



MEMORANDUM

To: Board of Directors

Date: February 25, 2025

From: Ellen Martin and Sharyl Silva
California Housing Finance Agency

Subject: Accessory Dwelling Unit Grant Program

This memorandum provides an update regarding allegations of fraudulent and/or unprofessional activity by several different Accessory Dwelling Unit (ADU) contractors and construction companies. CalHFA's ADU Grant program is set up to protect taxpayer funds from unscrupulous actors, but we are conducting a review of all ADU grant files for homeowners that used specific contractors alleged to have participated in these activities.

CalHFA's ADU Grant program provides funding for predevelopment and other costs necessary to build an ADU. Because CalHFA is not a direct lender (i.e., it does not provide loans or funds directly to homeowners), the ADU Grant Program was deployed through CalHFA's network of ADU partners, including lenders, credit unions, nonprofits, and local government agencies qualified to manage the grant funds in accordance with the ADU Grant Program guidelines.

The ADU Grant Program partner then works directly with the ADU grantee to monitor the progress of the ADU construction process and release grant funds in accordance with program guidelines, as described more specifically below.

CalHFA's ongoing review of all ADU grant files will ensure that CalHFA ADU Grant Program Partners have properly disbursed ADU grant program funds. If irregularities or inappropriate disbursements are identified, CalHFA will work with the ADU Grant Program partner to identify appropriate avenues of restitution.

ADU Construction and Contractor Fraud/Scam Allegations

CalHFA is aware of a number of allegations of fraudulent activity on the part of several different contractors and construction companies in the ADU ecosystem. Based on information from our ADU grant program partners, we understand that a very limited number of CalHFA ADU grantees (fewer than 20 homeowners at current count) were working with construction companies or contractors that failed to complete work for which they were contracted. Some of these companies or contractors may have received payment for predevelopment and/or construction work on ADU projects.

While CalHFA does not have an investigatory arm, we do work closely with the Department of Financial Protection and Innovation, the Department of Consumer Affairs, the Contractor State Licensing Board, the Department of Justice, and the Consumer Financial Protection Bureau.

When CalHFA is made aware of allegations of fraud or other illegal activities, we gather relevant information and share said information with the appropriate investigative organization. CalHFA, however, is not privy to the status or even existence of any investigations that may result.

CalHFA is aware of contractor and construction company issues reported and has engaged with the appropriate investigative organizations to provide relevant information.

In addition, CalHFA is responsible for ensuring that ADU grant funds were administered according to established program guidelines by our ADU Grant Program Partners. As described below, CalHFA has robust fraud deterrent and prevention measures in place to ensure that ADU grant funds are used only to reimburse eligible costs and completed work.

Fraud Deterrent and Prevention Measures

CalHFA designed the ADU grant program to ensure that grant funds were expended for eligible uses only, that work is completed prior to reimbursement, and that an ADU is actually constructed.

The key to the ADU grant program fraud deterrent and prevention is the requirement

that all ADU grant funds be deposited into a managed construction escrow account. That construction escrow account is managed by our ADU construction lender or nonprofit ADU partners.

Draw requests are submitted to the ADU lender/partner by the homeowner or the vendor, in which case the homeowner approves the draw request. The lender or partner then reviews the request, confirms that the work has been completed, ensures there is appropriate supporting documentation, and releases funds. This process ensures that ADU grant funds are only spent on eligible costs for completed work.

Grant funds may only be distributed to directly pay vendors for completed and properly invoiced work or to write down the principal balance on the loan. No grant funds may be distributed directly to the grantee.

Critically, when the ADU project is complete, the lender/partner is required to submit the Certificate of Occupancy to CalHFA. If they are not able to produce a Certificate of Occupancy, the lender is required to return the grant funds to CalHFA.

These processes ensure that sufficient funds are retained in the managed construction escrow account to cover the ADU grant until the ADU is completed.

In concert with our ADU program partners, CalHFA is reviewing all payments using grant funds made by our third-party construction escrow providers to entities that are the subject of fraud or scam allegations. If we identify that an ADU Grant Program partner has incorrectly administered the grant funds, we will work with that partner to establish appropriate remedies that maintain the integrity of the ADU grant program and supporting taxpayer funds.

ADU Grantee Tax Liability

Grant recipients do receive a 1099-G when their grant is funded. If the grant funds are not used and returned to CalHFA, as would be the case if the ADU is not completed or the managed construction escrow account is closed, CalHFA will issue a revised 1099-G.

Currently, CalHFA understands most of the impacted ADU grantees are working with their ADU lender/partner to find new contractors and vendors to complete their ADU

project. In many cases, our ADU partners are working to identify alternative sources of funding, such as local government funds or even donated materials.

It is important to note that CalHFA grant funds do not currently have an expiration date, which offers our ADU Grant Program partners and grantees the flexibility needed to secure new contractors and take other steps to complete their ADU project.

Assistance for Affected Grantees

As stated above, CalHFA is reviewing ADU grant files for all affected grantees that are identified by our ADU grant program partners. If CalHFA identifies that grant funds were not properly administered, we will work to identify appropriate remedies on a case-by-case basis.

In addition, we have received reports that a handful of ADU grantees may have bypassed the managed construction escrow process and made direct payments to contractors or construction companies. Where appropriate, CalHFA is working with our ADU partners and individual grantees on a case-by-case basis to provide support and guidance for those circumstances. Grantees that do not wish or are not able to proceed with their project may return the grant funds at any time, but CalHFA understands that most grantees are proceeding with their project with the support of their ADU grant program partner.

Consumers that suspect that they have been the victim of financial or other fraud are encouraged to contact local law enforcement, the [Department of Financial Protection and Innovation](#), and the [Contractor State Licensing Board](#) to file a report. The more information these entities have regarding alleged fraud, the better equipped they are to investigate. Consumers with a construction loan are also encouraged to contact their lender directly to discuss available options. ADU grantees are specifically encouraged to contact their managed construction escrow provider, who can provide assistance and guidance. If ADU grantees suspect that their ADU grant funds were not used for eligible and completed predevelopment work, they should notify CalHFA via an email to complaintresolutiondepartment@calhfa.ca.gov.

In concert with our ADU partners, CalHFA will continue to monitor the status of any known investigations and litigation activity, and any restitution that may be offered to ADU grantees. We also continue to work with our ADU partners to understand the scale of impacted ADU grantees. Based on the outcomes of these efforts, we will work to identify any future programmatic interventions that may be appropriate and will seek guidance from the Board at that time.