

Office of the City Auditor

**Report to the City Council
City of San José**

**AFFORDABLE
MULTIFAMILY HOUSING
LOAN PORTFOLIO:
CLEARER GOALS AND
STRONGER OVERSIGHT
WOULD IMPROVE
MONITORING**

**Report 26-03
June 2026**

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June 5, 2026

Honorable Mayor and Members
Of the City Council
200 East Santa Clara Street
San José, CA 95113

Affordable Multifamily Housing Loan Portfolio: Clearer Goals and Stronger Oversight Would Improve Monitoring

Affordable housing serves low- to moderate-income residents in the city of San José. To support the development of affordable multifamily housing, the City's Housing Department (Housing) provides loans to developers for the construction of new properties and the preservation of existing properties. Along with the loans come restrictions on tenant rents and income to ensure that the units remain affordable. Over the life of the agreement and the affordability period, Housing staff should verify that property owners repay loans, meet affordability restrictions, and maintain buildings. The permanent loan portfolio totals over \$745 million. There are nearly 25,000 units with active loans, affordability restrictions, or are in the pipeline across roughly 220 properties. Many loans were recorded before 2012 and are also subject to regulations from lenders and government agencies, including the state and the federal government.

The objective of this audit was to assess Housing's processes for managing the affordable housing loan portfolio, including loan servicing and compliance monitoring.

Finding 1: Housing Should Assess the Asset Management Team's Goals and Resources. The Asset Management team's role is to monitor loan compliance for the City's affordable housing loan portfolio. This involves verifying that borrowers repay City loans, housing units comply with affordability restrictions, and properties are appropriately maintained. We found:

- The team has not completed all annual property reviews or inspections in recent years for the more than 200 properties in the multifamily portfolio. Housing reports that staff have historically not been able to complete all reviews annually. Additionally, field audits have been on pause since 2024.
- Vacancies, unclear expectations, and inadequate software have hindered the team's ability to complete its work.

Recommendations: Housing should:

- Develop a program-level strategic plan to identify program goals and resource needs.

- According to Housing, current software tools are not sufficient to meet the goals of the program given the size and scope of the loan portfolio. Housing is developing an automated rent roll portal to assist with reviews.
- Housing is working on documenting procedures, which would support staff to complete their work consistently.

- Reconfigure the current software or acquire an asset management software platform.
- Update and standardize operating procedures and training.

Finding 2: Housing Should Strengthen Oversight of Affordability Restrictions and Higher-Risk Properties.

Some properties in the affordable housing portfolio do not comply with affordability restrictions, have not submitted required documentation, or have repeated property violations. We found:

- In a limited sample of 878 units across 10 properties (4 percent of the total units managed), 110 units had tenants with incomes above the cap for their unit type (13 percent of the sample); 48 units had tenants that earned 140 percent or more (5 percent).
- Housing does not have a documented escalation process to address compliance or property violations.
- Despite differences in property compliance, the Asset Management team’s current approach does not differentiate financial and affordability monitoring based on the risk of the property.

Recommendations: Housing should:

- Develop policies for addressing over-income tenants and resolving significant or repeated property concerns at higher-risk properties.
- Establish a risk rating system to prioritize compliance monitoring.

This report has nine recommendations. We plan to present this report at the June 15, 2026, meeting of the Community and Economic Development Committee of the City Council. We would like to thank the Housing Department for their time and insight during the audit process. The Administration has reviewed the information in this report, and their response is shown on the yellow pages.

Respectfully submitted,



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Background

Affordable housing serves low- to moderate-income residents in the city of San José. Affordable units have rents with utilities and fees limited to 30 percent or less of the target household income. Affordable multifamily housing includes deed-restricted projects in which all units are income restricted, as well as mixed income projects that provide both market-rate and below-market-rate rental units.

The City's 2023-2031 Housing Element identifies a goal of having an abundant and affordable housing stock:

Housing is essential to a healthy life and must be available to everyone at a reasonable cost. San José needs to support the creation of enough homes over the next eight years to ensure there is an affordable home for every household. While the City does not itself build homes, the City can create policies and programs that increase the rate at which homes are built and ensure a diversity of housing types to meet different needs.

To support the development of affordable multifamily housing, the City's Housing Department (Housing) provides loans to support new construction and the preservation of existing properties. The loans help cover remaining project costs, support site acquisition or rehabilitation, and ensure long-term affordability.

When the City loans money to developers for affordable housing projects, the agreements include restrictions on how much income tenants can make for each unit type and limits on allowed rents. These caps continue for a period of time—usually 55 years—with annual revisions based on area median income changes. Additionally, regulations allow for annual rent adjustments.

The objective of this audit was to assess Housing's processes for managing the affordable housing loan portfolio, including loan servicing and compliance monitoring.

Funding for Affordable Housing Developments

To build an affordable multifamily housing project, developers will typically put together a package that combines their own funds, a City gap financing loan, tax-exempt bonds, equity from the sale of tax credits, and other state or federal grants and loans.

The City's local funding includes revenues from the City's Real Property Transfer Tax (Measure E), the Low and Moderate Income Housing Fund, and the Inclusionary Fee Fund. These funds support the creation, acquisition and rehabilitation of affordable housing. The City issues loans to developers with these funds and signs loan agreements to dictate the terms of repayment and the affordability restrictions that apply to the property. Some of the City's loans were

made under the former San José Redevelopment Agency, which was dissolved in 2012. At the time of the audit, active loans dated from 1989 through 2025, and around two-thirds of the loans were recorded before 2012.

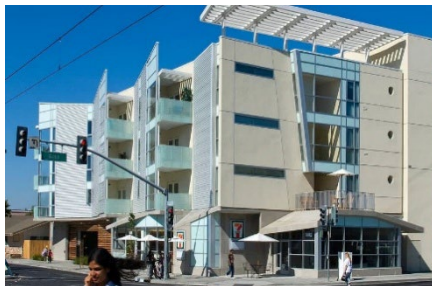
Among the funding sources is pass-through federal grant funding that is dedicated for affordable housing. This includes loans through the HOME Investment Partnerships Program, which are provided by the U.S. Housing and Urban Development Department. The City also issues tax-exempt bonds, as allocated by the state, to qualifying projects.

The City’s Multifamily Loan Portfolio

Housing maintains a significant multifamily loan portfolio. In total, there are nearly 25,000 units with active loans, affordability restrictions, or in the pipeline.

- Outstanding multifamily permanent loans had a balance of approximately \$745.6 million across 94 properties as of January 2026. This includes local funding as well as loans the City has made with grant funding (such as HOME loans). Loan balances ranged from \$60,000 to \$44 million, with an average balance of \$7.9 million.
- There are nearly 130 other properties that the City actively monitors for affordability restrictions or have funding committed or are in the pipeline.
- In FY 2024-25, the City received approximately \$18.1 million payments for principal, interest, and monitoring fees.¹

Exhibit I: Multifamily Properties Offer Affordable Housing



Gish Apartments



Markham Plaza II



Mayfair Court (interior)



Pollard Plaza (interior)

Source: Housing Department online material

¹ The calculation includes only the loan servicing fee and the affordability restriction monitoring fee.

The City's Loan Structure

The City's multifamily loans are typically made as gap financing. This strategy is to offer just enough financing (through a long-term, low-interest loan) to make an affordable housing project financially attractive to a developer. This will generally be included within a broader financial package that may include other financing tools, including state and federal loans, tax exempt bonds, and other sources (described previously).

The City's loans are structured with low or no interest and are repaid as a portion of the remaining income after eligible expenses and senior debt to other lenders is already repaid. These are called "net cash flow payments."

Properties Have Varying Target Populations and Repayment Expectations

Properties in the City's portfolio serve a mix of target populations, ranging from extremely low-income households to moderate-income. Rent limits correspond to the target population for a particular unit: a unit intended for an extremely low-income household will have a lower limit than a unit intended for an above low-income household. They also vary based on apartment size. In 2025, for example:

- A one-person household making \$27,320 was at 20 percent of the area median income. For this household, a one-bedroom apartment had a rent cap of \$781 per month.
- A four-person household making \$117,120 was at 60 percent of the area median income. For this household, a three-bedroom apartment had a rent cap of \$2,928 per month.

Depending on the target population, rents charged can vary between properties. For example, a two-bedroom apartment had rent limits between \$658 per month (for households at 15 percent of area median income) and \$5,271 per month (for households at 120 percent of the area median income). This can result in variances of how much income the properties make, which affects the net cash flow payments to the City.

Not every project that the City funds is expected to fully repay its City loan. In some cases, the City's loans are written such that the loans will be forgiven at the end of the affordability restriction. Loans can also be renegotiated with an increased affordability period or restructured to extend the loan, change the terms, or make other amendments.

The City's Loan and Affordability Monitoring

Multifamily affordable loan oversight is shared between City and external partners. The City monitors loan repayments and long-term compliance with its affordability restrictions, which typically last for 55 years. State and federal agencies may provide additional monitoring tied to their respective funding or regulatory

programs. For developments assisted by multiple funding sources with income restrictions, Housing’s expectation is that the most restrictive limits are applied to comply with all programs’ rules.

Housing’s Asset Management team oversees long-term monitoring of the City’s affordable housing loans with local funding, state funding, federal funding, and for projects with tax-exempt bonds. This includes reviewing audited financial statements, monitoring reserve requirements, verifying rent and income compliance, and conducting physical inspections. At the time of the audit, there were five active staff and two vacancies. Active staff included a senior development officer, two development officers, a development specialist, and a building rehabilitation inspector. Two team members joined the City within the last two years, and two joined during the audit.

Any property that has a City loan, affordability restrictions, or bond requirements is subject to some type of property review. The Asset Management team monitors multiple aspects of affordable housing properties and units. Depending on the specific terms of the loan agreement, the City may charge monitoring fees for both loan servicing and affordability restriction monitoring.

Housing’s role is to provide asset management. Per industry guidance, asset management involves monitoring the financial performance of the property, including long- and short-term goals, and analyzing an overall property portfolio. This differs from property management, which handles the day-to-day operations of running the facility.

| | Purpose | Process |
|-------------------|--|---|
| Financial Reviews | <p>Financial reviews are conducted to determine whether borrowers are repaying loans correctly and expenditures are appropriate. Staff should examine audited financial statements, operating budgets, and other documentation required to be submitted by property owners. If staff do not perform financial reviews, the City could be foregoing revenue from net cash flow payments or miss indicators of poor financial performance.</p> <p>In addition, staff monitor rehabilitation and replacement reserve and operating reserve levels to ensure borrowers are sufficiently planning for future building needs. Loan documents may also require rent burden reserves and resident services reserves.</p> | <p>Loan agreements require borrowers to submit information annually, including:</p> <ul style="list-style-type: none"> • Annual audited financial statements and net cash flow calculations • Long-term capital improvement plans • Detailed and summarized operating budgets • Replacement reserve expenditures • A vacancy loss report • Evidence of insurance coverage <p>At a minimum, staff are expected to review the audited financial statements and net cash flow calculations to verify that borrowers’ net cash flow payments are accurate.</p> <p>Staff also approve requests to draw from rehabilitation and replacement reserves.</p> |

| | | |
|---|--|---|
| <p>Affordability Restriction Monitoring</p> | <p>Purpose</p> <p>The City’s loan agreements require that tenants’ rents fall below certain limits. There are also limits on tenant incomes at move-in. Affordability restriction monitoring involves checking whether properties are complying with these restrictions, such that units remain affordable.</p> | <p>Process</p> <p>Property managers submit rent rolls with rent levels and tenant income information to Housing staff. Staff should then check whether the rents are within the allowed rent limits for the unit type and may check tenant incomes.</p> <p>Staff also should be conducting field audits to verify the accuracy of the information included in the rent rolls. For projects with federal HOME funding, periodic field audits may be required.</p> |
| <p>Property Inspections</p> | <p>Purpose</p> <p>Housing conducts property inspections to review the physical condition of properties. Building inspections enable the City to monitor the building’s condition and any problems that need to be addressed to maintain the long-term viability of the property. The inspector also conducts special inspections in response to complaints, to check on specific issues that need to be addressed separately, or when Housing is negotiating with a property to preserve or alter loan terms.</p> | <p>Process</p> <p>The building inspector assesses the physical condition of properties to ensure they are decent, safe, and sanitary, as specified in the loan agreements. If the inspector identifies issues, they will conduct re-inspections, and work with properties to plan needed fixes and guide properties through the rehabilitation process.</p> |

A Recent Consultant Report Identified Improvement in Asset Management Practices

In 2025, Housing worked with a consultant to identify improvements for its asset management practices. The consultant documented a total of 14 processes related to Housing’s monitoring program. The processes included rent roll reviews, site inspections, financial reviews, reserve requests, and payment processing. The report included a number of process improvement ideas and four recommendations for changes to improve asset management processes.

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Finding I Housing Should Assess the Asset Management Team’s Goals and Resources

Summary

The Asset Management team has not been able to complete all annual property reviews and inspections in recent years. Staff did not complete one-third of property compliance reviews in 2024 and 2025, and no field audits have been conducted since 2024. Housing staff did not inspect every building annually and estimate there is a three-month backlog of annual inspections. Vacancies and unclear expectations have hindered the team’s ability to complete its work. According to Housing, current software tools are not sufficient to meet the goals of the program given the size and scope of the loan portfolio. Housing should clarify the expectations for the team via a strategic plan for the program and assess the resources needed, including potentially a new software solution, to successfully put that plan into action. Finally, documented procedures and additional tools would support staff to complete their monitoring consistently.

The Asset Management Team Is Behind on Property Reviews and Inspections

Per the City’s 2025-26 Adopted Operating Budget, the Affordable Housing Portfolio Management core service is, in part, to: “Manage the City’s affordable housing loan portfolio, including loan servicing and monitoring, compliance of income restricted apartments...”

The Budget further defines its two programs under the Affordable Housing Portfolio Management core service as:

| | |
|-------------------------------------|---|
| Loan Compliance | Manages and oversees the City’s affordable housing loan portfolio, including loan servicing and monitoring and compliance of affordable deed restricted apartments. |
| Property Maintenance and Inspection | Work with existing developments to retain and preserve the long-term viability of affordable apartments. |

Limited Staff Has Hindered the Department’s Ability to Complete Property Reviews

Vacancies and turnover in recent years have impacted the Asset Management team’s ability to complete property reviews. In late 2025, the team of three included one division manager and two staff assigned to perform 250 property

reviews for nearly 25,000 affordable housing units.² Both team members had less than two years of experience with the City. Over the course of the audit, two more staff members were hired; however, two vacancies remained.

In 2024 and 2025, the Asset Management team did not complete all property reviews, including financial reviews and reviews of affordability restrictions. A third of all property reviews were not completed in 2024; over half were not completed in 2025.

- **Financial reviews:** As described in the background, financial reviews involve verifying a variety of compliance documents and ensuring accurate principal, interest, and fee payments. The Asset Management team reported that staff completed a review of payments submitted in 2025. However, these reviews do not mean that staff reviewed all aspects of a property for compliance or even that all documents were submitted. Staff also noted that there was the potential of uncollected payments from prior years when not all property reviews had been completed.
- **Affordability restrictions:** In a sample of ten properties, staff had reviewed the rent rolls for only two of them in 2025. Staff paused rent roll reviews in 2025, waiting for a new automated platform to be developed. Staff have also not conducted field audits to verify information in the rent rolls submitted by property owners since 2024.

In addition, Housing staff estimated there was a three-month backlog of annual inspections at the time of the audit. The team only had one building rehabilitation inspector position, despite having nearly 25,000 affordable housing units. At the time of the audit, Housing was considering hiring another building rehabilitation inspector if budget authority allowed.

According to Housing, the Asset Management team has historically not been able to complete all property reviews due to insufficient resources. Without completing reviews or inspections, Housing could miss out on revenues to the City or not identify affordability or habitability issues with properties.

Limited Sample Review Shows Additional Gaps in Property Reviews

Additionally, in a sample of nine properties, there was no evidence that staff had received or reviewed key documents to ensure compliance with the City's requirements.

- For five properties, not all net cash flow analyses were on file, and there was no evidence that staff had reviewed them. The net cash flow analysis is important to confirm the accuracy of loan payments.

² One property can have multiple reviews required annually.

- Three properties were missing a copy of current property or liability insurance coverage. Without copies of insurance coverage, staff cannot verify that the building is protected.
- Operating budgets, which help the team understand a property's income and expenses, were missing for eight of the nine sampled properties.
- Staff had not reviewed schedules of rental income and/or long-term capital improvement plans for seven properties. This information provides insight into a property's anticipated income and ability to cover future maintenance needs.

Even in situations where staff marked a review as completed, that does not indicate that properties submitted all required documentation or that staff reviewed the documents for compliance. Two of the nine sampled properties had reviews marked as complete in Housing's database for 2025, but these properties did not have all required documents in Housing's database.

Unclear Expectations Have Further Hindered Staff

Current expectations on the depth and number of reviews are not aligned or not well defined. Staff described not having clear directions on what to review when looking at financial audits and reported that due to changes in the team's management, priorities and compliance practices had been inconsistent or unclear. Clear expectations from management are needed to communicate to staff what should be performed and the anticipated workload.

- **Defining review parameters:** What should be completed during an annual review needs clarification. The 2025 consultant report noted this as a pain point, saying that "there is no defined level of review to be conducted" for financial reviews. The consultant also noted that there "isn't a clear understanding of what level" the reviews should be for properties' budgets and long-term capital improvement plans. Across the Asset Management team's reviews, the consultant recommended that "additional clarity on the breadth and depth of these processes should be established."

As an example, the Asset Management team reported that they do not check tenant incomes except at move-in. This is because the team understands that tenants earning above income limits after move-in is not a violation of the City's agreements. Management reported that those checks would ideally be occurring annually and that, depending on the property, tenants exceeding income limits could violate the City's agreement terms.

- **Setting annual review completion targets:** The performance measure target for annual reviews completed does not align with management's reported expectations. The 2025-26 Adopted Operating Budget included the performance measure "% of annual property

compliance reviews completed,” with a target of 80 percent. However, management has reported that the expectation is that staff complete 100 percent of financial and affordability restriction reviews. As noted previously, in the past two years, staff completed roughly two-thirds of reviews.

- **Setting annual property inspection targets:** The Asset Management team has reported that there is also a goal to inspect at least 105 properties annually, though this does not represent the entire multifamily housing portfolio. However, Housing staff estimate the inspector can inspect 80 properties annually (along with required re-inspections).

Housing Should Evaluate the Asset Management Team’s Resources, Goals, and Documented Procedures

As noted earlier, as described in the City’s Adopted Operating Budget the Asset Management team’s role is broadly to monitor loan compliance for the City’s portfolio. Housing Department management has reported that the description of the core service of Affordable Housing Portfolio Management is subject to change, but this was not yet underway as of the time of the audit.

In early 2026, the Asset Management team developed a draft improvement plan that lays out goals for improvements, and a project timeline for making changes to the team’s processes. To accomplish these, the plan includes initiating a request for proposals for an asset management software system and working with a consultant on data cleanup and developing a risk rating (see Finding 2). Goals in the improvement plan include:

- standardizing operations,
- improving use of their software system,
- continuing annual reviews, and
- improving the visibility into the financial health of the portfolio.

While this improvement plan provides steps to address the team’s challenges, a *program-level strategic plan* with long-term goals around financial and compliance monitoring would more clearly set expectations for the team. Strategic planning includes a vision for the team’s success, tactics for implementing the vision, and methods to monitor progress and performance.

The 2025 consultant report recommended:
Housing Department leaders first establish metrics & goals which will then drive a more detailed discussion about each process. The team should then establish the purpose, components and level of scrutiny for each.

Housing has developed strategic plans for other programs within the department. In 2024, Housing finalized a plan for the Rent Stabilization Program focusing on

strengthening housing stability, preserving existing units, and expanding outreach to tenants and housing providers. The plan outlines how the Program can enhance data collection, improve compliance processes, and build partnerships across departments and community organizations to better support residents and ensure consistent application of the City's rental protections.

For the Asset Management team, strategic planning could include:

- Goals for overall compliance with affordability restrictions and loan repayments which are appropriate for the size and scope of the loan portfolio.
- Performance metrics regarding how many or what percent of properties staff review each year, for financial reviews, affordability restriction monitoring and property inspections. As noted above, a metric regarding the percentage of annual property compliance reviews was added to the City's 2025-26 Adopted Operating Budget. As Housing reviews resources and overall goals, this measure or the associated target may be further refined.
- Strategies for prioritizing higher-risk properties, as discussed in Finding 2.
- Staff roles, including team management oversight.

A program-level strategic plan with clearer goals, metrics, and staff responsibilities will clarify for staff and management the role of the Asset Management team.

Housing Should Explore Replacing or Re-tooling the Asset Management Team's Software Solution

As part of the strategic plan, Housing should identify the resources needed to implement the plan's vision and goals, including software requirements. According to Housing, current software tools are not sufficient to meet the goals of the program given the size and scope of the loan portfolio.

In particular, the primary software platform has not been configured to provide centralized information, which limits insights into the properties' health and adds staff time spent on monitoring. As it is used now, the software does not have complete information about properties in an easily usable format. It does not contain all loan documents, track compliance with loan agreements, or include summary information about loan terms. According to staff, the data within the software system also has some inaccuracies, which makes it less reliable. Housing has included developing an RFP for an asset management software solution in their proposed improvement plan.

Other California jurisdictions surveyed similarly reported difficulties completing in-depth financial analysis of their portfolios without better asset management software or outside support. The City of Long Beach and the City of Los Angeles have outsourced some of the work related to financial reviews. The City of

Oakland, the City of Fresno, and the Sacramento Housing and Redevelopment Agency reported interest in software solutions to conduct asset management monitoring.

Current Automation Efforts

During the audit, staff were in the process of automating some of their work. The Asset Management team was working with a consultant on a portal through which property managers could upload tenant rental and income information. The portal is expected to be able to flag issues like missing documentation, instances where rents are over rent caps, or tenants who exceed income limits. The team had also expressed interest in working with a consultant that could automate responses to property management, and potentially outsourcing financial reviews.

Documented Procedures and Additional Tools Would Support Staff to Complete Work Correctly and Consistently

As Housing clarifies the Asset Management team's goals and workload, documented procedures will allow staff to complete that work in accordance with management's expectations. Standardizing operations was one goal in the team's draft improvement plan.

The 2025 consultant report had several improvement ideas regarding standardization, including the use of checklists and templates.

At the time of the audit, the Asset Management team did not have current formal procedures to guide reviews. While the team had a draft manual from 2013, Housing advised that these were out of date. A separate set of standard operating procedures from 2021 covered aspects of the team's work, but did not cover others, such as document reviews or how to prioritize them. Staff reported that they were developing procedures over the course of the audit, but these were still in progress.

The lack of procedures can lead to inconsistent reviews. As described earlier, in our sample of nine properties, there was variability among the reviews. Not all required documents were on file, or there was no evidence that the documents had been reviewed. These included operating budgets, insurance documents, schedules of rental income, and long-term capital improvement plans.

- **Checklists** would help staff track which documents had been submitted and whether reviews were completed. As noted previously, many of the nine sampled properties had documentation missing from Housing's database and files. They could also assist management in tracking progress across various work areas, such as inspections and reviews. The City of Fresno has checklists to facilitate staff review of properties. The City of Oakland also has checklists to guide on-site reviews and property inspections.

Checklists to help with conducting financial and budget document reviews was an improvement area noted by the 2025 consultant report.

- **Guidance on review requirements** would create a uniform approach to reviewing documents. In our sample review, there was little evidence of how staff reviewed and verified information such as budgets, net cash flow payments, and rent rolls. Staff reported that documented procedures would be helpful to ensure they are completing the reviews as expected. For example, staff have to review properties' requests to use replacement reserves. However, the allowable uses for replacement reserves are not always included in loan agreements and Housing does not have a documented list of allowable uses for staff to refer to.

The 2025 consultant report noted an improvement area for financial reviews to: "Discuss and determine the level of review, including what to review and how to do it."

- **Summaries of loan terms** would simplify the review process for staff. Annual reviews can be time-consuming as staff must reference multiple documents to verify the City's net cash flow share, fees, and affordability restrictions. This includes loan documents such as the construction and permanent loan agreement, promissory note, and an affordability restriction document.

Per Housing staff, these summaries should be created when a permanent loan is first added to the Asset Management team's portfolio. Since loan agreements can have amendments which may alter the terms, ongoing updates to the summaries would help to ensure they are still accurate and minimize the risk that changes may be missed.

- **Centralized document storage** ensures all documents are on file and properties comply with loan agreements. Staff store documents in the team's asset management software, in an internal database, and in their own City emails. Staff reported that because properties can directly email documents to individual Housing staff, if staff do not save documents into Housing's database or online files, documents could be lost when staff leave the City. The absence of required documentation could prevent the Asset Management team from completing reviews and verify that properties are complying with loan requirements.

The 2025 consultant report identified improvements for streamlining document storage. The report noted that saving documents in multiple places "eats up extra time and effort for the team members" and recommended using one platform only for document storage.

- **Standard training** on the procedures and expectations would allow the team to onboard staff efficiently and promote consistent reviews across properties. Staff described the training now as informal and on-the-job. The team reported that some tasks may be more challenging due to having no prior experience conducting that work.

For projects with federal funding, the City is required to have and follow written policies, procedures, and systems.³ HUD maintains a handbook for field office staff, Multifamily Asset Management and Project Servicing (4350.1), which provides guidance for ongoing oversight, financial management, and regulatory compliance of HUD multifamily housing projects. While not all loans in Housing's loan portfolio have federal funding, these standards and the handbook offer best practices that the Asset Management team could incorporate into standard operating procedures.

As the team formalizes goals and procedures, having standardized guidance and centralized locations for information can help the team achieve goals set by management. The procedures, centralized document storage, and loan summaries and checklists can reduce review times by standardizing operations within the Asset Management team. It would also allow for improved oversight and opportunities to escalate issues to management.

Recommendations:

- 1: The Housing Department should develop a program-level strategic plan for the Asset Management team that includes overall goals for loan servicing and monitoring for affordable housing units, performance metrics for different aspects of the program, staff roles, and resource needs.**
- 2: Along with establishing goals and clarifying expectations for the Asset Management team, the Housing Department should modify existing software or procure a new software platform that allows for more comprehensive management of the affordable multifamily housing portfolio.**
- 3: To expedite reviews of tenant income and rent compliance, the Housing Department should implement an automated tool to review data on rents and income limits.**
- 4: To standardize affordable multifamily housing loan monitoring, the Housing Department should update its standard operating procedures, including guidance for:**
 - a. Completing financial and affordability restriction reviews,**
 - b. Conducting building inspections,**
 - c. Creating and updating loan agreement summaries such that loan terms and requirements are easily accessible, and**
 - d. Maintaining document submissions in a centralized file or software system.**

³ Code of Federal Regulations 24 CFR § 92.504(a).

- 5: The Housing Department should develop standard training for the Asset Management team to ensure reviews are completed in accordance with the standard operating procedures.**
- 6: To expedite property reviews, the Housing Department should develop checklists to track document submissions and completion status to facilitate verification.**

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Finding 2 Housing Should Strengthen Oversight of Affordability Restrictions and Higher-Risk Properties

Summary

Some properties in the multifamily affordable housing portfolio do not comply with affordability restrictions, have not submitted required documentation, or have repeated property violations. In a limited sample of 878 units across 10 properties (4 percent of the total units managed), 110 units had tenants with incomes above the cap for their unit type (13 percent of the sample); 48 units had tenants that earned 140 percent or more (5 percent). Housing does not have a mechanism to address this. Additionally, some property inspections result in repeated violations and numerous re-inspections before achieving compliance. The escalation process for property issues and violations should be documented to ensure consistency and efficient use of staff time. Despite differences in property compliance, the Asset Management team's current approach does not differentiate financial and affordability restriction monitoring based on the risk of the property. A risk rating system, which Housing reports is under development, would focus staff time on the higher risk properties and allow for earlier detection of issues. Housing should approach the development of a risk rating system in conjunction with an overall assessment of resources as recommended in Finding 1.

The City Does Not Have a Mechanism to Address Tenants That Do Not Meet Income Expectations

To ensure that low-income tenants have access to affordable housing, the City imposes affordability restrictions on properties. These restrictions set limits on the amount of income a household can make to qualify for tenancy and the allowable rent a property can charge. Both vary depending on unit type. The City enforces income limits at the time that a tenant moves in; however, the City's affordability restriction agreements do not explicitly bar tenants from earning more than the allowed income after they move in.

In a sample of 10 properties totaling 878 units (4 percent of the nearly 25,000 affordable housing units), 13 percent of tenant incomes (110 units) were above the allowed cap for their unit type. In most of these cases, tenants were making

just slightly more than the cap. Five percent of tenants in the sample (48 units) made 140 percent or more of the income cap.⁴

Some properties had significantly more over-income tenants than others. Among our sample, some properties had no over-income tenants while another had 29 percent of units (27 of 94 units) that were over income. That property had two households each making over \$300,000; these incomes represented over 400 percent of the allowed income limit. Another household had exceeded the income limit even at the time of move-in. All these units had rent and income limits (at the time of move-in) in the property's loan agreement.

Over-income tenants are not all paying the maximum allowable rent, per affordability restrictions. This results in lower income for the property. For the property with 27 over-income tenants, each of them was charged below the rent cap. In total, the property potentially forwent \$9,555 per month in rent, or over \$114,000 in one year, by under-charging these tenants. This affects the property's income and thus the amount it can repay the City. In 2025, the property repaid the City just \$1,694 out of the total \$7.6 million it owed the City.

A Clear Escalation Pathway Would Clarify the City's Approach to Over-Income Tenants

Housing staff reported that they regularly review rent caps to ensure that rents do not exceed the limits and tenants are not overburdened, but do not verify that tenants meet income requirements after move-in. The Asset Management team reported that having over-income tenants may not be a contract violation, so this is not regularly reviewed.⁵ Housing Department management stated that, given sufficient staffing capacity, checking incomes annually would be the City's goal, and that this was an expectation for the team historically.

For properties that receive tax credits, bond funding, or funding from non-City sources, there are requirements regarding tenant incomes.⁶ In these cases, Housing reports that staff could hold properties to those outside requirements and report properties to outside agencies. Additionally, loan agreements require properties to have management plans, which may include

⁴ The federal Low-Income Housing Tax Credit (LIHTC) program defines a tenant as over-income if they are making more than 140 percent of the allowed income limit for the unit.

⁵ At move-in, properties must verify that tenants' incomes are under the restricted amount. After that, the agreements require property owners to report tenant incomes annually, but do not require that those incomes stay under the restricted amount.

⁶ Tax-exempt bonds are administered by the state and issued by the City. There are affordability requirements for these bonds that developers must comply with. Developers can receive tax credits through the federal Low Income Housing Tax Credit program. The program has both rent and income restrictions.

processes for reviewing and addressing tenant incomes. Each property would need to be evaluated to ensure income requirements are appropriate given their particular funding structure.

The City Attorney's Office advises that the most appropriate way for the City to ensure its income restrictions are met beyond the tenant's initial move-in would be to include that requirement in loan agreements. This would cover properties that do not have, or no longer have, external requirements. Amending the loan agreements that are already in place can be done if the borrower agrees or during re-negotiations if a loan is extended or changed. Amending all the agreements would take time.

If the City wants to ensure that affordable housing units remain occupied by low-income tenants, Housing should create a clear pathway to resolve situations where tenants exceed income restrictions, where possible. The City of Long Beach reported that, depending on funding sources, tenants are allowed to earn up to 140 percent of the allowed income and can be charged up to 30 percent of their income in rent. San Francisco also allows rents up to 30 percent of income. Several jurisdictions, including the Santa Clara County Housing Authority, noted that properties could swap affordable restriction limits between units within the property to minimize displacement of tenants.

Based on prior draft procedures and best practices from other agencies, monitoring and escalation paths could include:

- Asset management staff annually reviewing tenant incomes.
- Encouraging borrowers to increase rents for over-income tenants in units. Increased income could help properties keep up with building maintenance or increase the loan repayments to the City, both of which would support ongoing affordable housing.
- For units with tax credit agreements or other regulations with affordability restrictions, refer the properties to outside agencies for enforcement. Per the federal Low-Income Housing Tax Credit Program, a unit ceases to be treated as low-income if the tenant's income exceeds 140 percent of the applicable income limitation. If a tenant's income does exceed 140 percent of the limit, then another available unit in the property must be rented out at the same applicable income limitation to maintain compliance.⁷
- For units without tax credit agreements, working with borrowers to:
 - Increase the rent to the allowable affordability restriction for that unit;

⁷ Code of Federal Regulations 26 CFR § 1.42-15

- Potentially abstain from renewing the lease with the over-income tenant; or
- Lease the next available unit to a tenant at noncompliant unit's level of affordability.

Properties May Also Have Under-Income, Rent-Burdened Tenants

On the opposite end of the spectrum, some tenants' incomes are below expectations. Per Housing, properties are intended to have a mix of target income levels to ensure financial stability, based on the project type. However, in some cases, tenants make far below the income intended for their unit. This can lead to rent burden, where tenants are paying a significant percentage of their income on rent.

In March 2026, Housing reported that nearly half of renters in San José were cost burdened, paying 30 percent or more of their income in rent. Recent loan agreements include requirements for properties to review the rent burden of their tenants. This is a funding requirement by Housing, and properties have to report annually on how many units are occupied by rent burdened households.

Housing does not have documented procedures on how staff should review incomes or what steps to take if the Asset Management team determines that a property has a high number of rent burdened households. Having such a process will support Housing's efforts to address rent burden among low-income households.

Recommendation:

- 7: The Housing Department should develop a policy for addressing tenants that exceed income limits, or fall below income expectations, in affordable units. This may include changes to standard loan agreement terms going forward and considerations for units with tax credits or bond financing.**

Escalation Process for Noncompliant and Higher-Risk Properties Should Be Clarified

The 2025 consultant report notes that the Asset Management team does not have a common definition of noncompliance for properties and has inconsistent follow-up timelines, communication content, and formal noticing of noncompliance. The report includes improvement areas for Housing to "outline a detailed, consistent noncompliance definition" and "develop a penalty for noncompliance." As described in the Background, Housing's role

as asset managers is to monitor the financial performance of the properties but not be involved in the day-to-day operations as property managers.

Housing Should Document the Steps to Address Serious Concerns in Properties in the Loan Portfolio

As described in draft procedures from 2013, some properties can have serious issues that may impact the City's financial interest in the property. According to Housing staff, risk factors could include negative net cash flow, a high number of vacant units, inability to cover debt service, ongoing physical condition problems, or noncompliance with rent or income limits.

For example, at the time of the audit, the City was working to address concerns relating to one developer. One property had a loan totaling \$20.2 million as of mid-2022. In late 2022, staff reviewed the property's financial and operational challenges with the bank, the developer, and other lenders. The City chose to provide \$13 million in additional funding to pay off the property's bank loan to stabilize operations and address short-term financial obligations. At the time of the audit, the property was still facing difficulties, and the City was considering whether to replace the property management.

Depending on the property and the reasons for financial difficulties, the City has multiple avenues it could pursue to escalate financial concerns. The City could require:

- Additional reporting to more closely monitor the property.
- Property management staff or company be changed. City staff report exploring this option to address property concerns.
- Rents be raised to meet rent caps. As noted previously, not all rents meet rent caps even for tenants making over the income limit. Additional rental revenue could support a property's financial situation. If tenants are extremely low income, additional revenue from increased rents could be limited.
- Accelerated loan repayments. Though this is an option, for properties with financial trouble, this may not be an effective tool to preserve the long-term viability of the affordable housing units.

The City does not have a documented process for when staff should take these steps or how concerns should be escalated. This could lead to inconsistent enforcement or delays in escalating issues. Loan agreements have their own terms regarding actions the City can take regarding remedies or default, but there is also not a process documented for how staff should initiate those steps.

It is important to note that developments typically involve multiple layers of financing, including senior loans held by other lenders, each with their own

monitoring and reporting requirements. Accordingly, responsibility for ongoing financial oversight is shared among multiple stakeholders, not just the City.

Escalation Procedures for Follow-up Inspections Are Not Clearly Defined

Housing staff are tasked with assessing the physical condition of properties that they monitor. Housing currently has one inspector (1 FTE). Per the loan agreements, property managers must maintain decent, safe, and sanitary housing. If a property has issues at their annual inspection, then Housing staff conduct a re-inspection to verify that previously identified issues have been repaired within required timelines.⁸

Staff spend a significant amount of time on re-inspections. Across all initial inspections conducted in 2024 and 2025, 25 percent (44 out of 179 initial inspections) resulted in three or more re-inspections, and 6 percent (11 out of 179 initial inspections) resulted in more than five re-inspections. In one instance, Housing staff followed up with a property eight times before sending property management a notice of violation. From the notice, it was not clear which issues were the highest priority and escalation steps if the property did not resolve the issues. There are not current written procedures on when a notice of violation should be sent or when other actions, such as sending cure letters, should be taken.⁹

Housing staff cannot issue fines or citations, though this is an authority that the City's Code Enforcement and Fire Prevention inspectors have.¹⁰ Over the past few years, staff developed working relationships with City staff in the Fire Department and Planning, Building and Code Enforcement (PBCE) to address potential code violations. Housing staff reported instances where the inspector will coordinate follow-up or conduct a joint visit to a property. Housing staff have also reported violations to other City staff, such as when a property did not have a fire backup system. However, there is no clear guidance on when staff should collaborate with other departments or which properties are covered by each department's purview. For example,

⁸ Housing staff also conduct special inspections, which happen outside the normal cycle, usually prompted by a complaint or an urgent issue that needs separate documentation.

⁹ A cure letter may include detailed information about inspection deficiencies and documentation that was not submitted, stating that failure to comply will result in the City moving forward with formal enforcement, including notice of default, acceleration of debt, and notification to federal regulators.

¹⁰ Code Enforcement inspects multiple housing properties based on a tier system (Tier 1, 2, and 3). Tier 1 (fewer complaints and violations) has a target to have 10 percent of the building's self-certificated units inspected on a 6-year cycle. Code Enforcement aims to inspect 25 percent of a Tier 2 building's units on a 5-year cycle and 50 percent of units on a 3-year cycle for Tier 3. The Fire Department inspects multifamily residential properties annually for compliance with the fire code, per state regulations.

multifamily housing properties are inspected by Code Enforcement on a regular cycle.¹¹

The 2025 consultant report included improvement areas to develop consequences for unresolved deficiencies and to continue involving other Housing staff (beyond the inspector) in those situations. By establishing standardized procedures and identifying opportunities to coordinate with other City staff, Housing would be better positioned to escalate inspection issues and formalize working relationships with staff who can follow up on inspection issues. This could help reduce the number of re-inspections by clearly defining escalation steps, including notifying property management of potential further City action.

Recommendation:

- 8: The Housing Department should establish clear escalation policies to address higher-risk properties. These policies should include:**
- a. Clear definitions of noncompliance to ensure conformance with loan agreement and affordability restrictions terms;**
 - b. Escalation processes and steps staff should take to resolve concerns identified during financial and affordability restriction monitoring reviews;**
 - c. Escalation processes for inspections, including when staff should issue violation notices and when to notify Code Enforcement or other City staff of property violations; and**
 - d. How escalation steps should be communicated to property managers and borrowers.**

The Asset Management Team Should Develop a Risk Rating System to Focus Staff Time on Higher Risk Properties

The multifamily affordable housing portfolio comprises nearly 25,000 units with a small team of Asset Management staff to oversee them. Despite this, the Asset Management team does not have a system to prioritize staff time to focus on the highest risk properties for all types of property reviews. Such a system could also allow staff to target resources on early intervention for properties that risk running into major difficulties.

¹¹ In cases where the City owns the land for a multifamily affordable housing development, PBCE advises that it would not be inspected by Code Enforcement staff.

For property inspections, Housing staff use an informal risk rating to determine inspection frequency. Based on observations at annual inspections, staff assign properties a rating. Better-rated properties are inspected less frequently than poorer-rated ones. However, this applies to only one component of the Asset Management team's work. Extending the risk rating system more broadly to include all aspects of a property review would allow staff to evaluate a property based on several factors, such as cash flow, ability to make loan payments, reserve levels, and property condition.

According to the Affordable Housing Investors Council, a **risk rating model** can be used to identify potential issues early and determine when increased oversight or intervention may be necessary.

As noted in the 2025 consultant report, when determining goals and metrics:

“... the team will have to consider the workload. Will a very high level of scrutiny be feasible for every review or every property? One way to ensure the most effective use of resources might be to develop a risk-based or sample-based approach to some of the less significant reviews such as the Rent Roll or for some of the fully compliant properties.”

For projects with federal funding, the City should have a system for assessing the risk of activities and projects.¹²

Risk Ratings Can Inform Inspection Frequency and Monitoring

Staff can use risk ratings and watchlists to determine which properties should get more frequent or more thorough monitoring. Though Housing staff reported previously having a watchlist, it was not in use at the time of the audit and the 2025 consultant report noted: “inconsistent & unclear use of the watchlist.”

- The San Diego Housing Commission uses a risk rating model where each area, including loan repayment, financial performance, physical condition, and compliance with loan documents, receives a weighted score that adds up to an overall rating expressed as a percentage from 0 to 100. They then use that score to decide when a property should be placed on a watchlist, at which point staff reach out to the property to discuss needed improvements and next steps.
- The Santa Clara County Housing Authority uses a risk rating and watchlist. Staff find this useful when looking at long-term trends and how properties are operating.
- The Affordable Housing Investors Council recommends developing a risk rating model that evaluates each asset quarterly using a five-tier

¹² Code of Federal Regulations 24 CFR § 92.504(a).

scale, from A as the highest performance through F. It recommends having clear criteria for when an asset becomes a watchlist item, including automatic watchlist consideration for any rating of C or below. Properties on a watchlist should be monitored more closely until conditions improve.

- The U.S. Department of Housing and Urban Development uses a risk-based approach to determine the frequency of management and occupancy reviews for their asset management. Review frequency is informed by prior review results and risk classifications, with higher-risk or lower-performing properties subject to more frequent reviews and increased oversight, and higher-performing properties reviewed less frequently.¹³

Risk-based Monitoring Requires an Evaluation of Resources

At the time of the audit, Housing was intending to develop a risk rating model to prioritize workload and identify properties that may warrant additional monitoring. This is in line with the 2025 consultant report that recommended Housing develop a risk-based or sample-based approach. Housing reports that current staff capacity and monitoring processes are not designed to track all the early indicators of financial instability at the level that would be needed for a risk rating system. As such, Housing should approach the development of a risk rating system in conjunction with an overall assessment of resources as recommended in Finding I.

Recommendation:

- 9: To better assess the financial health of properties and detect issues in the affordable multifamily housing loan portfolio, the Housing Department should implement a risk rating model that:**
- a. Defines risk categories and evaluation criteria, and**
 - b. Establishes clear procedures for how often and how thoroughly property reviews are conducted based on a property's risk level.**

¹³ While not all City loans utilize federal funding and not all properties have Section 8 vouchers, these federal practices provide a useful framework for developing a risk-based monitoring system.

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Conclusion

The City supports the creation and maintenance of affordable housing for the city's residents through multifamily affordable housing loans. As of January 2026, Housing oversaw a loan portfolio that totaled approximately \$745.6 million. In total, there are roughly 220 properties and nearly 25,000 housing units covered by active loans, affordability restrictions, or are in the pipeline. However, Housing has not been able to complete all property reviews in recent years, due in part to staff vacancies, unclear expectations, and software limitations. A program-level strategic plan, along with an assessment of resources and documented procedures, would allow Housing to communicate goals and refine expectations for the Asset Management team overseeing the properties. Establishing mechanisms to enforce income affordability restrictions and escalating property violations would allow Housing to better monitor properties in the portfolio. Lastly, to target staff's time on the highest risk properties, Housing should develop a risk rating system to inform monitoring activities.

RECOMMENDATIONS

Finding 1: Housing Should Assess the Asset Management Team's Goals and Resources

Recommendation #1: The Housing Department should develop a program-level strategic plan for the Asset Management team that includes overall goals for loan servicing and monitoring for affordable housing units, performance metrics for different aspects of the program, staff roles, and resource needs.

Recommendation #2: Along with establishing goals and clarifying expectations for the Asset Management team, the Housing Department should modify existing software or procure a new software platform that allows for more comprehensive management of the affordable multifamily housing portfolio.

Recommendation #3: To expedite reviews of tenant income and rent compliance, the Housing Department should implement an automated tool to review data on rents and income limits.

Recommendation #4: To standardize affordable multifamily housing loan monitoring, the Housing Department should update its standard operating procedures, including guidance for:

- a. Completing financial and affordability restriction reviews,
- b. Conducting building inspections,
- c. Creating and updating loan agreement summaries such that loan terms and requirements are easily accessible, and
- d. Maintaining document submissions in a centralized file or software system.

Recommendation #5: The Housing Department should develop standard training for the Asset Management team to ensure reviews are completed in accordance with the standard operating procedures.

Recommendation #6: To expedite property reviews, the Housing Department should develop checklists to track document submissions and completion statuses to facilitate verification.

Finding 2: Housing Should Strengthen Oversight of Affordability Restrictions and Higher-Risk Properties

Recommendation #7: The Housing Department should develop a policy for addressing tenants that exceed income limits, or fall below income expectations, in affordable units. This may include changes to standard loan agreement terms going forward and considerations for units with tax credits or bond financing.

Recommendation #8: The Housing Department should establish clear escalation policies to address higher-risk properties. These policies should include:

- a. Clear definitions of noncompliance to ensure conformance with loan agreement and affordability restriction terms;
- b. Escalation processes and steps staff should take to resolve concerns identified during financial and affordability restriction monitoring reviews;
- c. Escalation processes for inspections, including when staff should issue violation notices and when to notify Code Enforcement or other City staff of property violations; and
- d. How escalation steps should be communicated to property managers and borrowers.

Recommendation #9: To better assess the financial health of properties and detect issues in the affordable multifamily housing loan portfolio, the Housing Department should implement a risk rating model that:

- a. Defines risk categories and evaluation criteria, and
- b. Establishes clear procedures for how often and how thoroughly property reviews are conducted based on a property's risk level.

APPENDIX A

Audit Objective, Scope, and Methodology

The mission of the City Auditor's Office is to identify ways to increase the economy, efficiency, effectiveness, equity, and accountability of City government by independently assessing and reporting City operations and services. The audit function is an essential element of San José's public accountability, and our audits provide independent analysis, reliable information, and recommendations for improvement to the City Council, City Administration, and the public. In accordance with the City Auditor's Fiscal Year (FY) 2025-26 Audit Work Plan, we have completed an audit of the City's affordable multifamily housing loan portfolio.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The objective of this audit was to assess Housing's processes for managing the affordable multifamily housing loan portfolio, including loan servicing and compliance monitoring. We sought to understand the relevant internal controls over the Housing's multifamily loan portfolio, and have performed the following to achieve the audit objective:

- To understand laws, regulations, and City policies relevant to the audit objective, we reviewed:
 - Title 24 Code of Federal Regulations Part 92 – HOME Investment Partnerships Program
 - Title 26 United States Code Section 42 – Low-Income Housing Credit and related requirements
 - California Code of Regulations Title 4, Division 17, Chapter 1 – Federal and State Low Income Housing Tax Credit Laws
 - U.S. Department of Housing and Urban Development Multifamily Asset Management and Project Servicing (4350.1)
 - Council memorandums of Housing Department actions related to affordable housing
 - Requirements regarding the tax credits and tax-exempt bonds from the California Tax Credit Allocation Committee and the California Debt Limit Allocation Committee.
 - Requirements, monitoring, and compliance practices from the U.S. Housing and Urban Development Department and the California Debt Limit Allocation Committee.
 - Rent and income limits by Area Median Income for 2024 and 2025.
- To understand affordable multifamily housing loan monitoring processes and requirements, we:
 - Interviewed staff from the Housing Department and the City Attorney's Office.
 - Reviewed available asset management policies and procedures.
 - Reviewed a 2025 consultant report on the Housing Department's asset management practices.

- Compiled a list of all required property reviews in 2024 and 2025 to determine how many had been completed.
- Reviewed targets and goals as outlined in the City's 2025-26 Adopted Operating Budget.
- Reviewed the Asset Management Team's draft strategic improvement plan.
- To review monitoring processes and documentation, we selected a random sample of nine properties. Properties were categorized as low, medium, and high outstanding loan balances, and then were selected at random. We reviewed loan information on Housing's software system, available documentation, and payments received.
- To understand affordability restriction compliance and monitoring, we verified the rent and income limits for tenants for the random sample of nine properties described above. Following that review, we expanded our work to include a judgmental sample of three more properties owned by the developer who had the greatest noncompliance.
- Using Housing's software system and the financial management system, we compiled a list of all affordable housing properties along with loan balances, repayments, and fee payments to determine the overall size and scope of the portfolio.
- To determine the escalation of inspection violations, we reviewed information on Housing's software system, including inspection reports and notices to property owners.
- We benchmarked to the following jurisdictions to understand monitoring procedures, and software or tools used: the cities of Fresno, Long Beach and Oakland; the City and County of San Francisco; the Sacramento Housing and Redevelopment Agency; the San Diego Housing Commission; and the Santa Clara County Housing Authority.

We would like to thank the Housing Department for their time and insight during the audit process.

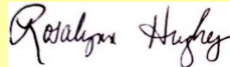
TO: JOE ROIS
CITY AUDITOR

FROM: Erik L. Soliván

SUBJECT: See Below

DATE: May 20, 2026

Approved



Date: 5/27/2026

SUBJECT: Response to the Audit of the Housing Department Loan Portfolio

BACKGROUND

The Housing Department manages a large and complex affordable multifamily housing loan portfolio consisting of approximately 220 properties and more than 22,000 affordable housing units financed through Redevelopment Agency and City loans subject to long-term affordability restrictions. The City's permanent multifamily loan portfolio, with over \$745.6 million, and includes projects financed through local funding sources, federal funds, tax-exempt bonds, and legacy Redevelopment Agency loans. The Housing Department's Asset Management team is responsible for monitoring these properties to ensure compliance with affordability restrictions, loan repayment obligations, property maintenance standards, and applicable state and federal regulations.

The City Auditor conducted an audit of the Housing Department's management of the affordable housing loan portfolio, including loan servicing and compliance monitoring. The Administration reviewed the audit titled *Affordable Multifamily Housing Loan Portfolio: Clearer Goals and Stronger Oversight Would Improve Monitoring*. The audit identified several operational and resource challenges affecting the Asset Management program, including incomplete property reviews, staffing vacancies, inconsistent procedures, limited technology systems, and the absence of a formalized risk-based monitoring framework. The audit also identified the need for clearer escalation procedures for higher-risk properties and stronger oversight of affordability compliance.

The Administration agrees with the nine audit recommendations, and the following are the Administration's responses to the recommendations. The Housing Department has already initiated several process improvement efforts, including development of updated standard operating procedures, implementation planning for a new rent roll compliance portal, evaluation of future asset management software solutions, and refinement of compliance and escalation protocols for higher-risk properties. As this is the fourth audit

of Housing Department programs conducted within the past two years, the implementation timeframes reflect the Department's experience implementing similar deliverables identified in the previous three audits. Additionally, the Housing Department's complex role at the intersection of federal and state regulatory oversight creates structural challenges and opportunities for effective management of the portfolio.

RECOMMENDATIONS AND ADMINISTRATION RESPONSES

Finding 1: Housing Should Assess the Asset Management Team's Goals and Resources

Recommendation # 1: The Housing Department should develop a strategic plan for the Asset Management team that includes overall goals for loan servicing and monitoring for income-restricted apartments, performance metrics for different aspects of the program, staff roles, and resource needs.

Administration's Response to Recommendation # 1: The Administration agrees with this recommendation.

Green – The Housing Department has initiated development of a strategic framework for the Asset Management team that establishes program goals and resource needs for long-term monitoring of the multifamily housing loan portfolio. Existing performance metrics are already tracked by the Department, including the percentage of annual property compliance reviews completed and the average vacancy rate across stabilized properties.

These measures may be refined as part of future program evaluation efforts. The strategic planning effort will build upon ongoing process improvement work and evaluation of staffing and technology needs necessary to support the size and complexity of the City's affordable housing portfolio.

Target Completion Date: December 31, 2026

Recommendation # 2: Once the Housing Department establishes goals and clarifies expectations for the Asset Management team, staff should implement a software solution that allows more comprehensive management of the affordable multifamily housing portfolio. This could include modifications to existing software or the procurement of a new software platform.

Administration's Response to Recommendation # 2: The Administration agrees with this recommendation.

Green – The Housing Department has known the current software systems are insufficient to support comprehensive portfolio monitoring for over 20,000 units and centralized document management for the affordable multifamily housing loan portfolio. The Department is evaluating options to enhance existing systems or procure a specialized asset management platform capable of supporting financial monitoring, compliance tracking, inspection management, document storage, and reporting functions. The Department anticipates initiating a formal assessment and procurement process following completion of the strategic planning effort and identification of operational requirements, identified in recommendation #1.

Target Completion Date: December 31, 2027

Recommendation # 3: To expedite reviews of tenant income and rent compliance, the Housing Department should implement an automated tool to review data on rents and income limits.

Administration’s Response to Recommendation # 3: The Administration agrees with this recommendation.

Green – The Housing Department is in the process of transitioning to a new vendor and anticipates launching a new rent roll portal in early 2027 to streamline tenant income and rent compliance reviews. The portal is expected to allow property managers to electronically upload rent roll and tenant income information and incorporate automated validation checks for rent caps, income limits, and missing documentation. The Housing Department anticipates testing and implementing the portal to improve review efficiency, strengthen compliance monitoring, and support more consistent affordability review processes across the portfolio.

Target Completion Date: March 31, 2027

Recommendation # 4: To standardize affordable multifamily housing loan monitoring, the Housing Department should update and standardize operating procedures, including guidance for:

- a. Completing financial and affordability restriction reviews,
- b. Conducting building inspections, and
- c. Maintaining document submissions in a centralized file or software system.

Administration’s Response to Recommendation # 4: The Administration agrees with this recommendation.

Green – The Housing Department is currently developing updated standard operating procedures for the Asset Management team to support consistent monitoring practices across the multifamily housing portfolio. The updated procedures will include guidance

related to financial reviews, affordability compliance monitoring, inspection processes, loan agreement summaries, document retention standards, and centralized file management. The Department will also evaluate opportunities to standardize templates, tracking tools, and review workflows to improve consistency and institutional knowledge across the team. This work operates at the intersection of federal and state regulatory oversight so it will take time to identify a clear lane for the Department's compliance administration.

Target Completion Date: June 30, 2027

Recommendation # 5: The Housing Department should develop standard training for the Asset Management team to ensure reviews are completed in accordance with the operating procedures.

Administration's Response to Recommendation # 5: The Administration agrees with this recommendation.

Green – Because asset management work is highly procedural and project-specific, the Housing Department will continue training staff primarily through a coordinated approach that aligns updated standard operating procedures, with structured on-the-job training and supervisory guidance, rather than through a standalone formal training program. As procedures are finalized, the Department will concurrently develop standardized onboarding materials and reference guides to ensure training and operational practices remain consistent and aligned. These materials are expected to address review procedures, inspection protocols, compliance monitoring requirements, software systems, and documentation standards.

Target Completion Date: June 30, 2027

Recommendation # 6: To expedite property reviews, the Housing Department should develop:

- a. Loan agreement summaries such that loan terms and requirements are easily accessible, and
- b. Checklists to track document submissions and completion status to facilitate verification.

Administration's Response to Recommendation # 6: The Administration agrees with this recommendation.

Yellow – The Housing Department has begun developing loan agreement summaries for the approximately 220 properties in the portfolio. Additionally, review checklists are being developed for financial reviews, affordability monitoring, inspections, and document submissions. These tools are intended to improve consistency in review processes, support supervisory oversight, and allow staff to more efficiently track

completion status and outstanding documentation requirements. This work operates at the intersection of federal and state regulatory oversight and will take time to identify a clear lane for the Department's compliance administration.

Target Completion Date: June 30, 2027

Finding 2: Housing Should Strengthen Oversight of Affordability Restrictions and Higher-Risk Properties

Recommendation # 7: The Housing Department should develop a policy for addressing tenants that exceed and fall well below income limits in affordable units. This may include changes to standard loan agreement terms going forward and considerations for units with tax credits or bond financing.

Administration's Response to Recommendation #7: The Administration agrees with this recommendation.

Yellow – Affordable housing regulations administered through agencies such as the U.S. Department of Housing and Urban Development, California Department of Housing and Community Development, California Tax Credit Allocation Committee, and California Housing Finance Agency establish income eligibility at initial and ongoing occupancy while also recognizing that tenant incomes may change over time and are addressed through applicable monitoring, recertification, rent-adjustment, and compliance mechanisms rather than automatic tenant displacement. At the same time, the Department notes that post-occupancy income increases do not necessarily constitute noncompliance or require tenant displacement, and the appropriate compliance response may vary depending on the project's governing regulatory agreements, funding sources, and applicable federal or state program rules.

The Department's new rent roll portal is expected to support enhanced compliance monitoring by improving the Department's ability to review tenant income and rent data more consistently across the portfolio. The Department is also updating its funding regulations and policies to strengthen oversight of rent-burdened households and project compliance more generally. This work operates within a complex regulatory framework involving overlapping federal, state, and local requirements. As a lender and local funding agency, the Department will continue to assess the appropriate scope of its compliance monitoring role, including when project-level concerns should be addressed through City loan compliance processes or referred to the applicable federal or state regulatory agency.

Target Completion Date: June 30, 2027

Recommendation # 8: The Housing Department should establish clear escalation policies to address higher-risk properties. These policies should include:

- a. Clear definitions of noncompliance from financial and affordability restriction monitoring and property inspections,
- b. Escalation processes and steps staff should take to resolve concerns, including when inspection staff should issue violation notices,
- c. How escalation steps should be communicated to property managers and borrowers, and
- d. When Housing staff should notify other City compliance departments regarding property violations.

Administration's Response to Recommendation # 8: The Administration agrees with this recommendation.

Yellow – The Housing Department is developing more formalized compliance and escalation procedures for the Asset Management program to support consistent responses to financial, operational, affordability, and inspection-related concerns. The Department anticipates developing standardized definitions of noncompliance, documented escalation steps, and communication protocols for use with borrowers and property managers. The Department also plans to continue coordination with Planning, Building and Code Enforcement and Fire Departments regarding property condition concerns and enforcement coordination. This work operates at the intersection of federal and state regulatory oversight and will take time to identify a clear lane for the Department's compliance administration.

Target Completion Date: June 30, 2027

Recommendation # 9: To better assess the financial health of properties and detect issues in the affordable multifamily housing loan portfolio, the Housing Department should implement a risk rating model that:

- a. Defines risk categories and evaluation criteria, and
- b. Establishes clear procedures for how often and how thoroughly financial reviews are conducted based on a property's risk level.

Administration's Response to Recommendation # 9: The Administration agrees with this recommendation.

Yellow – The Housing Department recognizes the value of implementing a formal risk rating model to distinguish between higher-performing and underperforming properties within the portfolio and identify potential concerns earlier. Given the size and complexity of the Department's Affordable Multifamily Housing Loan portfolio of approximately 220 properties, development and implementation of a comprehensive risk rating framework will require a phased approach to ensure the model is effective, consistent, and administratively sustainable.

JOE ROIS, CITY AUDITOR

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The Department will evaluate industry best practices and incorporate risk indicators related to financial performance, property condition, affordability compliance, and operational concerns to support earlier intervention and more targeted monitoring activities. The risk rating framework will likely establish risk categories, define evaluation criteria, and inform the frequency and depth of future financial reviews and property inspections on a property's assigned risk level. This work operates at the intersection of federal and state regulatory oversight, as well as tax credit equity investor requirements and will take time to identify a clear lane for the Department's compliance administration.

Target Completion Date: December 31, 2027

COORDINATION

This report has been prepared in coordination with the City Manager's Office and City Attorney's Office.

CONCLUSION

The Housing Department appreciates the City Auditor's review of the Affordable Multifamily Housing Loan Portfolio and the assessment of the Department's asset management and compliance monitoring practices. As outlined in the Department's responses, Housing agrees with all recommendations and has either initiated or is in the process of implementing measures to strengthen portfolio oversight, standardize monitoring procedures, improve compliance tracking, and enhance long-term operational effectiveness.

The Department remains committed to preserving and monitoring the City's affordable housing investments, maintaining compliance with affordability and regulatory requirements, and improving systems and processes necessary to support the size and complexity of the City's multifamily housing portfolio. Housing will continue coordinating with internal and external partners to implement the audit recommendations while supporting the long-term financial and physical stability of affordable housing properties citywide.

/s/

Erik L. Soliván

Housing Director

For questions, please contact Banu San, Deputy Director, Housing Department, at Banu.San@sanjoseca.gov.