stated that the second housing type currently required of a project with less than 75% special needs units can be SRO or senior housing type, which can create an appropriate mix of tenants, as easily as large family housing type. The commenter urged TCAC to keep the second housing type requirement but further reduce the 3-bedroom requirement if the non-special needs units use the large family housing type.

One commenter said that the language appears to prohibit non-special needs units from meeting SRO or senior requirements instead of large family requirements, and that requiring 10% 1-bedroom and 20% 2-bedroom units in projects whose non-special needs units are targeted to SRO or senior populations is not appropriate.

Four commenters, including an organizational commenter, supported eliminating the second housing type requirement but opposed the new unit mix requirement as it dictates family units which may not be appropriate. The special needs prescription of unit mix should be sufficient.

One commenter supported the elimination of the second housing type and opposes any incentive to build projects with 75% or more special needs units. The commenter also suggested eliminating the 2-bedroom requirement for non-special needs units in favor of greater flexibility and modifying the size requirements as larger units add cost.

Response to Comments:

Staff concurs with the comment to apply the non-special needs unit size and bedroom requirements only to projects with less than 75% special needs units. These projects currently have large flexibility to determine project layout, and staff agrees that specifying unit mixes for a small number of units is unnecessary.

Staff does believe, however, that specifying unit mixes for projects with a relatively large number of non-special needs units is appropriate but is willing to alter the unit mix requirements to reflect less of a family orientation. Staff proposes to clarify the waiver language to restrict waivers to rehabilitation projects on the theory that changing the mix of an existing project can be an expensive proposition.

Revised Proposed Change:

(4) Special Needs projects. To be considered Special Needs housing, at least 50% of the Tax Credit units in the project shall serve populations that meet one of the following: are individuals

living with physical or sensory disabilities and transitioning from hospitals, nursing homes, development centers, or other care facilities; individuals living with developmental or mental health disabilities; individuals who are survivors of physical abuse; individuals who are homeless as described in Section 10315(b); individuals with chronic illness, including HIV; homeless youth as defined in Government Code Section 11139.3(e)(2); or another specific group determined by the Executive Director to meet the intent of this housing type. The Executive Director shall have sole discretion in determining whether or not an application meets these requirements. In the case of a development that is less than 75% special needs: ~~the non-special needs units must meet another housing type (for example, large family), although the project will be considered as a special needs project for purposes of Section 10325. At~~ A) at least ~~10%~~ 20% of the non-special needs units in the project shall be one-bedroom units, and at least ~~20%~~ 10% of the non-special needs units in the project shall be larger than one-bedroom units~~, unless waived by the Executive Director~~; and B) ~~For non-special needs units,~~ studio or SRO units must include at least 200 square feet, one-bedroom units must include at least 500 square feet, and two-bedroom units must include at least 750 square feet of living space. These bedroom and size requirements ~~limits~~ may be waived for rehabilitation projects, at the discretion of the Executive Director;

Section 10326(g)(7)

Initial Proposed Change:

Require $15,000 in hard construction costs per unit in rehabilitation projects and $20,000 per unit if the project is a resyndication. Discount costs of leasing offices, parking facilities, or landscaping from the minimum rehabilitation thresholds.

Comments Received:

Three commenters supported the proposed minimum rehabilitation thresholds of $15,000 and $20,000. One stated it is unusual to spend less than these amounts.

One commenter recommended that the minimum rehabilitation thresholds be $15,000 for all projects. The commenter also said the exclusion of the offices, parking, and landscaping costs from the threshold will create substantial hurdles for projects that need these types of improvements.

One commenter recommended that resyndication projects have the same threshold. In addition, he stated that the 10-year hold rule can make it difficult to wait until a $20,000/unit threshold is feasible. A property might be for sale right after year 15 and it may be the only opportunity to resyndicate for 10 years. As for excluding certain costs, the commenter states that the developer and investor should best determine the allocation of rehabilitation dollars.

One organizational commenter opposed increasing the minimum rehabilitation threshold above $10,000 per unit. Such amounts may not be needed. The capital needs assessment should dictate the level of rehabilitation. The commenter also recommends deleting the exclusions for parking, leasing office, and landscaping, particularly in light of the drought.

One commenter states that the increased thresholds do not meet TCAC's stated goal of reducing costs and closing financing gaps by arbitrarily mandating project cost increases which may not

be supported by a physical needs assessment. Owners may discard perfectly performing building products to meet the standard. The commenter recommends keeping the $10,000 minimum or creating a staggered minimum based on age, such as $10,000 per unit for projects 15 to 17 years old and higher for older projects. The commenter also opposed the exclusions from the threshold.

Three commenters, including an organizational commenter, supported these changes but asked for consideration of drought tolerant landscaping, tot lots, and other recreational amenities.

One organizational commenter believes that allowable capital needs include maintaining leasing office, ensuring parking accessibility, and installing tot lots and drought-resistant landscaping.

One commenter agreed with the direction of this proposal but asked that drought tolerant landscaping and related irrigation, outdoor play structures, and seismic or other structural repairs to parking facilities that affect building integrity be counted towards the threshold.

One organizational commenter, endorsed by another commenter, opposed this proposal and suggested allowing rehabilitation costs associated with offices, parking, and landscaping to be included in the hard cost calculation but limited to $5,000 per unit towards the threshold.

Four commenters opposed this change as the entire project benefits the residents. One said the increase in the threshold accomplishes much of the same goal. Two added that is it ironic that the proposed changes to the scoring reward use of non-potable water for irrigation but that this change deters improving the efficiency of existing landscaping. One suggested counting up to $5000-$10,000 of such improvements towards the threshold or capping these improvements at 50% of the threshold.

One commenter understands the desire behind the change but argued that parking and landscaping have real capital needs and that improvements benefit the residents. The exclusion of these particular costs seems arbitrary, creates a new compliance burden, and should be withdrawn.

One commenter believes this proposal goes too far by dictating what rehabilitation is needed and urged TCAC to let developers, lenders, and investors decide.

Two commenters opposed the change because these amenities are very important to developments.

Response to Comments:

In TCAC's experience, very few rehabilitation applications propose less than $15,000 in hard construction costs per unit. This threshold seems in line with the market. Moreover, staff remains convinced that tax credits should be reserved for projects with significant rehabilitation needs. Staff proposed a lower threshold for existing non-tax credit projects because they are likely to be at-risk projects or conversions of market rate units to affordable units, for which syndication achieves additional public benefit. Existing tax credit projects are likely to have long remaining regulatory agreements. Staff remains convinced that a higher threshold is appropriate for resyndications to discourage the unnecessary resyndication of projects that have minimal rehabilitation needs.

With respect to proposed exclusions from the threshold, nothing in the proposed change disallows improvements to leasing offices, parking facilities, and landscaping. In addition, the proposed change does not exclude the costs of leasing offices, parking facilities, and landscaping

from basis, just from the calculation of the minimum rehabilitation threshold. As a result, owners will still have a large incentive (i.e., tax credit equity and a higher basis on which the developer fee is calculated) to renovate these facilities when warranted.

The intent of the proposed change is to ensure that these are not the primary repairs and that repairs to structures and units receive adequate attention. Nonetheless, upon further reflection staff believes it is appropriate for some amount of costs associated with leasing offices, parking facilities, and landscaping to count towards the minimum rehabilitation threshold. Staff has revised the proposal to allow up to $2000 per unit in leasing office, parking, and landscaping costs to count towards the threshold. The focus on rehabilitating structures and units remains.

Revised Proposed Change:

(7) Minimum Rehabilitation Project Costs. Projects involving rehabilitation of existing buildings shall be required to complete, at a minimum, the higher of:

(A) ~~$10,000~~$20,000 in hard construction costs per unit for resyndications and $15,000 in hard construction costs per unit for all other projects; or

(B) 20% of the adjusted basis of the building pursuant to IRC Section 42(e)(3)(A)(ii)(I)

~~Notwithstanding Section 10302(u), for purposes of meeting this threshold, hard construction costs shall not include~~ At least $18,000 in hard construction costs per unit for resyndications and at least $13,000 in hard construction costs per unit for all other projects shall be for rehabilitation costs other than the costs of rehabilitation for leasing offices, parking facilities, or landscaping.

Section 10327(c)(5)(A) – Structured Parking Threshold Basis Increase

Initial Proposed Change:

Prohibit threshold basis boost for structured parking for spaces beyond 1 space for studio/1 bedroom units and 1.5 spaces for 2+ bedroom units.

Comments received:

One commenter supported the change to the basis limit increase for parking but suggested that the threshold should include up to .15 spaces per unit for visitors and .05 spaces per unit for staff. Also, the threshold should be rounded to the nearest integer. The language should regulate only residential parking in mixed use projects.

One commenter supported this change but has concerns about how the thresholds may or may not meet local parking requirements and design standards.

Two commenters, including an organizational commenter, agreed with the policy direction but recommended the ratio for 3+ bedroom units be set at 2 spaces per unit. However, the commenter strongly disagreed with the "all or nothing" approach proposed and suggested limiting the boost only for those parking spaces in excess of the threshold.

One commenter pointed out that parking is mandated by local governments and often the first issue brought up in neighborhood meetings. The commenter requested that TCAC use the higher density bonus ratios (studio and 1-bedroom: 1 space per unit; 2-3 bedrooms: 2 spaces per unit; 4+ bedrooms: 2.5 spaces per unit) if it chooses to limit the basis increase. The commenter further urged TCAC to allow the basis increase for all spaces up to the threshold, as opposed to the "all or nothing" approach proposed.

One commenter stated that the change to the threshold increase for structured parking will have a significant negative impact while doing little to reduce parking requirements imposed by public bodies. Cities will not alter requirements, and developers will be forced to seek risky and time-consuming variances. NIMBY jurisdictions will be only too happy to maintain their requirements to discourage affordable housing.

One commenter urged reconsideration of the proposed change to the threshold increase for structured parking because it is unlikely to influence local governments unless they are predisposed to affordable housing already, which is rarely the case. More likely, the local government will not alter parking requirements, and the project will not pencil.

One commenter opposed the change because developers do not control parking and must comply with local parking requirements.

One commenter opposed the change because it ignores local requirements, may increase neighborhood opposition, and underestimates parking needs, which can average 1.75-1.8 spaces per unit in locations not near transit.

One commenter preferred that the Legislature address local government parking requirements for affordable housing. At a minimum, the commenter suggested pro-rating the parking basis boost for projects that exceed a threshold, as opposed to taking away the entire boost. A second commenter endorsed the pro-ration idea.

One commenter stated that the intent to affect local government parking requirements seems unrealistic. The effect will only be to put projects over the threshold basis limits.

One commenter stated that this policy unfairly penalizes developers for a city's existing policy on parking. Developers will have to seek lengthy variances, increasing costs and giving opponents an opportunity to stop or delay a project. While the commenter prefers no change, she recommends at a minimum an incremental reduction in the threshold basis limit increase and exempting spaces for non-income restricted units.

One commenter strongly opposed this provision as special needs projects have no influence over the amount of parking required and will have to seek challenging entitlements or risk infeasibility.

One commenter stated that residents in suburban locations without high quality transit need and have cars at a 1.7 space/unit ratio, though the projects on small sites or with expensive land still require structured parking. The proposed threshold is equivalent to a 1.3 to 1 ratio. The increase in spillover parking will make entitlements for large family projects more difficult. Moreover, there is no need to limit parking as the current increase covers only half the cost of structured parking, so developers have every incentive to reduce parking when allowed to do so. At a minimum, the commenter urged a ratio of 2 spaces for 3-bedroom units and excluding guest, employee, and commercial parking.

Two commenters, including one organizational commenter, opposed the change because lower-income households must often commute to jobs and there is already sufficient incentive to limit the number of spaces to only those absolutely needed.

One commenter opposed this change because it ignores actual costs and will leave developers looking for even more scarce public resources.

One commenter appreciated the intent but opposed the proposal as it would disadvantage projects in cities with higher requirements and where public transportation systems are insufficient. The result will be increased gaps and reduced project viability. At a minimum, the commenter urged a grandfathering of pipeline projects and a 3-year delay to give local governments time to change their policies.

One commenter urged a 2 spaces per unit ratio for managers' units regardless of size as localities will generally not allow reduced parking for these units.

One commenter agreed that local parking requirements are overly onerous but stated that the proposed thresholds are too low and unfairly penalize developers. It is unlikely to affect local zoning practices. The commenter encouraged TCAC to engage the Legislature.

One commenter opposed the change saying it shifts the burden of city parking requirements to the developer from the city. If the decision is not within the developer's control then the developer should not be penalized.

One commenter believes this provision will do more harm than good as it will render some projects infeasible. The commenter suggested at least matching the ratios in state density bonus law, limiting the provision to 9% projects and allowing a waiver process, especially for pipeline projects that have already been entitled.

Response to comments:

Staff is sympathetic to the concern that local governments will not alter parking policies and that projects requiring structured parking may then exceed threshold basis limits. Nonetheless, staff remains interested in finding a mechanism to encourage local governments to reduce the number of spaces that must be accommodated in structured parking given their expense. Staff concurs that the "all or nothing" approach may be too drastic but considers the idea of pro-rating the basis increase to maintain a positive effect while imposing less impact on a developer. The revised proposed change decreases the threshold basis limit increase by a percentage equal to the percentage by which the number of parking spaces exceeds the benchmark ratios.

State density law allows developers of affordable housing to obtain parking ratio of one space per unit for studio and one-bedroom units and two spaces per unit for two- and three-bedroom units without the need for a discretionary approval. As a result, the proposed change only has value if the ratios are lower than the density bonus entitlement.

Staff does concur that the proposed change should not apply to projects that have already received, or will imminently receive, entitlements.

Revised Proposed Change:

A seven percent (7%) increase to the unadjusted eligible basis for a new construction development where parking is required to be provided beneath the residential units (but not "tuck under" parking) or through construction of an on-site parking structure of two or more levels.~~, provided that the project will have no more than 1 parking space per studio or one-bedroom unit and 1.5 parking spaces for units with two or more bedrooms~~ Unless the project received entitlements prior to January 1, 2016, the increase shall be reduced in the proportion that the required parking exceeds 1 parking space per studio or one-bedroom unit and 1.5 parking spaces for units with two or more bedrooms;