Date of Hearing: July 16, 2025

ASSEMBLY COMMITTEE ON HOUSING AND COMMUNITY DEVELOPMENT
Matt Haney, Chair
SB 686 (Reyes) – As Amended July 7, 2025

SENATE VOTE: 38-0

SUBJECT: Housing programs: financing

SUMMARY: Changes recently passed trailer bill language in AB 130 (Committee on Budget), Chapter 22, Statutes of 2025 that authorized the Department of Housing and Community Development (HCD) to allow owners of developments with affordable housing funding from HCD to extract equity for specified purposes. Specifically, **this bill**:

1) Adds to the list of eligible uses of extracted equity, reimbursement of borrower advances for predevelopment costs, unreimbursed capital improvements, and unreimbursed operating deficits.

2) Revises the definition of "extracted equity" to mean "distributed funds that are financed with debt that is secured by a department-regulated property" rather than "debt added on to a department-regulated property."

EXISTING LAW:

1) Authorizes HCD, to the extent permitted under federal law and the California Constitution, to allow an owner of a property subject to a regulatory agreement with the department to take out additional debt from a development to finance rehabilitation of the property or investment in new affordable housing if all of the following conditions are met:

    a) All hard debt, including the additional debt, is underwritten with a debt-service coverage ratio of at a minimum 1.15 and is demonstrated to project positive cash flow for 15 consecutive years. For the purposes of this subdivision, "hard debt" means debt that must be repaid via an amortizing payment or at a specified maturity date;

    b) Any new debt is subordinate to the department's lien and regulatory agreement, as applicable, unless the department reasonably determines that subordination of the department's lien is necessary for the feasibility of a project and to fund reasonable rehabilitation or improvements, including soft costs;

    c) Any extracted equity is any of the following:

        i) With HCD's approval, contributed to other projects that will increase or improve the supply of deed-restricted affordable housing serving low-income households in the state;

        ii) Utilized in the purchase of a limited partner interest of a tax credit investor in the project, provided that the amount used to purchase that interest shall be subject to the guidelines adopted, as specified;

iii) Utilized in the payment of any unpaid deferred developer fee for the project pursuant to any applicable department regulations;

iv) Applied toward payment for necessary repairs and rehabilitation of the project;

v) Utilized for the establishment or replenishment of department-approved project reserves; or

vi) Utilized for any other purposes approved by the department.

d) The department's regulatory agreement remains in place for the project for its remaining term. If equity is extracted for purposes allowed, the department's regulatory agreement will be recorded in a senior position; and

e) The department continues to be entitled to receive monitoring fees to ensure compliance with the existing regulatory agreement. (Health and Safety Code (HSC) Section 50406.4)

2) Defines "extracted equity" to mean debt added to a department-regulated property that is used for any of the following purposes:

a) Approved project rehabilitation work;

b) To pay off existing debt;

c) Replenishment of reserves; or

d) Other department-approved project specific uses. (HSC 50406.4)

FISCAL EFFECT: Unknown.

COMMENTS:

Author's Statement: According to the author, "California is in a serious deficit of affordable housing supply. Investing and financing affordable housing are key tools to addressing the housing supply deficit. With the passage of AB 130, the Department of Housing and Community Development (HCD) may now accept the early repayment of loans by housing developers. With the approval of HCD, developers can now leverage extracted equity to create more affordable housing projects or for the preservation of existing affordable housing. SB 686's previous language was included in this trailer bill and will unlock millions of dollars to be used on more affordable housing projects. The bill now seeks to follow up on this investment by addressing the lack of clarity involving permitted uses of the extracted equity and better define the term extracted equity."

Affordable Housing Finance: The state finances affordable multifamily rental housing using a combination of loans, tax credits, and private activity bonds. Unlike market rate housing, affordable housing does not have the cash-flow from rents to support traditional financing. Affordable housing is provided to tenants whose household income is below the area median income (AMI). To qualify, very low-income tenants must make 60% or less of the AMI and lower-income tenants must make 80% or less of AMI. Tenants in affordable housing are only required to pay 30% of their income toward rent, so the state provides enough long term subsidy to reduce the overall debt service on a development. HCD loans serve as the permanent financing

that comes in once a development is complete to take out the predevelopment and construction loans a developer took on to construct the development. HCD loans are secured with a lien in first position on the property. Developments are also subject to a 55-year recorded regulatory agreement which runs with the project. If a developer pays off an HCD loan before the covenants expire, the regulatory agreement is not extinguished and the developer must continue to provide the units at an affordability rent for the length of the regulatory agreement to lower-income tenants.

Challenges Facing Affordable Housing Developments: Due to several factors including the depletion of operating reserves resulting from the COVID-19 eviction moratorium and unprecedented increases in insurance rates, affordable housing developments are facing financial challenges. Enterprise Community Partners recently conducted a survey of 130 affordable properties and found that on average the developments were experiencing insurance cost increases of 70%, with some providers reporting increases up to 500%. Because rents are capped, these properties have fewer options to cover these increases. In some cases, the situation is made worse because the project's operating reserves have not recovered from the eviction moratorium. Due to these financial pressures some properties are at risk of foreclosing or becoming market-rate developments, which would eliminate vital affordable housing units.

Recent Trailer Bill: Just last month, the Legislature approved and the Governor signed a budget trailer bill, AB 130 (Committee on Budget), Chapter 22, Statutes of 2025, which authorized HCD to allow owners of affordable housing developments financed with HCD loans to extract equity from the development for specified purposes. HCD has ultimate authority to allow an extraction of equity and while there is a list of specified uses of equity withdrawals including, approved project rehabilitation work, to pay off existing debt, and replenishment of reserves, the bill also gave HCD broad authority to approve other uses. Any new debt must be subordinated to HCD's lien and regulatory agreement unless the department determines that subordination of its lien is necessary for the feasibility of the project and to fund the rehabilitation or improvements.

This bill would add to the list of eligible uses of extracted equity, reimbursement of borrower advances for predevelopment costs, unreimbursed capital improvements, and unreimbursed operating deficits. In addition, this bill revises the definition of "extracted equity" to mean "distributed funds that are financed with debt that is secured by a department-regulated property" rather than "debt added on to a department-regulated property." According to the sponsors, they are in discussions with the department about the need to make these changes which they view as clarifying.

Arguments in Support: According to the bill's cosponsor, the California Council for Affordable Housing, "The amendments in SB 686 serve as essential clarifying revisions to the language in the budget trailer bill. These amendments provide clarification on the following points:

- Amendment 1: Section 50406.4(c)(1) – This language clarifies that the permitted uses for extracted equity include reimbursements for borrower advances for predevelopment costs, unreimbursed capital improvements, and unreimbursed operating deficits and that these things are allowable. This amendment makes the language consistent with the permitted uses described in 50560(e).

- Amendment 2: Section 50406.4(c)(2). – The language in the budget bill describes extracted equity as 'debt added' to a property. This is confusing and inaccurate because,

> in these circumstances the purpose of the law is to allow for the debt to be repaid to HCD, effectively removing the debt rather than adding debt. This amendment clarifies that 'distributed funds that are financed with debt that is secured by a department-regulated property…' which more accurately describes the action."

Arguments in Opposition: None on file.

Related Legislation:

AB 130 (Committee on Budget), Chapter 22, Statutes of 2025: Authorized HCD, to the extent permitted under federal law and the California Constitution, to allow an owner of a property subject to a regulatory agreement with the department to take out additional debt from a development to finance rehabilitation of the property or investment in new affordable housing if specified conditions are met.

AB 913 (Celeste Rodriguez), of this legislative session, would authorize HCD to take specified actions to improve the fiscal integrity of an affordable housing development financed with department resources. This bill is pending a hearing in the Senate Appropriations Committee.

AB 2638 (Ward, 2024) would have authorized HCD to approve the payoff of an HCD loan in whole or part, prior to the end of its term, and the extraction of equity from a development for purposes approved by HCD. This bill was held on the Senate Appropriations Committee suspense file.

AB 515 (Ward, 2023) would have authorized HCD to approve the payoff of an HCD loan in whole or part, prior to the end of its term, and the extraction of equity from a development for purposes approved by HCD. This bill was held on the Senate Appropriations Committee suspense file.

REGISTERED SUPPORT / OPPOSITION:

Support

California Council for Affordable Housing (Sponsor)
California Housing Consortium (Co-Sponsor)
California Housing Partnership
Housing Action Coalition
Housing California
MidPen Housing Corporation
Resources for Community Development

Opposition

None on file.

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