

DEPARTMENT OF HOUSING AND COMMUNITY DEVELOPMENT**DIVISION OF STATE FINANCIAL ASSISTANCE****ASSET MANAGEMENT AND COMPLIANCE BRANCH**

2020 W. El Camino Avenue, Suite 400, 95833

P.O. Box 952054

Sacramento, CA 94252-2054

(916) 263-2771

www.hcd.ca.gov

ASSET MANAGEMENT AND COMPLIANCE (AMC)**ADMINISTRATIVE NOTICE
NOTICE NUMBER: 21-03**

DATE: May 7, 2021**TO: Sponsors and Borrowers****FROM: Steven Marshall, Section Chief
Asset Management and Compliance Branch****SUBJECT: Cash Flow Analysis and Determination of Annuity under the Housing
Loan Conversion Program (HLCP)**

Administrative Note: This Administrative Notice establishes a formal written notification of administrative guidelines that affect the operation of Department programs. This format is used to identify, clarify and record administrative guidelines and interpretations of public interest.

Purpose and Background

The purpose of this Administrative Notice is to provide guidance to Department staff, Project Borrowers, Sponsors and Management Agents on the criteria for determining cash flow calculations for HLCP projects whose original loan was funded under the Rental Housing Construction Program – Original (RHCP-O) pursuant to Health and Safety Code section 50515.2.

The State provides an annual rent subsidy (“Annuity”) to cover operating account shortfalls under the RHCP-O Program. The Department of Housing and Community Development (HCD) holds the Annuity Fund in a designated account known as the “938 Fund”. The State continued to provide the Annuity when a Project restructured under the HLCP Program however, the Annuity was restricted to units occupied by lower income tenants who were in residence at the time of the HLCP extension. The HLCP Program was discontinued after the promulgation of the Loan Portfolio Restructuring (LPR) Guidelines (Statutes of 2012, Chapter 780, Section 2 “AB 1699”).

Under the RHCP-O Program, a Project submits an annual Budget that estimates the operating shortfall for the upcoming fiscal year. The Department reviews this Budget and issues an Annuity subsidy based on the approved estimated operating shortfall. After the close of each fiscal year, the Project submits an Annual Report and Audit describing the actual operating account shortfall. The

Department reviews the Annual Report and Audit and reconciles the Annuity already sent to the project, in one of the manners listed in the tables below entitled Step One and Step Two. The Department may determine that either an Excess Annuity Payment (EAP), an Additional Annuity Payment (AAP) or an Excess Rent Revenue (ERR) Payment is due depending on how the actual operating shortfall (“negative cash flow”) or excess revenue (“positive cash flow”) changed.

An EAP is the payment back to the Department for the amount of annuity in excess of the amount actually needed. This amount is calculated when the audit is reviewed. After audit review, the borrower is sent a request for payment to be made within 30 days of the request.

An AAP is an additional payment to the project to cover any shortfall due to the insufficiency of the initial annuity payment. This amount is calculated when the audit is reviewed.

An ERR is the amount of positive cash flow from the Annuity-assisted units. This amount is calculated when the audit is reviewed. The borrower is sent a request for payment to be made within 30 days of the request for RHCP-O Projects; however, repayment does not apply under the HLCP Program.

Under the RHCP-O Program it is possible to have a Project owe both an EAP and an ERR. This occurs when a Project received an Annuity at the time of Budget approval and subsequently the Project had positive cash flow as determined by the Annual Report/Audit. The Project pays the Department an EAP for the Annuity paid at the time of Budget and then pays an ERR for the remaining positive cash flow. Because ERR repayment does not apply to Projects under the HLCP Program, any positive cash flow for Annuity Assisted Units is applied to the total cash flow for the Project.

The HLCP Program requires a specific priority of cash flow based on the HLCP Guidelines and corresponding Regulatory Agreement (RA). The Department will use the original guidelines under the RHCP-O Program for purposes of the Annuity (HLCP RA Annuity Special Terms and Conditions). The Department will use the HLCP Guidelines for all other components of the Project. The EAP and AAP apply under the HLCP Program but only for cash flow associated to units that are eligible for the Annuity under the RA (see Step One and Step Two tables below).

The Department will use the following steps when determining cash flow for HLCP Programs.

Step One: Determine the cash flow for the Annuity Assisted Units and the Non-Annuity Assisted Units.

Annuity Assisted Units – Cash Flow Computation	Non-Annuity Assisted Units – Cash Flow Computation
Revenue – Expenditures = Adjusted Net Operating Income per the RHCP-O Regulations	Revenue – Expenditures = Adjusted Net Operating Income per the HLCP Regulations
Mandatory Debt – No mandatory debt payment is allowed.	Mandatory debt including, but not limited to, the 0.42% HCD Mandatory Debt per the terms of the RA
Reserves – Prorated deposit (Annuity Assisted Units/Total Project Units) into the Replacement Reserve Account	Reserves – Prorated deposit (Non-Annuity Assisted Units/Total Project Units) into the Replacement Reserve Account. Full deposit into the Operating Reserve (OR) Account and in other required Reserve Accounts per the RA

Step Two:

- 1. Determine the total cash flow (revenue from Annuity Units plus Non-Annuity Units and commercial revenue, if any)**
- 2. Determine the amount of Annuity due to the Project**
- 3. Determine any EAP or AAP; Underfunded Reserve deposits required and not made as part of Step 1; Asset Management Fee (AMF); Deferred Developer Fee (DDF); Borrower Distributions and Residual Receipt Payments. The table below includes all of the possible cash flow scenarios (per HCD's approval of the Annual Report/Audit).**

Annuity Assisted Units – Cash Flow Prior to Distributions	Non-Annuity Assisted Units – Cash Flow Prior to Distributions	Total Cash Flow	Annuity, EAP, AAP, AMF, DDF, Borrower Distributions, and Residual Receipt Payments
Positive	Positive	Positive	<ol style="list-style-type: none"> 1. No Annuity 2. EAP – The Borrower submits any difference to the Department in the form of an EAP payment. 3. AAP – N/A 4. Any Annuity Assisted Unit positive cash flow will be applied to the total cash flow computation for the Project 5. Deposits to Underfunded Reserves, if any 6. AMF, DDF, Borrower Distributions and Residual Receipts disbursed per the RA.
Positive	Negative	Positive	<ol style="list-style-type: none"> 1. No Annuity 2. EAP – The Borrower submits any difference to the Department in the form of an EAP payment. 3. AAP – N/A 4. Any Annuity Assisted Unit positive cash flow will be applied to the total cash flow for the Project 5. Deposits to Underfunded Reserves, if any

Annuity Assisted Units – Cash Flow Prior to Distributions	Non-Annuity Assisted Units – Cash Flow Prior to Distributions	Total Cash Flow	Annuity, EAP, AAP, AMF, DDF, Borrower Distributions, and Residual Receipt Payments
			6. AMF, DDF, Borrower Distributions and Residual Receipts disbursed per the RA.
Positive	Negative	Negative	<ol style="list-style-type: none"> 1. No Annuity 2. EAP – The Borrower submits any difference to the Department in the form of an EAP payment. 3. AAP – N/A 4. Annuity Assisted Unit positive cash flow will be applied to the total cash flow for the Project 5. Underfunded Reserves – N/A 6. No AMF, DDF, Borrower Distributions and Residual Receipts 7. Borrower is required to cover the resulting negative cash flow
Negative	Positive	Positive	<ol style="list-style-type: none"> 1. No Annuity – Apply all cash flow from the Non-Annuity Assisted Units to the Annuity Assisted Units after all underfunded reserves are fully funded and in advance of receiving an AMF, DDF, Borrower Distributions and Residual Receipts. 2. EAP – The Borrower submits any difference to the Department in the form of an EAP payment. 3. AAP – N/A 4. AMF, DDF, Borrower Distributions and Residual Receipts disbursed per the RA
Negative	Positive	Negative	<ol style="list-style-type: none"> 1. Annuity – Apply all cash flow from the Non-Annuity Assisted Units to the Annuity Assisted Units after all underfunded reserves are fully funded. Calculate the available Annuity on any remaining operating shortfall for the Annuity Assisted Units and issue to project as an AAP. 2. EAP – The Borrower submits any difference to the Department in the form of an EAP payment. 3. Additional AAP to the Borrower, if applicable. 4. AMF, DDF, Borrower Distributions and Residual Receipts – N/A
Negative	Negative	Negative	<ol style="list-style-type: none"> 1. Annuity – Calculated based on the Annuity Assisted Units only. Additional Annuity may be issued to the Project if the Project’s Annual Report demonstrated a higher need for an Annuity than was originally issued per the Operating Budget.

Annuity Assisted Units – Cash Flow Prior to Distributions	Non-Annuity Assisted Units – Cash Flow Prior to Distributions	Total Cash Flow	Annuity, EAP, AAP, AMF, DDF, Borrower Distributions, and Residual Receipt Payments
			<ol style="list-style-type: none"> 2. EAP – The Borrower submits the difference to the Department in the form of an EAP payment. 3. AAP - The Department issues the difference to the Project to cover the additional Operating shortfalls. 4. Underfunded Reserves – N/A 5. AMF, DDF, Borrower Distributions and Residual Receipts – N/A because the Project overall had negative cash flow 6. Borrower is required to cover the resulting negative cash flow for Non-Annuity Assisted Units

0.42% Mandatory Payment to HCD

The 0.42% payment (monitoring fee) amount that is due will be reflected in the RA. The Borrower is required to pay the 0.42% from the Non-Annuity Assisted Units cash flow because mandatory debt including the 0.42% is not an Annuity eligible expense.

Operating Reserves

The RA may require the Project to hold an OR Account, however not all HLCP RAs included this requirement. The Project also may elect to establish an OR Account, when one is not required, upon the Department’s prior written approval. The Department may approve an account balance not to exceed amounts outlined in the Uniform Multifamily Regulations section 8308 pursuant to HLCP Guidelines section 112. The Borrower may have capitalized the OR (if created voluntarily or if required in the RA) at the time of conversion to HLCP. However, if they have not capitalized an OR, the project shall only fund this account with positive cash flow from the Non-Annuity Assisted Units (see Step 1) or under certain cash flow circumstances when the Project is not eligible for any Annuity due to positive cash flow (see Step 2). The Department will provide the Project an Annuity for any allowable operating shortfalls for only the Annuity Assisted Units. The Project can request an OR withdrawal, subject to the Department’s prior written approval, to cover any unanticipated operating shortfalls for Non-Annuity Assisted Units.

For further information, please contact your AMC Fiscal Representative, or the Asset Management and Compliance Branch at AMCBranch@hcd.ca.gov.