

**ANALYSIS OF CITY OF LOS ANGELES
RENT STABILIZATION ORDINANCE
MAJOR REHABILITATION PROGRAM**

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Analysis of Los Angeles Rent Stabilization Major Rehabilitation Program

Executive Summary

A. Purpose

The Los Angeles Housing Department (LAHD) Rent Stabilization Division (RSD) commissioned David Paul Rosen & Associates (DRA) to prepare background economic research and analysis and recommend any changes that should be made to the program so that it better fulfills the purposes of the Rent Stabilization Ordinance. LAHD also retained DRA to assist in crafting a consensus recommendation to the City Council from the participation of an Advisory Committee representing landlords and renters.

The goals of the City of Los Angeles Rent Stabilization Ordinance, as specified in Section 151.01, are to “regulate rents so as to safeguard tenants from excessive rent increases, while at the same time providing landlords with just and reasonable returns from their rental units.” The impetus for this study was a concern on behalf of the City Council that evidence suggested landlords may have employed, or attempted to employ, the major rehabilitation provisions of the RSO to improperly evict long-term, low-rent paying tenants and reposition their markets as high-rent buildings through high-end renovations. The City has a policy interest in preserving stabilized rents while at the same time encouraging reinvestments in building condition.

The study documents economic data and analysis that formed the basis for DRA’s recommendations, to assist the City Council in reaching informed decisions on revisions to the program. In particular, the City Council directed the Consultant to gather and develop information that will allow the City to make informed policy decisions regarding the following issues raised by the Housing and Community Development Committee:

1. The retention, elimination or redefinition of major rehabilitation as an allowed ground for tenant evictions;
2. The determination of an appropriate dollar threshold, if any, for major rehabilitation evictions; and,
3. The establishment of temporary relocation thresholds or assistance requirements for construction work that does not involve the eviction of tenants.

B. Background

It is generally recognized by housing policy analysts that the regulation of residential rents may create financial disincentives for owners to invest in maintenance and capital improvements of their units. Therefore, the RSO contains provisions for a variety of reinvestment programs that seek to counterbalance the disincentives for investment. These include provisions for major rehabilitation, capital improvements, and rehabilitation related to housing code changes and natural disasters. The purpose of this study is to analyze provisions of the major rehabilitation program.

The current definition for major rehabilitation in the RSO requires each of three standards be met:

1. The total cost of rehabilitation work per unit must be at least \$10,000;
2. Primary work – defined as work of a structural, plumbing, electrical or mechanical nature for which a building permit is required – must be at least \$9,000 per unit; and,
3. The work must render the unit uninhabitable for a period of at least 45 days.

The major rehabilitation provisions of the RSO further require landlords to maintain at least 25 percent (25%) of the rehabilitated units at the prior rent level plus allowable annual increases for a period of 30 years. This provision applies to landlords who have used the major rehabilitation eviction provision of the RSO on four or more rental units within a two-year period.

C. Data/Economic Analysis and Case Studies

DRA analyzed available data on the housing stock, and particularly the rent-stabilized stock, in Los Angeles, including unit production, demolitions, rents, vacancy rates, turnover rates and historical applications and investment under the Rent Stabilization Ordinance major rehabilitation (major rehabilitation) and capital improvement programs.

DRA also conducted case studies of seven selected cities in California and nationwide with rent control ordinances and regulations. These cities are Santa Monica, San Francisco, West Hollywood, Berkeley, Oakland, San Jose and New York City. DRA reviewed rent control ordinances and interviewed city staff to understand the definitions of capital improvements, permitted rent increases, and permanent or temporary relocation benefit provisions of rehabilitation program in these cities.

D. Advisory Committee Review Process

DRA reviewed the findings of the data and economic analyses through a series of meetings with an Advisory Committee composed of landlord and tenant stakeholder representatives. **Appendix A** contains a list of Advisory Committee participants as well as agendas and notes from the meetings. The goal of the Advisory Committee review process was to build consensus on the recommended revisions to the RSO major rehabilitation program.

DRA initially met with the Advisory Committee on September 9, 2002 to review the scope and methodology of the study. A second meeting of the Advisory Committee was held on November 4 to review available data on the L.A. housing market and DRA's approach to the economic analysis on landlord return.

A third meeting of the Advisory Committee was held on December 9, 2002 to review DRA's draft recommendations based on the findings of the economic analysis. A fourth meeting was held on December 17, 2002 to review refinements and revisions to DRA's conclusions and recommendations, and to craft a consensus recommendation for revisions to the major rehabilitation processes. A fifth and final meeting was held on February 19, 2003 to review and finalize the Advisory Committee's consensus recommendations for revisions to the major rehabilitation program, and to agree to forward these recommendations to the City Council.

In addition to the formal Advisory Committee meetings, DRA held additional meetings and teleconferences with landlord and tenant stakeholder representatives to hear concerns with the existing provisions of the major rehabilitation program and gather input on DRA's draft recommendations.

E. Recommended Program Revisions

The Advisory Committee's consensus recommendations on changes to the major rehabilitation program are based on a combination of economic data analysis, case studies of other cities with rent stabilization rehabilitation provisions, and a consensus approach that seeks to balance competing interests of owner and renter stakeholder groups. These recommendations are supported by consensus of the Advisory Committee as a fair compromise. They represent a middle ground that is limited on both ends of the spectrum of preserving affordability for low income tenants and stimulating investment in rent-stabilized properties.

The full report discusses policy options and recommendations considered by the Advisory Committee (Section V: Policy Options and Recommendations). Each of the conclusions and recommendations below is discussed in the context of the economic analysis, review of other City practices regarding Rent Stabilization and Major Rehabilitation, and Advisory Committee consensus and compromise.

Within the context of the Rent Stabilization Ordinance, the goals of the major rehabilitation program should be to: (1) to encourage needed investment in the rent-stabilized housing stock without allowing speculation and gentrification; and (2) to protect in-place tenants from excessive rent increases and unnecessary eviction. To better meet these goals, the Advisory Committee recommends the following changes and additions to the major rehabilitation program:

Recommendation #1: No eviction of in-place tenants for rehabilitation work. Tenants do not relinquish their "lease" on rehabilitated units that must be vacated for repairs. Tenants may be temporarily relocated so repairs may be completed. However, all tenants have the right to return to their unit. Vacating the unit is no longer mandatory to qualify for major rehabilitation.

Anecdotal evidence, supported by the geographic distribution of major rehabilitation applications, suggests that landlords may have employed, or attempted to employ, the major rehabilitation provisions of the RSO to improperly evict long-term, low-rent paying tenants and reposition their markets as high-rent buildings through high-end renovations. This is not consistent with the goals of the RSO. Prohibiting evictions will remove landlords' incentives to use, or threaten to use, the major rehabilitation program in this manner.

The geographic distribution of major rehabilitation applications in the last several years indicates they are in higher rent areas of the City where market pressures to reposition properties as high-rent buildings are strong. Of the 373 affected units in major rehabilitation applications processed between 1999 and July 31, 2002, 32 percent (120 units) were in the downtown area. Another 32 percent (117 units) were in the Wilshire, Westlake and Hollywood areas. The other largest concentrations of major rehabilitation units were in Venice (12 percent, 46 units) and West Los Angeles (4 percent, 16 units).

Recommendation #2: Temporary relocation with the right to return for all relocated tenants. A landlord must provide for the relocation of tenants, including costs for two moves, in a comparable unit and comparable area of the City. Prior to receiving a building permit, landlords must provide an acceptable means and methods plan for relocating affected tenants. For relocations under 30 days, or for longer periods with the tenant's consent, the landlord can put up a tenant in a hotel.

Temporary relocation is needed at times for the safety of in-place tenants, such as when asbestos or other safety hazards exist or the scope of the primary work is extensive.

The rent stabilization provisions of all of the other cities surveyed provide for temporary relocation in certain circumstances, specifically when substantial repairs are ordered by a government agency and/or a government agency has determined that the work cannot be completed unless the tenant is relocated. In Santa Monica, West Hollywood, and San Francisco, landlords are required to provide comparable units in a comparable area of the city or to make up any rent differential. In San Francisco, a tenant cannot be required to

vacate a unit for more than three months and landlords must pay each tenant \$1,000 for moving and relocation expenses.

Recommendation #3: Either LAHD/RSD staff or a third party LAHD/RSD contractor to certify new rents upon tenants' return. The new rent must be certified by LAHD or its contractor prior to issuance of final inspection on building permit. LAHD/RSD will make the Final Determination as to whether tenants must vacate the unit for the rehabilitation work to proceed. LAHD/RSD will support a landlord's effort to enforce a determination that a unit must be vacated in order to perform the work in the event of tenant non-compliance after a reasonable notice has been given. Failure by landlords to pay for relocation costs, certify new rents, or comply with allowed rent increases will result in penalties, fines, and/or liens.

Landlords have not been applying for re-rental certificates as required under the major rehabilitation program, and to document their compliance with the 25 percent set-aside requirement at former rent levels. Increased monitoring and enforcement provisions are required to ensure that landlords comply with the recommended new provisions.

Recommendation #4: Permanent relocation for cases who cannot be expected to move twice. (The amount of permanent relocation benefits should be evaluated in the context of the entire RSO). Tenants entitled to permanent relocation benefits would be limited to designated cases, similar to those recommended in San Francisco: tenants over the age of 62 who have been in their unit for 10 years; tenants who are disabled and have been in their unit for 10 years; tenants who suffer from a severe illness and have been in their unit for at least 5 years.

Recommendation #5: Increases in the floor rents for investment in "primary work" items, plus temporary and/or permanent relocation costs, calculated by amortizing the dollar amount of construction and relocation costs plus compound interest at an indexed rate. Determine an amortization schedule and finance index by regulation. Monthly dollar rent increases should be capped at 10 percent of current tenant rent. Only one 10 percent rent increase is allowed per tenancy, except for items that have reached the end of their amortized life per the schedule published by regulation. The 10 percent cap applies to primary work items that must be repaired or replaced again. Increases to be applied at rate of 5 percent of pre-rehabilitation rent upon re-occupancy, and 5 percent of pre-rehabilitation rent on next rent anniversary date. Annual rent adjustments apply per current RSO in addition to these "pass through" rent increases.

The 10 percent cap on the rent increase and two-year phase-in represents the best compromise solution that could be agreed upon by the Advisory Committee. Landlord representatives prefer a higher rent cap or no cap to encourage rehabilitation of the housing stock. Tenant representatives prefer a lower rent cap or no rent increase at all to preserve affordability for lower income tenants.

The allowable rent increase for major rehabilitation should be retained for at least three years from the date the rehabilitation is completed, regardless of unit turnover, i.e. no vacancy decontrol for three years from the date the unit rehabilitation is classified complete.

The major rehabilitation rent increase remains in force permanently in the event the unit is not vacated by the tenant last occupying the unit pre-rehabilitation. After three years, the unit rent is subject to decontrol upon the next vacancy.

DRA analyzed the permitted rent increases and supportable investment under a capitalization rate approach, which models investment under financial underwriting standards, and an amortization approach used by several cities surveyed, including San Francisco, Oakland, San Jose and New York. DRA determined that these approaches can provide a reasonable return to landlords on their investment. The amortization approach was determined to be easier to understand and to implement. An amortization period of 20 years and an interest rate equal to the ten-year Treasury rate plus a one-percent spread was determined to be equivalent to a 9 percent cap rate.

An amortization schedule should be developed for primary work items related to the anticipated useful life of the improvement. An interest rate index and spread should be selected to provide a reasonable rate of return to landlords on their investment.

Recommendation #6: Failure for a landlord to pay all of the temporary or permanent relocation benefits required, or failure of the landlord to certify a proper new rent, will subject the landlord to a lien filed by the City equivalent in seniority to a tax lien, and subject the owner to fines and penalties as specified in the RSO.

As noted above, landlords have not been applying for re-rental certificates as required under the major rehabilitation program, and to document their compliance with the 25 percent set-aside requirement at former rent levels. Increased monitoring and enforcement provisions are required to ensure that landlords comply with the recommended new provisions.

Recommendation #7: Eliminate current thresholds for primary work as defined by the major rehabilitation program.

The 10 percent cap on rent increases will create a limit on the amount investors will be willing to invest, therefore increasing the thresholds will reduce the “window” of investment. Since evictions will be prohibited and permitted rent increases will be tied to the costs of rehabilitation work and relocation costs, the thresholds for the major rehabilitation are no longer considered necessary. The goal of removing the thresholds is to provide an incentive for landlords to undertake lower cost primary work to help extend the useful life of rent-stabilized buildings.

Recommendation #8: Review and revision, as needed, of the primary work definition in the RSO to ensure that it effectively limits allowed improvements to those required to extend useful life of the building, and prohibits those that would reposition the building to a higher rent market.

F. Additional Observations

Through the course of our work, DRA also identified the following larger issues related to capital investment in the rent-stabilized stock:

1. The rent-stabilized stock will likely degrade over time without continued investment in capital improvements, including at times, major rehabilitation. Adjusting the major rehabilitation provisions of the RSO cannot create an incentive for investment in areas where market rents are insufficiently high to finance rehabilitation costs. The proposed cap on rent increases, combined with the temporary relocation benefit, will limit the amount of money invested by owners in major rehabilitation.
2. One way for the City to avoid the decline of the rent-stabilized stock in low income areas is to transfer ownership to non-speculative owners and provide subsidies for rehabilitation. This strategy requires a strong nonprofit developer community interested in and capable of taking over long-term ownership of RSO properties. This requires a concerted citywide effort. To apply this strategy to just one fifth of the rent stabilized housing stock in Los Angeles likely will require capital subsidies in excess of \$2 billion.
3. The City of Los Angeles will benefit from aggressively pursuing State bond and other financing sources to rehabilitate and preserve the City's existing rent-stabilized affordable housing stock.
4. One Advisory Committee member representing landlord interests suggested that some owners of RSO properties may be willing to permanently restrict a percentage of units in their buildings as affordable to very low income household rents in exchange for permanently decontrolling the balance of the building. While no percentages were specified in this suggestion (e.g. 40 percent of the units affordable to families at 50 percent area median income; 60 percent of the units at market rate), DRA finds this suggestion compelling and intriguing. If indeed owners are willing to permanently restrict a meaningful percentage of their units, then over the very long term, from a housing policy perspective for the City of Los Angeles, this may better preserve affordable housing and at the same time target it to very low income eligible households. This suggestion merits evaluation and development if feasible.

5. The provisions of the major rehabilitation program cannot be viewed in isolation of other provisions of the RSO. All provisions of the RSO which affect investment in the rent-stabilized stock should be reviewed in combination, including major rehabilitation, capital improvements, cited rehabilitation, and permanent relocation benefits.
6. As well as providing incentives to landlords to invest in the preservation of their buildings through permitted rent increases as described above, City policy should discourage landlords from allowing buildings to deteriorate. To this end, the City should continue the current RSO policy prohibiting landlords from passing through rent increases for costs to correct code violations, except for changes to the building code per current RSO. In addition, the City should continue its current policy of aggressive code enforcement through the Systematic Code Enforcement Program (SCEP) and Rent Escrow Account Program (REAP). Landlords who allow their properties to fall into continued disrepair, as determined by the REAP program or some other standard, must repair their buildings to defined standards with no rent increase allowed.
7. We project limited use of the major rehabilitation as proposed above. Most of the recent applications for the major rehabilitation program have been in areas where market rents are high or rapidly increasing, and presumably are speculative in nature. Limits on rent increases based on the cost of primary work plus temporary relocation will limit the owner's ability to raise rents to market and will sharply reduce speculative use of the major rehabilitation program.
8. Limiting speculative rent increases in rent-stabilized stock through the proposed changes to the major rehabilitation program will likely lead to increased demolition of the existing stock in high rent areas of the City. Under the Ellis Act, owners have the right to exit the multifamily rental housing business and use their property for another use, such as owner housing. In some areas current zoning is at a lower density which, combined with market forces, will lead to a reduction in the number of housing units. We recommend that the City develop (1) replacement housing requirements as a means to replace some the lost affordable housing stock; and (2) permanent relocation benefits as a means to protect the most economically vulnerable tenants currently residing in stabilized units.

G. Next Steps

Through the course of our work, a number of additional tasks suggest themselves as necessary to complete the proposed revisions to the major rehabilitation program of the RSO. These tasks include:

1. Develop a formula for permanent relocation benefit amounts within the context of the entire RSO;
2. Reform the capital improvement program, consistent with the recommended reforms to the major rehabilitation program;
3. Develop a formula for major rehabilitation rent increases employing the amortization approach, amortization schedules for various improvements, and an interest rate index by regulation;
4. Review and revise as appropriate the definition of “primary work” in the major rehabilitation program to eliminate rehabilitation activities which may “gentrify” RSO buildings;
5. Review the feasibility and acceptability of the suggestion that some RSO building owners may be willing to permanently restrict a percentage of their units as affordable to very low income households in exchange for decontrolling the balance of the units in their buildings. This proposal may provide more rental housing affordable to very low income households than the RSO program will over the long term;
6. Examine the feasibility and proposed program guidelines and financing sources for an acquisition/rehabilitation program by non-speculative owners of RSO properties. This program would bring into permanent deed restriction buildings which otherwise reset unit rents to market upon every vacancy;
7. Develop a replacement housing program proposal for the City of Los Angeles, in light of active demolition activity among RSO building owners already under way. Demolitions are likely to continue or accelerate as high market rent areas of the City increase pressure for demolition and construction of new, high end housing.

I. City of Los Angeles Housing Market Overview

This section provides an overview of housing market conditions, providing the economic backdrop for consideration of revisions to the RSO major rehabilitation program.

A. Housing Stock, Tenure and Occupancy

As indicated in **Table 1** below, the 2000 Census reports that there were a total of 1,337,706 housing units in the City, of which 783,530, or 58.6 percent, were renter-occupied. An additional 491,882 units, or 36.8 percent, were owner-occupied and the remaining 62,294 units, or 4.66 percent, were vacant.

Table 1
Housing Units, Tenure and Occupancy
City of Los Angeles
2000 Census

	Number	Percent of Total Housing Units
Renter-Occupied Units	783,530	58.6%
Owner-Occupied Units	491,882	36.8%
Total Occupied Units	1,275,412	95.3%
Vacant Units	62,294	4.7%
Total Housing Units	1,337,706	100.0%

Source: 2000 U.S. Census; David Paul Rosen & Associates.

B. Housing Production and Demolition Trends

Table 2 below displays residential building permit data for the City of Los Angeles for the last two decades from the Construction Industry Research Board (CIRB). Multifamily housing production peaked in 1985 and 1986, just prior to the Tax Reform Act of 1986, which unfavorably revised tax laws with respect to the treatment of rental properties. Multifamily housing unit production reached its lowest level in 1996, and has increased in the last several years.

Table 3 shows housing demolitions in the City of Los Angeles during the 2000 through 2002 period. Demolitions have averaged 716 units per year over the past three years.

Table 2
New Housing Unit Production
City of Los Angeles
1981 to 2001

Year	Single-Family Units	Multifamily Units	Total Housing Units
1981	916	7,253	8,169
1982	732	4,514	5,246
1983	1,124	8,608	9,732
1984	2,020	12,395	14,415
1985	2,004	20,499	22,503
1986	2,350	20,357	22,707
1987	2,324	16,931	19,255
1988	2,088	18,121	20,209
1989	2,550	12,804	15,354
1990	1,869	9,957	11,826
1991	1,166	4,649	5,815
1992	911	1,716	2,627
1993	436	1,627	2,063
1994	880	1,549	2,429
1995	983	1,654	2,637
1996	873	1,305	2,178
1997	1,201	2,039	3,240
1998	1,334	1,474	2,808
1999	1,384	3,067	4,451
2000	1,679	4,950	6,629
2001	1,723	5,528	7,251

Source: Construction Industry Research Board David Paul Rosen & Associates.

**Table 3
Housing Unit Demolitions
City of Los Angeles
1999 to 2002**

Council District	2000	2001	2002	Total
CD 1	17	18	93	128
CD 2	50	33	0	83
CD 3	21	0	1	22
CD 4	215	182	50	447
CD 5	101	118	90	309
CD 6	15	10	39	64
CD 7	2	0	0	2
CD 8	32	18	19	69
CD 9	109	33	3	145
CD 10	22	1	16	39
CD 11	125	156	64	345
CD 12	0	0	0	0
CD 13	3	31	37	71
CD 14	1	11	382	394
CD 15	10	0	10	20
TOTAL	723	611	804	2,138
Annual Average				713

Source: City of Los Angeles Housing Department; David Paul Rosen & Associates.

C. Rental Housing Vacancy Rate Trends

Table 4 below summarizes trends in rental housing vacancy rates between 1980 and August 31, 2002 based on water meter data provided by the Los Angeles Department of Water and Power (DWP). Generally, a vacancy rate below 5.0% is considered to reflect a “tight” housing market, which makes it difficult for renters to move into or within the area and find new housing. The overall rental housing vacancy rate for the City has been above 5.0% only during the period of 1992 through 1997, when the regional economy was in recession. For the last three years, the vacancy rate has approximated 3.5 percent, indicating a tight rental housing market.

Table 4
Rental Housing Vacancy Rates
City of Los Angeles
1980 to 2002

1980	3.1%
1982	3.7%
1984	3.2%
1986	3.9%
1988	4.5%
1990	5.0%
1992	6.7%
1993	7.9%
1996	8.1%
1997	7.2%
1998	5.4%
1999	4.4%
2000	3.5%
2001	3.7%
2002	3.5%

Source: Los Angeles Department of Water and Power; all vacancies are for December 31 except for 2002 which is August 31. Data for the year is 1996 through 2002 or derived from the City’s website. Prior year data (including missing years) were quoted by the HR&A study.

Table 5 below summarizes the DWP rental housing vacancy rate data by market subarea for the 1996 through 2002 period. The data show considerable variation in vacancy rates by subarea. Interestingly, vacancy rates in the West Los Angeles area remained very low during the recession years 1996 through 1998, but have increased somewhat in the last two years. Rental vacancy rates in all subareas have been below 5.0% for the past three years.

Table 5
Rental Housing Vacancy Rates by Market Subarea
City of Los Angeles
1996 to 2002

	San Fernando Valley	West Los Angeles	Central Los Angeles	Harbor	Northeast Los Angeles	Total City
1996	9.0%	3.5%	9.1%	7.1%	8.2%	8.1%
1997	7.2%	3.2%	8.4%	7.1%	8.3%	7.2%
1998	4.7%	2.7%	6.5%	5.1%	6.5%	5.4%
1999	3.4%	3.0%	5.3%	4.3%	4.4%	4.4%
2000	2.7%	2.9%	5.4%	2.9%	3.1%	3.5%
2001	2.9%	4.1%	4.0%	2.5%	2.9%	3.7%
2002	2.8%	4.3%	3.7%	2.3%	2.4%	3.5%

Source: Los Angeles Department of Water and Power; all vacancies are for December 31 except for 2002 which is August 31.

D. Housing Turnover

Table 6 shows tenure (renter, owner) by the year the householder moved into their present housing unit for the City of Los Angeles based on 2000 Census data. The data indicate that nearly 31 percent of renter households lived in their present housing unit for less than one year. Another 42 percent of renter households lived in their units for two to five years, for a total of 73 percent of renters who lived in their present unit for five years or less. At the other end of the spectrum, 8 percent of householders lived in their units for 10 to 20 years, 4 percent for 21 to 30 years, and 2 percent for over 30 years.

Table 6
TENURE BY YEAR HOUSEHOLDER MOVED INTO UNIT
CITY OF LOS ANGELES
2000 Census

Year Householder Moved Into Unit		1999	1995 to 1998	1990 to 1994	1980 to 1990	1970 to 1979	Before 1970	Total
Years in Unit (1)		1 Year	2 to 5 Years	7 to 10 Years	10 to 20 Years	21 to 30 Years	Over 30 Years	
Owners	Number of HH	45,993	108,647	74,591	99,687	76,951	86,117	491,986
	Percent of HH	9.3%	22.1%	15.2%	20.3%	15.6%	17.5%	100.0%
Renter	Number of HH	238,734	326,812	112,475	64,297	29,492	11,632	783,442
	Percent of HH	30.5%	41.7%	14.4%	8.2%	3.8%	1.5%	100.0%
Total	Number of HH	284,727	435,459	187,066	163,984	106,443	97,749	1,275,428
	Percent of HH	22.3%	34.1%	14.7%	12.9%	8.3%	7.7%	100.0%

(1) As of the year 2000.

Source: 2000 U.S. Census; Los Angeles Planning Department, Demographics Unit; David Paul Rosen & Associates.

E. Market Rents

Table 7 summarizes the results of a rent survey conducted by the Southern California Association of Non-Profit Housing (SCANPH). The survey results include a total of 330 properties totaling 21,944 units, with an average of 66 units per property. Of these, 228 properties and 15,197 units (69 percent of total units and properties in the survey) reported which year the property was built. DRA divided the survey data into stabilized and non-stabilized properties based on year built. DRA calculated average rents by bedroom and bath count and by market subarea.

Table 8 summarizes rent data provided by REALFACTS for the period 1995 through 2002. These data have also been divided into stabilized and non-stabilized properties based on the year the property was built. The REALFACTS database includes a total of 205 properties and 45,205 units. The properties are on average larger than those in the SCANPH survey, with an average of 220 units.

In most cases, the average rent for rent-stabilized properties is lower than those for non-stabilized properties. However, with vacancy decontrol under the RSO and the high turnover rate in rental properties, the differential in average rents is not as great as one might expect. **Table 9** below compares the average rent by unit bedroom count for stabilized and non-stabilized properties using the 2002 REALFACTS data.

Table 9
Average Rental Rates for Stabilized and Non-Stabilized Properties
Based on REALFACTS Data
City of Los Angeles
2002

Bedrooms/ Baths	Non-Stabilized Properties	Stabilized Properties	Rent Differential	Percent Rent Differential
Studio/1 Bath	\$960	\$918	\$42	4.6%
1 BR/1 Bath	\$1,298	\$1,169	\$129	11.0%
2 BR/2 Bath	\$1,798	\$1,686	\$112	6.6%
3 BR/2 Bath	\$3,220	\$2,432	\$788	32.4%

Source: REALFACTS; David Paul Rosen & Associates

Table 7
SUMMARY OF SCANPH RENT SURVEY
2002

	Number Properties	Average Units Per Property	Number of Units	Percent of Units	Vacancy Rate	Average Monthly Rent	Percent of Stabilized Rent
RENT STABILIZED PROPERTIES (Built Before 1978)							
By Rental Market Area							
Beach	12	45	539	7%	2.4%	\$1,180	
Central LA	19	72	1,373	18%	1.5%	\$811	
Central LA West	23	27	629	8%	4.8%	\$1,300	
Downtown LA	12	99	1,188	15%	3.1%	\$1,187	
East San Fernando Valley	14	74	1,036	13%	2.4%	\$1,167	
Harbor/San Pedro	16	20	327	4%	7.0%	\$1,225	
Northeast LA	8	28	225	3%	4.9%	\$1,408	
South LA	13	132	1,716	22%	1.3%	\$940	
West LA	12	26	306	4%	4.9%	\$1,177	
West San Fernando Valley	9	55	493	6%	2.6%	\$979	
By Bedroom Count							
Studio	35	73	2,546	33%	2.1%	\$734	
1 BR/1 BA	36	69	2,472	32%	1.9%	\$899	
1 BR/1 BA/Loft/Den	2	61	122	2%	2.5%	\$1,299	
2 BR/1 BA	26	16	412	5%	9.0%	\$1,225	
2 BR/2 BA	21	82	1,714	22%	1.7%	\$1,416	
2 BR/2 BA/Loft/Den	5	57	287	4%	7.3%	\$1,858	
3 BR/2 BA	11	14	153	2%	10.5%	\$1,820	
Other	2	63	126	2%	3.2%	\$1,960	
Total/Average	138	57	7,832	100%	2.7%	\$1,126	
NON-RENT STABILIZED PROPERTIES (Built After 1978)							
By Rental Market Area							
Beach	3	30	91	1%	6.6%	\$990	84%
Central LA	7	44	310	4%	2.6%	\$802	99%
Central LA West	9	93	840	11%	1.3%	\$1,678	129%
Downtown LA	6	266	1,598	22%	4.3%	\$1,029	87%
East San Fernando Valley	15	93	1,401	19%	3.9%	\$1,063	91%
Harbor/San Pedro	12	43	520	7%	1.9%	\$1,513	124%
Northeast LA	10	40	403	5%	2.0%	\$1,187	84%
South LA	5	189	947	13%	2.2%	\$945	101%
West LA	7	16	109	1%	7.3%	\$1,669	142%
West San Fernando Valley	16	72	1,146	16%	2.6%	\$1,118	114%
By Bedroom Count							
Studio	9	219	1,971	10%	4.5%	\$926	126%
1 BR/1 BA	29	84	2,435	32%	3.0%	\$923	103%
1 BR/1 BA/Loft/Den	2	29	58	2%	3.4%	\$1,525	117%
2 BR/1 BA	10	48	481	11%	2.9%	\$1,061	87%
2 BR/2 BA	27	71	1,909	30%	1.8%	\$1,375	97%
2 BR/2 BA/Loft/Den	4	48	190	4%	2.6%	\$1,778	96%
3 BR/2 BA	7	46	319	8%	2.2%	\$1,879	103%
Other	2	1	2	2%	50.0%	\$1,995	102%
Total/Average	90	82	7,365	100%	3.1%	\$1,224	109%
ALL PROPERTIES IN SURVEY (1)							
By Rental Market Area							
Beach	30	26	772	4%	4.1%	\$1,106	
Central LA	42	48	2,011	9%	2.4%	\$806	
Central LA West	44	133	5,833	27%	0.9%	\$1,361	
Downtown LA	24	126	3,034	14%	3.8%	\$1,018	
East San Fernando Valley	40	69	2,761	13%	3.8%	\$1,104	
Harbor/San Pedro	38	23	863	4%	4.3%	\$1,356	
Northeast LA	24	42	1,018	5%	2.3%	\$1,204	
South LA	30	100	3,008	14%	1.8%	\$861	
West LA	29	19	564	3%	5.9%	\$1,328	
West San Fernando Valley	29	72	2,080	9%	2.6%	\$1,084	
By Bedroom Count							
Studio	72	73	5,266	24%	3.3%	\$734	
1 BR/1 BA	97	62	5,970	27%	2.8%	\$899	
1 BR/1 BA/Loft/Den	7	40	279	1%	3.6%	\$1,299	
2 BR/1 BA	51	23	1,158	5%	5.5%	\$1,225	
2 BR/2 BA	65	126	8,185	37%	1.0%	\$1,416	
2 BR/2 BA/Loft/Den	9	53	480	2%	5.6%	\$1,858	
3 BR/2 BA	24	20	481	2%	5.8%	\$1,820	
Other	5	25	125	1%	1.6%	\$1,960	
Total/Average	330	66	21,944	100%	2.5%	\$1,126	

(1) Includes properties for which year built was not available; so totals are greater than the sum of rent-stabilized and non-rent stabilized.
Source: Southern California Association of Non-Profit Housing; City of Los Angeles; David Paul Rosen & Associates.

Table 8
Average Rent by Unit Bedroom Count
Stabilized and Non-Stabilized Properties
City of Los Angeles
1995 to 2002

Bedrooms/ Baths	Average Annual Compound Increase									# of Units 2002	% of Units 2002	Ave. SF		
	1995	1996	1997	1998	1999	2000	2001	2002	95-98				99-02	95-02
Rent-Stabilized Properties (Up to 1978)														
Studio/1 BA	\$686	\$722	\$753	\$735	\$738	\$826	\$899	\$918	2.33%	7.55%	4.25%	2,326	11.7%	472
1 BR/1 BA	\$803	\$843	\$883	\$916	\$962	\$1,106	\$1,162	\$1,169	4.49%	6.71%	5.51%	8,832	44.3%	745
2 BR/1 BA	\$755	\$780	\$772	\$794	\$855	\$967	\$1,229	\$1,252	1.69%	13.56%	7.49%	604	3.0%	847
2 BR/2 BA	\$1,377	\$1,392	\$1,370	\$1,438	\$1,444	\$1,674	\$1,732	\$1,686	1.46%	5.30%	2.93%	7,237	36.3%	1,121
2 BR Townhome	\$1,072	\$1,108	\$1,109	\$1,255	\$1,626	\$1,702	\$1,744	\$1,755	5.39%	2.58%	7.30%	347	1.7%	1,014
3 BR/2 BA	\$1,579	\$1,686	\$1,799	\$2,053	\$2,172	\$2,457	\$2,534	\$2,432	9.14%	3.84%	6.36%	484	2.4%	1,709
3 BR Townhome	\$1,783	\$1,546	\$1,465	\$1,461	\$1,694	\$1,925	\$2,115	\$2,163	-6.42%	8.49%	2.80%	128	0.6%	1,923
Overall Average	\$1,003	\$1,018	\$1,075	\$1,091	\$1,133	\$1,294	\$1,346	\$1,346	2.84%	5.91%	4.29%	19,958	100.0%	857
Non-Rent Stabilized Properties (1979 and Later)														
Studio/1 BA	\$644	\$649	\$675	\$716	\$755	\$856	\$904	\$960	3.60%	8.34%	5.87%	4,510	16.3%	498
1 BR/1 BA	\$824	\$865	\$867	\$922	\$969	\$1,089	\$1,187	\$1,298	3.82%	10.23%	6.71%	13,269	47.9%	726
2 BR/1 BA	\$1,152	\$1,229	\$1,417	\$1,280	\$1,357	\$1,673	\$1,570	\$1,866	3.57%	11.20%	7.13%	1,051	3.8%	960
2 BR/2 BA	\$1,102	\$1,192	\$1,175	\$1,241	\$1,301	\$1,490	\$1,624	\$1,798	4.04%	11.39%	7.24%	6,264	22.6%	1,068
2 BR Townhome	\$1,087	\$1,075	\$1,128	\$1,217	\$1,266	\$1,410	\$2,111	\$2,330	3.84%	22.55%	11.51%	1,056	3.8%	1,280
3 BR/2 BA	\$1,220	\$1,301	\$1,338	\$1,715	\$1,663	\$2,033	\$2,430	\$3,220	12.02%	24.64%	14.87%	1,303	4.7%	1,502
3 BR Townhome	\$1,105	\$1,226	\$1,339	\$1,376	\$1,410	\$1,485	\$1,568	\$1,625	7.59%	4.84%	5.66%	275	1.0%	1,335
Overall Average	\$922	\$981	\$980	\$1,041	\$1,091	\$1,244	\$1,353	\$1,530	4.13%	11.93%	7.50%	27,728	100.0%	863
All Properties														
Studio/1 BA	\$672	\$697	\$724	\$727	\$739	\$830	\$896	\$908	2.66%	7.11%	4.39%	6,546	14.5%	478
1 BR/1 BA	\$808	\$847	\$869	\$910	\$956	\$1,092	\$1,161	\$1,176	4.04%	7.15%	5.51%	20,894	46.2%	733
2 BR/1 BA	\$885	\$955	\$981	\$1,006	\$1,060	\$1,213	\$1,310	\$1,310	4.36%	7.31%	5.76%	1,561	3.5%	859
2 BR/2 BA	\$1,253	\$1,284	\$1,274	\$1,332	\$1,358	\$1,567	\$1,662	\$1,659	2.06%	6.90%	4.09%	12,848	28.4%	1,074
2 BR Townhome	\$1,067	\$1,073	\$1,067	\$1,194	\$1,498	\$1,611	\$1,752	\$1,721	3.82%	4.73%	7.07%	1,333	2.9%	1,043
3 BR/2 BA	\$1,534	\$1,596	\$1,735	\$1,970	\$2,071	\$2,309	\$2,461	\$2,419	8.70%	5.31%	6.72%	1,626	3.6%	1,633
3 BR Townhome	\$1,671	\$1,480	\$1,426	\$1,430	\$1,627	\$1,770	\$1,928	\$1,883	-5.06%	4.99%	1.72%	397	0.9%	1,739
Overall Average	\$971	\$999	\$1,031	\$1,064	\$1,108	\$1,265	\$1,339	\$1,346	3.10%	6.70%	4.78%	45,205	100.0%	848

Source: REALFACTS; David Paul Rosen & Associates

F. Rental Property Sales Prices

Table 10 below summarizes sales data for multifamily rental properties of five units or more for the City of Los Angeles based on data from Dataquick Information Systems for the month of January 2002. The data are divided into stabilized and non-stabilized properties based on year built. The average sales price per unit for stabilized properties was approximately 29 percent higher than for non-stabilized properties, reflecting the age and rent differential in these two groups of properties.

Table 10
Summary of Multifamily Property Sales
City of Los Angeles
January 1, 2002 to February 1, 2002

	<u>Total Sales</u>	<u>Total Units</u>	<u>Average Units Per Property</u>	<u>Average Sales Price Per Unit</u>
Rent Stabilized Properties (Built Prior to 1979)	86	963	11	\$59,309
Non-Rent Stabilized Properties (Built After 1978)	25	387	15	\$76,380
Total	111	1,350	12	\$64,203

Source: Dataquick Information Systems; David Paul Rosen & Associates.

II. Historical Reinvestment Activity under the RSO

This section reviews data from the Los Angeles Housing Department on historical investment under the RSO's reinvestment programs, including major rehabilitation, capital improvement and cited rehabilitation.

A. Major Rehabilitation Program

Table 11 summarizes historical investment under the major rehabilitation program from 1985 to July, 2002 (except for 1993 to 1998 for which summary data are not available). Annual investment activity peaked in 1987 at \$16.3 million spent on 1,431 units. For the three and one-half year period from 1999 through July 31, 2002, investment activity totaled \$16.5 million for 676 units, affecting an average of about 200 units per year.

Table 12 tabulates the number of applications submitted, processed and denied under major rehabilitation program for the period January 1, 1999 through July 31, 2002 by planning district. The Housing Department received a total of 224 applications during this period, of which 119 were processed and 87 were denied. Over half of the applications submitted (126 or 56%) were for projects in the Hollywood, Wilshire, Venice and West Los Angeles subareas.

Table 13 details the number of housing units involved in the major rehabilitation applications submitted and processed over the same 1999 through 2002 period. The 87 properties for which applications were processed contain a total of 930 units. Of these total units, 373 units were affected by the major rehabilitation applications. For all of the applications processed over this time period, the average total rehabilitation cost per unit was \$26,800, and the average cost of the primary work was \$17,300.

B. Capital Improvement and Mandated Rehabilitation Program Activity

In addition to major rehabilitation, the RSO provides for rent increases associated with capital improvements, defined as the addition or replacement of a defined list of improvements that have a useful life of five or more years (e.g. roofing, carpeting, stuccoing, painting). Landlords are entitled to a temporary monthly rent increase equal to 1/60th of fifty percent (50%) of the average per unit capital improvement cost for a period not to exceed six years. The maximum temporary monthly surcharge is \$55.00, unless agreed upon in writing between tenant and landlord. If the temporary monthly surcharge based on the above formula is greater than \$55.00 per month, the surcharge period may be extended until the allowable capital improvement expenses are recovered.

The RSO also provides for rehabilitation work done to comply with an order of the Department of Building and Safety, Health Department, Fire Department due to changes in the housing code or to repair damage resulting from fire, earthquake or other natural disasters.

Table 14 summarizes program activity for the capital improvement and mandated rehabilitated program of the RSO

Table 11
Historical Investment under the Major Rehabilitation Program
City of Los Angeles Rent Stabilization Ordinance
1985 to July 31, 2002

Year	Total Investment	Total Units	Average/ Unit
1985	\$4,847,673	419	\$11,653
1986	\$7,805,019	816	\$9,565
1987	\$16,342,020	1,431	\$11,420
1988	\$0	0	\$0
1989	\$41,947	4	\$10,487
1990	\$355,922	35	\$10,169
1991	\$399,650	40	\$9,991
1992	\$210,000	21	\$10,000
1993 to 1998	Not Available	Not Available	Not Available
1999	\$2,553,684	132	\$19,293
2000	\$3,513,662	176	\$19,933
2001	\$7,709,748	285	\$27,057
2002	\$2,724,985	83	\$32,962
Total/Average	\$46,504,310	1,736	\$26,794

Sources: 1985-1992: Hamilton, Rabinovitz & Alschuler, Inc.; 1993-2002: Los Angeles Housing Department; Rent Stabilization Department; David Paul Rosen & Associates.

Table 12
Major Rehabilitation Program Activity
Applications Received, Processed and Denied/Withdrawn
City of Los Angeles
January 1, 1999 through July 31, 2002

Planning Commission Area/ Planning District/	Total Applic.		Processed		Denied/Withdrawn	
	No.	%	No.	%	No.	%
<u>East</u>						
Northeast LA	8	4%	4	3%	4	5%
Silver Lake - Echo Park	12	5%	6	5%	5	6%
Subtotal	20	9%	10	8%	9	10%
<u>Harbor</u>						
Harbor Gateway	0	0%	0	0%	0	0%
San Pedro	4	2%	2	2%	2	2%
Wilmington - Harbor City	0	0%	0	0%	0	0%
Subtotal	4	2%	2	2%	2	2%
Downtown	7	3%	6	5%	1	1%
Central City North	0	0%	0	0%	0	0%
Hollywood	24	11%	16	13%	8	9%
Westlake	7	3%	3	3%	4	5%
Wilshire	43	19%	27	23%	13	15%
Subtotal	81	36%	52	44%	26	30%
Arleta - Pacoima	0	0%	0	0%	0	0%
Chatsworth - Porter Ranch	0	0%	0	0%	0	0%
Granada Hills - Knollwood	0	0%	0	0%	0	0%
Mission Hills - Panorama City	2	1%	0	0%	2	2%
Northridge	0	0%	0	0%	0	0%
Sun Valley - La Tuna Canyon	0	0%	0	0%	0	0%
Sunland - Tujunga - Lakeview						
Terrace - Shadow Hills - E La Tuna Canyon	0	0%	0	0%	0	0%
Sylmar	0	0%	0	0%	0	0%
Subtotal	2	1%	0	0%	2	2%
Canoga Park - Winnetka - Woodland Hills - West Hills	0	0%	0	0%	0	0%
Encino - Tarzana	0	0%	0	0%	0	0%
North Hollywood - Valley Village	4	2%	2	2%	1	1%
Reseda - West Van Nuys	2	1%	0	0%	2	2%
Sherman Oaks - Studio City - Toluca Lake - Cahuenga	10	4%	7	6%	3	3%
Van Nuys - North Sherman Oaks	3	1%	1	1%	2	2%
Subtotal	19	8%	10	8%	8	9%
<u>South Los Angeles</u>						
South Central Los Angeles	7	3%	1	1%	6	7%
Southeast Los Angeles	4	2%	1	1%	3	3%
West Adams - Baldwin Hills - Leimert Park	16	7%	10	8%	6	7%
Subtotal	27	12%	12	10%	15	17%
<u>West Los Angeles</u>						
Bel Air - Beverly Crest	0	0%	0	0%	0	0%
Brentwood - Pacific Palisades	3	1%	1	1%	1	1%
Palms - Mar Vista - Del Rey	4	2%	1	1%	3	3%
Venice	38	17%	19	16%	9	10%
West Los Angeles	21	9%	10	8%	9	10%
Westchester - Playa Del Rey	2	1%	1	1%	1	1%
Westwood	3	1%	1	1%	2	2%
Subtotal	71	32%	33	28%	25	29%
TOTAL	224	100%	119	100%	87	100%

Source: Los Angeles Housing Department, Rent Stabilization; David Paul Rosen & Associates

Table 13
Major Rehabilitation Program Activity
Affected Housing Units and Rehabilitation Costs
City of Los Angeles
January 1, 1999 through July 31, 2002

Planning Commission Area/ Planning District/	TOTAL APPLICATIONS				PROCESSED APPLICATIONS					
	Total Units in Properties		Affected Units		Total Units in Properties		Affected Units		Ave. Rehab.	Ave. Primary
	No.	%	No.	%	No.	%	No.	%	Cost/Unit	Work/Unit
Northeast LA	34	2%	14	2%	18	2%	8	2%	\$16,917	\$16,542
Silver Lake - Echo Park	95	6%	32	5%	38	4%	11	3%	\$17,121	\$12,571
Subtotal	129	8%	46	7%	56	6%	19	5%		
Harbor Gateway	0	0%	0	0%	0	0%	0	0%		
San Pedro	23	1%	12	2%	14	2%	5	1%	\$13,900	\$10,638
Wilmington - Harbor City	0	0%	0	0%	0	0%	0	0%		
Subtotal	23	1%	12	2%	14	2%	5	1%		
Downtown	329	20%	139	22%	305	33%	120	32%	\$38,113	\$29,500
Central City North	0	0%	0	0%	0	0%	0	0%		
Hollywood	130	8%	39	6%	92	10%	26	7%	\$24,006	\$16,893
Westlake	69	4%	45	7%	50	5%	39	10%	\$34,085	\$22,539
Wilshire	189	12%	83	13%	115	12%	52	14%	\$26,482	\$16,473
Subtotal	717	45%	306	48%	562	60%	237	64%		
Arleta - Pacoima	0	0%	0	0%	0	0%	0	0%		
Chatsworth - Porter Ranch	0	0%	0	0%	0	0%	0	0%		
Granada Hills - Knollwood	0	0%	0	0%	0	0%	0	0%		
Mission Hills - Panorama City	8	0%	8	1%	0	0%	0	0%	\$27,628	\$9,209
Northridge	0	0%	0	0%	0	0%	0	0%		
Sun Valley - La Tuna Canyon	0	0%	0	0%	0	0%	0	0%		
Sunland - Tujunga - Lakeview Terrace - Shadow Hills - E La Tuna Canyon	0	0%	0	0%	0	0%	0	0%		
Sylmar	0	0%	0	0%	0	0%	0	0%		
Subtotal	8	0%	8	1%	0	0%	0	0%		
Canoga Park - Winnetka - Woodland Hills - West Hills	0	0%	0	0%	0	0%	0	0%		
Encino - Tarzana	0	0%	0	0%	0	0%	0	0%		
North Hollywood - Valley Village	36	2%	14	2%	28	3%	8	2%	\$34,393	\$22,058
Reseda - West Van Nuys	2	0%	2	0%	0	0%	0	0%	N/A	N/A
Sherman Oaks - Studio City - Toluca Lake - Cahuenga	63	4%	14	2%	46	5%	9	2%	\$26,485	\$18,429
Van Nuys - North Sherman Oaks	42	3%	26	4%	16	2%	9	2%	\$13,395	\$9,070
Subtotal	143	9%	56	9%	90	10%	26	7%		
South Central Los Angeles	28	2%	15	2%	4	0%	2	1%	\$28,341	\$8,886
Southeast Los Angeles	9	1%	7	1%	2	0%	1	0%	\$18,850	\$4,850
West Adams - Baldwin Hills - Leimert Park	56	3%	24	4%	33	4%	16	4%	\$17,066	\$11,390
Subtotal	93	6%	46	7%	39	4%	19	5%		
Bel Air - Beverly Crest	0	0%	0	0%	0	0%	0	0%		
Brentwood - Pacific Palisades	49	3%	22	3%	6	1%	1	0%	\$14,615	\$12,615
Palms - Mar Vista - Del Rey	19	1%	5	1%	4	0%	1	0%	N/A	N/A
Venice	196	12%	89	14%	120	13%	46	12%	\$40,864	\$27,667
West Los Angeles	93	6%	36	6%	34	4%	16	4%	\$29,590	\$13,279
Westchester - Playa Del Rey	125	8%	13	2%	2	0%	2	1%	\$31,080	\$13,770
Westwood	16	1%	3	0%	3	0%	1	0%	\$23,502	\$27,404
Subtotal	498	31%	168	26%	169	18%	67	18%		
TOTAL	1,611	100%	642	100%	930	100%	373	100%	\$26,794	\$17,311

Source: Los Angeles Housing Department, Rent Stabilization; David Paul Rosen & Associates

Table 14
Capital Improvement and Mandated Rehabilitation Case Summary
1985 through 2002

Year	# of Cases	Applied \$	Approved \$	Applied # of Units	Approved # of Units	Average Applied \$/unit	Approved Average \$/unit	Average Approved Increase/Mo
1985	2,504	N/A	\$17,215,503	N/A	26,486	N/A	\$650	N/A
1986	2,277	N/A	\$22,901,881	N/A	26,331	N/A	\$870	N/A
1987	2,065	N/A	\$33,397,195	N/A	29,895	N/A	\$1,117	N/A
1988	1,808	N/A	\$36,701,958	N/A	24,967	N/A	\$1,470	N/A
1989	2,731	N/A	\$42,936,476	N/A	32,666	N/A	\$1,314	N/A
1990	893	N/A	\$15,099,125	N/A	9,643	N/A	\$1,566	N/A
1991	616	N/A	\$11,777,056	N/A	5,570	N/A	\$2,114	N/A
1992	304	N/A	\$5,649,759	N/A	3,209	N/A	\$1,761	N/A
1993	204	\$3,353,728	\$1,651,937	2,471	1,247	\$1,357	\$1,325	\$ 13.44
1994	172	\$3,576,566	\$1,969,010	2,888	1,650	\$1,238	\$1,193	\$ 18.23
1995	183	\$7,976,155	\$5,854,615	7,517	2,483	\$1,061	\$2,358	\$ 37.10
1996	128	\$4,991,090	\$2,481,920	3,312	1,777	\$1,507	\$1,397	\$ 21.09
1997	116	\$2,061,363	\$1,053,012	1,982	1,050	\$1,040	\$1,003	\$ 26.56
1998	122	\$3,784,954	\$1,389,665	3,663	1,585	\$1,033	\$877	\$ 14.42
1999	206	\$5,910,875	\$1,896,128	3,644	2,658	\$1,622	\$713	\$ 14.83
2000	202	\$21,292,952	\$7,768,261	6,308	2,504	\$3,376	\$3,102	\$ 16.54
2001	234	\$13,243,748	\$4,784,603	6,966	3,828	\$1,901	\$1,250	\$ 14.46
2002	134	\$1,692,054	\$754,200	2,030	1,033	\$834	\$730	\$ 17.76
Total	14,899	\$67,883,484	\$215,282,304	40,781	178,582	\$1,497	\$1,206	\$ 19.44

Source: 1985-1992: Los Angeles Housing Department, RSD; Hamilton, Rabinovitz & Alschuler, Inc.
1993-2002: Los Angeles Housing Department; RSD; David Paul Rosen & Associates.

III. Provisions of Other Major Rehabilitation Programs

This section summarizes the thresholds of other major rehabilitation programs in California and examines the major rehabilitation provisions of selected cities with rent control programs.

A. Thresholds of Other Major Rehabilitation Programs

DRA compiled definitions of “major rehabilitation” from federal and State housing programs as a comparison to the Rent Stabilization Ordinance (RSO) definition of major rehabilitation. The definition of major rehabilitation in the RSO is as follows:

1. the total cost of rehabilitation work must be at least \$10,000 per unit;
2. primary work must be at least \$9,000 per unit; and,
3. the work must render the unit uninhabitable for at least 45 days.

All three standards must be satisfied to qualify work as major rehabilitation.

To assist the Rent Stabilization Board with assessing the RSO’s current definition of major rehabilitation, DRA reviewed definitions of rehabilitation used by major affordable housing subsidy programs. DRA reviewed definitions under the following programs:

- California Redevelopment Law;
- California Tax Credit Allocation Committee (low income housing tax credits);
- California Debt Limit Allocation Committee (tax-exempt bond allocations); and,
- Federal HOME program.

Table 15 summarizes the definitions of rehabilitation used by these programs.

Table 15
Definition of Rehabilitation
Major Affordable Housing Programs

Affordable Housing Program	Definition
California Redevelopment Law	"Substantial rehabilitation" means rehabilitation valued at least 25 percent of the after-rehabilitation value of the dwelling (including the value of land)
California Tax Credit Allocation Committee	At least \$7,500 hard construction costs per unit, excluding contractor profit and overhead (lower threshold for at-risk projects)
California Debt Limit Allocation Committee	At least \$7,500 hard construction costs per unit, excluding contractor profit and overhead (lower threshold for at-risk projects)
Federal HOME Program	At least \$1,000 per unit

California Redevelopment Law

California Redevelopment Law (CRL) uses a definition for “substantial” rehabilitation for housing production requirement purposes. In addition, CRL defines substantial rehabilitation in cases where units housing low and moderate income households are destroyed or removed from the low- and moderate-income housing market as part of a redevelopment project. In this instance, a redevelopment agency is obligated to replace these units.

The definition of “substantial rehabilitation” means rehabilitation valued at least 25 percent of the after-rehabilitation value of the dwelling (including the value of land).

California Tax Credit Allocation Committee

The California Tax Credit Allocation Committee (TCAC) adopted regulations implementing Federal and State Low Income Housing Tax Credit laws on June 19, 2002. These regulations state that:

Projects involving rehabilitation of existing buildings shall be required to complete a minimum of \$7,500 hard construction costs per unit (meaning, in this context, the amount of the construction contract excluding contractor profit and overhead) except for those projects defined as “at risk” pursuant to these regulations, which may spend the minimum amount required by Section 42 of the Internal Revenue Code.

California Debt Limit Allocation Committee

On May 31, 2002, the California Debt Limit Allocation Committee (CDLAC) adopted the procedures implementing the allocation of the State ceiling on qualified private activity bonds. These regulations incorporate the following definition for acquisition and rehabilitation projects:

Qualified Residential Rental Projects involving the rehabilitation of existing buildings, except for Federally Assisted at Risk Projects, must complete a minimum of \$7,500 in hard construction costs per unit. Hard construction costs means the amount of the construction contract not including contractor profit or overhead. A Federally Assisted at Risk Project may spend the minimum amount required by 26 U.S. C. Section 147(d)(2).

Federal HOME Regulations

The HOME program, administered by HUD, does not have a definition for substantial rehabilitation. Instead, the HOME program provides local jurisdictions with flexibility to design programs to fit their affordable housing needs. Therefore, the HOME program only sets a minimum threshold without regard to new construction or rehabilitation. The minimum amount of HOME funds that must be invested in a project involving rental housing or homeownership is \$1,000 per HOME-assisted units in the project.

Importantly, HOME funds can be used for a wide variety of affordable housing needs and is not restricted to new construction or major rehabilitation of affordable housing. For example, HOME funds can be used to fund downpayment assistance loans, which can be relatively small (under \$5,000) depending upon the conditions of the local housing market. Therefore, we do not believe that the minimum threshold set by the HOME program is an appropriate benchmark for the Rent Stabilization Board.

B. Requirements of Other Rent Control Programs

DRA reviewed rent control ordinances and regulations of the following cities:

- Santa Monica;
- San Francisco;
- West Hollywood;
- Berkeley;
- Oakland;
- San Jose; and,
- New York City

With some cities, DRA was able to interview City staff involved in the administration of the rent control ordinances. DRA interviewed staff from Berkeley, Santa Monica, and West Hollywood.

The purpose of the review is to determine:

- the definition of capital improvements in the cities' rent control ordinances;
- what circumstances, if any, are landlords allowed to increase rents because of capital improvements and/or major rehabilitation performed in their buildings;
- the methodology for calculating an increase in rent as a result of capital improvements and/or major rehabilitation expenses;
- what circumstances, if any, are landlords allowed to relocate a tenant – either temporarily or permanently – because of capital improvement and/or major rehabilitation work;
- whether tenants are provided any relocation benefits; and,
- whether tenants are allowed a first right of refusal to return to their units when the capital improvements and/or major rehabilitation are completed.

A summary chart is attached as **Chart 1**. Detailed case studies for each city are incorporated as **Appendix B**.

Chart 1

SURVEY OF CITIES WITH RENT STABILIZATION ORDINANCES

City	Definition of Capital Improvement	Calculating Pass-Through Rent Increase	Rent Increase Limits	Conditions For Tenant Displacement, Tenant First Right of Refusal	Relocation Benefits
<p>Santa Monica</p>	<p>The addition or replacement of a long-term improvement to a property. Expenses exceeding \$200 per unit generally considered capital improvements.</p>	<ul style="list-style-type: none"> • <u>Capital improvements affecting all units</u>: Landlords may increase NOI by 40% of the CPI. NOI equals rental income less operating expenses and the amortization of the costs of capital improvements. Mortgage expenses are not incorporated in NOI calculation. Santa Monica uses a list of capital improvements with amortization periods assigned to each capital improvement item. • <u>Capital improvements affecting a portion of the units</u>: the cost of capital improvement is amortized and added to the maximum allowable rent for the units that benefit from the capital improvement. 	<p>For low and moderate income tenants, rent increases are limited to the greater of:</p> <ul style="list-style-type: none"> • 12% of current rent; • two times the Employment Cost Index; or, • \$50 per month. <p>To qualify for rent increase limit, a tenant must demonstrate economic hardship due to proposed rent increase. Economic hardship is defined as:</p> <ul style="list-style-type: none"> • the tenant is a very low income senior or disabled; or, • the gross household income is 120% or lower of area median income and the household pays more than 30% of income toward housing costs. <p>A landlord can increase rents in subsequent years to make up for allowable rent increases that exceed these amounts.</p>	<p>Evictions due to renovations are not allowed with the following exceptions:</p> <ul style="list-style-type: none"> • substantial repairs are ordered by a government agency; • repairs cannot be completed with the tenant in the unit; • a government agency has determined that the work will take more than six months; or, • the unit is uninhabitable. <p>Tenants have the right to move back into a renovated apartment. Tenants pay the same rent they were paying before moving out, although landlords can petition for a rent increase based on the cost of capital improvements.</p>	<p>Landlords are required to provide a tenant with a comparable unit in a comparable area of the city. The tenant's rent payment to the landlord stays the same - the landlord is responsible for making up the rent differential, if any.</p>

City	Definition of Capital Improvement	Calculating Pass-Through Rent Increase	Rent Increase Limits	Conditions For Tenant Displacement, Tenant First Right of Refusal	Relocation Benefits
San Francisco	Improvements that materially add to the value of the property, appreciably prolong useful life, or adapt it to new uses, and which may be amortized over the useful life of the building. Capital improvements do not include normal routine maintenance and repair.	<p>For properties with six or more units, tenants can elect to have 50% or 100% of the amortized costs of capital improvements passed through. The tenant's election affects the rent increase limits (see next column).</p> <p>For properties with one to five units, 100% of the amortized cost of capital improvements may be passed through to the tenants.</p>	<p>For properties with six or more units, rent increases may not exceed 10% of a tenant's base rent or \$30.00, whichever is greater, if a tenant chooses to have 50% of capital improvement costs passed through. A landlord may accumulate any certified increase that exceeds this amount and impose the increase in subsequent years.</p> <p>If a tenant elects to have 100% of capital improvement costs passed through, the annual rent increase is limited to 5% of a tenant's base rent, with a total limit of 15%.</p> <p>For properties with one to five units, capital improvement rent increases are limited to 5% of the tenant's base rent or \$30.00, whichever is greater.</p>	<p>A landlord may relocate a tenant to carry out capital improvement work. A tenant cannot be required to vacate a unit for more than three months.</p> <p>A landlord cannot take possession of a unit if the tenant is:</p> <ul style="list-style-type: none"> • 60 years of age or older and has been in the unit for 10 years or more; • disabled and has been in the unit for 10 years or more ; or, • catastrophically ill and has been in the unit for 5 years or more. <p>Tenants have the right to reoccupy a unit at the prior rent.</p>	<p>A landlord must offer a comparable unit owned by the landlord, if vacant and available. If not, a non-comparable unit can be offered at the tenant's current rent, with adjustments allowed based upon condition, size, and other amenities of the replacement unit.</p> <p>Landlords must pay up to \$1,000 for actual moving and relocation expenses.</p>

City	Definition of Capital Improvement	Calculating Pass-Through Rent Increase	Rent Increase Limits	Conditions For Tenant Displacement, Tenant First Right of Refusal	Relocation Benefits
<p>West Hollywood</p>	<p>A list of capital improvements is incorporated in the regulations.</p> <p>A landlord must demonstrate that the capital expenditure was necessary or reasonable to maintain and/or improve the property and resulted in real benefit to the tenants of the property.</p>	<p>Landlords may increase NOI by 60% of CPI. Capital improvements are amortized according to a schedule in the regulations and then incorporated in the calculation of net operating income. Landlords can recover financing costs. If capital improvements are financed by the landlord, a financing cost of 5.5 percent interest is assumed.</p> <p>West Hollywood uses the NOI methodology when capital improvement costs are applied to all units. When a capital improvement is attributable to a specific unit, then the maximum allowable rent can increase by the cost of the capital improvement divided by the amortization period in years (and multiplied by 12 for a monthly rent increase amount).</p>	<p>Increases in tenant rent is limited to 12% the first 12 months after the increase is approved. In the second year, rent may be increased to the fully corrected rent and the landlord may receive interest on the delayed full increase in rents for the next 12 months.</p>	<p>Landlords may vacate a unit to repair or renovate it if:</p> <ul style="list-style-type: none"> • repairs were ordered by a governmental agency authorized to require compliance with existing codes; and, • the repairs cannot be completed with the tenant in the unit or the unit has been ordered demolished or removed from residential use; and, • the required work will take more than six months; or, • the unit must be eradicated or demolished because it is uninhabitable or not permitted. <p>Tenants have the right to move back into a unit. Tenants pay the same rent they were paying before moving out, although landlords can petition for a rent increase based on the cost of capital improvements.</p>	<ul style="list-style-type: none"> • If an agency redtags a unit or has ordered the unit vacated in less than 60 days, the landlord must pay for temporary housing at a hotel or other vacant apartment. • If an agency orders a unit vacated for longer than 6 months, a relocation fee is paid based on number of bedrooms: <ul style="list-style-type: none"> • Studio, \$2,000 • 1 BR, \$3,000 • 2 BR, \$4,300 • 3+ BR, \$4,700 <p>Seniors, persons with one or more minor, dependent children, disabled, or low-income persons receive a fee of \$5,000.</p> <p>With temporary relocation, a landlord must provide reasonable accommodations, and the tenant pays the same rent.</p>

City	Definition of Capital Improvement	Calculating Pass-Through Rent Increase	Rent Increase Limits	Conditions For Tenant Displacement, Tenant First Right of Refusal	Relocation Benefits
Berkeley	<p>A capital improvement is any improvement to a unit or property that:</p> <ul style="list-style-type: none"> materially adds to the value of the property; appreciably prolongs its useful life or adapts it to new use; has a useful life of more than one year; and/or, has a direct cost of \$200 or more per unit affected, or \$1,500 total, whichever is less. <p>A major repair covers substantially all or a structurally independent portion of a building:</p> <ul style="list-style-type: none"> a new roof a significant upgrade of the foundation a substantially new plumbing, electrical or heating system exterior painting or replacement of siding repairs reasonably related to correcting and/or preventing the spread of defects pest report. Repairs must exceed the lesser of \$6,000 or the \$1,000 times the number of units in the property. 	<p><u>Capital improvement</u>: monthly increase is equal to 1.042% of the cost of the improvement attributable to a unit.</p> <p><u>Major repairs</u>: monthly increase is equal to 0.927% of the cost of the major repair.</p>	<p>Rent increases may be no greater than \$25 for:</p> <ul style="list-style-type: none"> Tenants over 62 years whose household income does not exceed 30% of area median income or 150% of the total SSI payment (i.e. federal and state components), whichever is more. Tenants receiving general assistance, AFDC, SSI, or SSDI. 	<p>Landlords may displace tenants to improve their properties if the building permit department determines that a tenant cannot stay in the unit as the work occurs.</p> <p>A tenant has the right to return to the unit. The rent remains the same, with adjustments for the capital improvement or major repair allowable.</p> <p>The rent charged remains the same even if the original tenant does not return to the unit.</p>	<p>A tenant receives:</p> <ul style="list-style-type: none"> Initial storage and moving costs; and, Up to \$200 per month in rent differential. <p>Relocation benefits are limited to three months.</p>

City	Definition of Capital Improvement	Calculating Pass-Through Rent Increase	Rent Increase Limits	Conditions For Tenant Displacement, Tenant First Right of Refusal	Relocation Benefits
<p>Oakland</p>	<p>Capital improvements materially add to the value of the property and appreciably prolong useful life or adapt it to new building codes. Improvements must primarily benefit tenants. Eligible capital improvements also include:</p> <ul style="list-style-type: none"> • painting of the exterior of a building, and the complete interior painting of internal dwelling units. • equipment permanently fixed in place or relatively immobile. • Repairs completed in order to comply with Code. If repairs are considered Priority 1 or 2 conditions, then repairs may not be considered capital improvements. <p>A Priority 1 condition indicates major hazardous or uninhabitable conditions. A Priority 2 condition indicates major hazardous or inhabitable conditions that can be deferred through agreement with Code Enforcement.</p>	<p>Capital improvement expenses are amortized over five years.</p> <p>If capital improvements are financed with a loan (with a term that exceeds five years), the allowable increase in rent is the monthly loan payment divided by number of units.</p>	<p>No more than 12 months of capital improvement costs may be passed on to a tenant in any 12 month period.</p> <p>The rent increase justified by capital improvements shall be <u>reduced</u> from the allowable rent in the sixty-first month.</p>	<p>Tenant displacement is governed by the City's Just Cause for Eviction ordinance.</p> <p>An owner may seek temporary possession of a unit to undertake substantial repairs if the repairs cannot be completed while the unit is occupied and:</p> <ul style="list-style-type: none"> • repairs are necessary either to bring the property into compliance with applicable codes and laws affecting the health and safety of tenants; or, • repairs are necessary under an outstanding notice of code violations affecting the health and safety of tenants. <p>A tenant cannot be displaced for more than three months unless the owner receives permission from the Rent Board.</p> <p>Owners must offer displaced tenants the first right to return to the units at the same rents with rental agreements of substantially the same terms.</p>	<p>Tenant relocation benefits are regulated by the City's Code Enforcement Relocation Ordinance.</p> <p>If the displacement is for 60 days or longer, a tenant is entitled to a payment equal to twice the HUD Fair Market Rent figure for a unit of comparable size to the vacated unit, plus a payment of \$200.</p> <p>If the displacement is for less than 60 days, a tenant may recover their actual and reasonable moving expenses and the cost of temporary housing accommodations.</p> <p>If immediate displacement of the tenant is required (the tenant has less than 30 days notice to move), the tenant is entitled to an additional \$500 payment from the owner.</p>

City	Definition of Capital Improvement	Calculating Pass-Through Rent Increase	Rent Increase Limits	Conditions For Tenant Displacement, Tenant First Right of Refusal	Relocation Benefits
San Jose	<p>Capital improvements are improvements that:</p> <ul style="list-style-type: none"> materially add to the value of the property; appreciably prolong its useful life or adapt it to new uses; and, are required to be amortized over the useful life of the improvement of the building using the straight line depreciation provisions of the Internal Revenue Code. <p>Rehabilitation is defined as the costs of any rehabilitation or repair work done on or in a rental unit or common area to comply with an order issued by the San Jose Building Department, San Jose Director of Neighborhood Preservation, or the Fire Department, or to repair damage resulting from fire, earthquake, or other natural disaster.</p>	<p>Capital improvement costs are averaged on a per unit basis and amortized over at least 60 months. The amortization of costs can be added to rents, subject to an overall rent increase limit (see next column regarding rent increase limit).</p> <p>Rehabilitation expenses are averaged on a per unit basis and amortized over at least 36 months. The amortization of costs can be added to rents, subject to an overall rent increase limit (see next column regarding rent increase limit).</p> <p>Financing costs related to maintenance and upkeep of units is an allowable pass-through.</p>	<p>Generally, a monthly rent increase of up to five percent, plus proposed rent increases because of pass-through of costs of capital improvements, increased costs of maintenance and operation, and/or costs of rehabilitation, are allowable.</p> <p>A Hearing Officer can make the determination that a proposed increase imposes an unreasonably severe financial or economic hardship on a particular tenant, and is empowered to disallow the increase beyond eight percent of current rent. A tenant whose household income and monthly housing expense meet the criteria for the Section 8 program are deemed to be suffering under financial and economic hardship.</p>	<p>Property owners have two options for removing tenants from rent-controlled units through "no cause" notices to vacate. For tenants living in a rent-controlled unit one year or more, the owner may choose one of the following options to end a tenancy:</p> <ul style="list-style-type: none"> Issue a 90-day "no cause" notice in a slow market, or 120 days in a tight market (defined as a 3% vacancy rate or less); or, Issue a 60-day "no cause" notice with an offer to go to mediation/arbitration. <p>If a tenant can demonstrate certain hardships, such as living in the unit for three or more years, significant illness, or other factors, the tenant is eligible to have the move out date extended by an additional 60 days (for a total of 120 days).</p>	

City	Definition of Capital Improvement	Calculating Pass-Through Rent Increase	Rent Increase Limits	Conditions For Tenant Displacement, Tenant First Right of Refusal	Relocation Benefits
New York City	<p>Major capital improvements must meet all of these criteria:</p> <ul style="list-style-type: none"> depreciable under the Internal Revenue Code; is for the operation, preservation and maintenance of the structure; is an improvement that directly or indirectly benefits all tenants; and the item being replaced meets the requirements set forth in a useful life schedule incorporated in the regulations. 	<p>For major capital improvements, the increase in the rent may be up to 1/84th of the total cost (seven year amortization), with no allowance for interest expense. An increase is not allowed if government grants are used to finance the major capital improvements. Low interest rate loans are not considered grants.</p>	<p>An increase is not allowed during the term of a lease in effect, unless a specific provision in a lease authorizes an increase during its term.</p>	<p>An owner is allowed to displace a tenant if the owner will demolish his/her building or if the owner is required to eliminate inadequate, unsafe or unsanitary conditions and must demolish or rehabilitate the unit. In this instance, an owner is required to:</p> <ul style="list-style-type: none"> prove that it has a commitment for the required financing to demolish or rehabilitate the unit; prove that any rehabilitation requires the temporary removal of the tenant; and, agree to offer (and will offer) the tenant the right of first occupancy following any rehabilitation at an initial rent as determined by the applicable law. 	<p>An owner must pay all reasonable moving expenses and a reasonable stipend and/or relocate the tenant to a suitable housing accommodation at the same or lower rent in a closely proximate area. If no units are available at the same or lower rent, the owner may be required to pay the difference in rent between the tenant's current rent and the rent of the new unit for a period determined by the City.</p> <p>In cases of permanent relocation, an owner must pay:</p> <ul style="list-style-type: none"> reasonable moving expenses and a \$5,000 stipend if the tenant is relocated to unit at the same or lower rent in a closely proximate area; moving expenses if the tenant is relocated to a unit at a higher rent. The owner may also be required to pay a stipend equal to any difference in rent, multiplied by 72 months. <p>Alternatively, the landlord must pay the tenant a stipend that is the difference between the tenant's current rent and the amount from the demolition stipend chart, and multiplied by 72 months.</p>

1. Definition of Capital Improvements

Generally, the cities surveyed share a similar definition of capital improvements, where an improvement:

- materially adds to the value of a property;
- has a useful life of several years or more, and is fixed permanently in the building; and/or,
- benefits tenants and not just the landlord.

In addition, routine maintenance and repair are not considered capital improvements.

In two jurisdictions, Berkeley and Santa Monica, the definition of capital improvement incorporates a dollar amount. Berkeley's ordinance states that a capital improvement is an improvement with a direct cost of \$200 or more per unit, or \$1,500 total, whichever is less. Santa Monica's rent control regulations state that one consideration for defining an expense as a capital improvement is a cost of \$200 per unit.

New York's rent control regulations state that a capital improvement is for the operation, preservation, and maintenance of the structure of a building. New York also requires a landlord to demonstrate that the useful life of an item or equipment has expired. The ordinance incorporates a "Useful Life Schedule for Major Capital Improvements" that lists major capital improvements and their estimated life. If a landlord proposes to replace an item prior to the expiration of its useful life, as defined in the schedule, then the landlord must demonstrate that the item is beyond repair and must be replaced during its useful life. Typically, certification by an engineer or architect is required.

All cities incorporate in their regulations and/or ordinance a schedule of items that are considered eligible capital improvements.

Importantly, all ordinances exclude routine maintenance and repair from the definition of capital improvements. West Hollywood states that landlords cannot be compensated for neglecting necessary maintenance, and therefore establishes minimum standards of maintenance for units. Oakland states that repairs completed to remedy major hazardous conditions are not considered capital improvements. These major hazardous conditions are described in detail in Oakland's rent control regulations (and incorporated in the case study for the City of Oakland in **Appendix B**).

2. Permanent Increase in Rents Because of Capital Improvements

All cities surveyed allow landlords to increase rents to recover costs of capital improvements. The methodologies for calculating rent increases vary. Generally, methodologies fall under three categories:

- amortizing capital improvement costs;
- calculating net operating income; and,
- multiplying a fixed percentage to capital improvement costs.

a. Amortizing Capital Improvement Costs

Some cities surveyed calculate rent increases based on amortization of the costs of capital improvements. San Francisco, Oakland, San Jose, and New York use this method for calculating rent increases.

San Francisco and New York list the types of capital improvement expenditures landlords are allowed to pass through to tenants. With each category of capital improvement, an amortization period is assigned. For example, under San Francisco's current rent control regulations, a new foundation is assigned a 10-year amortization. Therefore, the verified costs of a new foundation are divided by 120 (10 years times 12 months per year) to calculate allowable monthly rent increases. Because all units benefit from the new foundation, the amortization of capital improvements is allocated among all units.

San Francisco also allows landlords to incorporate the cost of financing the capital improvements. If the landlord does not finance the cost of capital improvements, the City allows the landlord to incorporate an imputed interest expense. For capital improvements with 7-year amortizations, the allowable interest rate is 5.4 percent. For capital improvements with 10-year amortizations, the allowable interest rate is 5.0 percent.

In San Francisco, landlords are allowed to pass through either 50 percent or 100 percent of the costs of capital improvements on buildings of six or more units, depending upon the choice of the tenants. If tenants choose to a pass through of 50 percent of capital improvement costs, their annual rent increase is limited to 10 percent of base rent. If tenants choose a pass through of 100 percent of capital improvement costs, their annual rent increase is limited to five percent of base rent plus a total limit of 15 percent.

In San Jose, New York, and Oakland, all costs of capital improvements can be passed on to tenants, subject to some limitations (described in the attached reports for each city).

b. Net Operating Income Methodology

Two cities, West Hollywood and Santa Monica, employ a method for calculating rent increases based on the landlords' net operating income. Rather than simply factoring in the costs of capital improvements, West Hollywood and Santa Monica base rent increases on all factors that affect the net operating income of a landlord and allow rent increases based on a fair rate of return to a landlord. These cities believe it is reasonable to review the cost of capital improvements along with other costs, such as changes in property taxes and utility expenses, when determining rent increases.

Santa Monica allows landlords to increase their net operating income by 40 percent of the Consumer Price Index. Net operating income is determined by calculating rental income less operating expenses and the amortization of the costs of capital improvements. Mortgage expenses are not incorporated in this calculation to avoid any issues regarding refinancing. Similar to other cities such as New York and San Francisco, Santa Monica uses an extensive list of capital improvements with amortization periods assigned to each capital improvement item. For example, if a landlord installs new cabinetry, the cost of the cabinets is divided by 120 because the city has assigned a ten year amortization period to cabinets. This amortization of costs is then added to other eligible operating expenses in the calculation of net operating income.

Similarly, West Hollywood allows landlords to increase their net operating income by a percentage of the Consumer Price Index. West Hollywood allows landlords to increase net operating income by 60 percent of the Consumer Price Index for the year. West Hollywood also uses an extensive list of eligible capital improvements and an accompanying amortization schedule for each item as one part of the calculation of net operating income. West Hollywood allows recovery of actual financing costs incurred by the landlord. Financing costs of capital improvements are an allowable expense in the calculation of net operating income. If the landlord self-finances the capital improvements, then an imputed interest rate of 5.5 percent per year is allowed.

Both West Hollywood and Santa Monica use the net operating income methodology when capital improvement costs should be applied to all rental units in a property. However, when a capital improvement is attributable to a specific unit, then the maximum allowable rent can increase by the cost of the capital improvement divided by the amortization period in years (and divided by 12 to arrive at a monthly rent increase amount).

c. Fixed Percentage of Capital Improvement Costs

One city, Berkeley, calculates allowable rent increases based on a percentage of capital improvement costs.

Berkeley allows permanent increases in rents based on a maximum of 1.042 percent of the cost of a capital improvement or 0.927 percent of the cost of a major long-term repair. Major long-term repairs are generally repairs that benefit all units, such as a new roof or new plumbing for all (or substantially all) units in a building. Previously, Berkeley employed a net operating income methodology for calculating rent increases based on capital improvement expenditures. However, with the passage of Costa Hawkins, which effectively eliminates controls on the rents of vacant units (due to legal evictions or voluntary move-outs by tenants), Berkeley believes that landlords now have an additional method for recovering costs of capital expenditures. Because of Costa Hawkins, turnover in a building will affect a landlord's ability to increase net operating income and recover costs of capital improvements. Rent increases based on a net operating income methodology cannot take into account potential increases in net operating income due to future turnover.

To address this issue, Berkeley decided to conduct an analysis of changes in net operating income of rental buildings in the city. Using this analysis and looking at typical turnover rates, increases in net operating income, and typical capital improvement expenditures, City staff calculated that a permanent rent increase based on 1.042 percent of the cost of capital improvement expenditures provides landlords with the ability to recover costs. With major long-term repairs, the factor is 0.927 percent of the cost of the repair.

This methodology is simple to use because the 1.042 percent factor (or 0.927 percent in the case of major long-term repairs) is applied to an actual capital improvement expenditure, and then applied to a rent increase.

3. Limitations on Rent Increases

All cities limit the amount rents can increase, even if a capital improvement cost may justify a higher rent increase.

a. Rent Limit for Special Populations

Some cities, such as Santa Monica, San Jose, and Berkeley, limit rent increases for special populations. For example, Santa Monica limits rent increases to low and moderate income tenants to the greater of:

- 12 percent of current rent;
- two times the Employment Cost Index; or,
- \$50 per month.

A tenant, however, must demonstrate that he/she is experiencing economic hardship because of a proposed rent increase. Economic hardship is defined as:

- the tenant is a very low income senior or disabled; or,
- the gross household income is 120 percent or lower of area median income and the household pays more than 30 percent of income toward housing costs.

A landlord can increase rents in subsequent years to make up for any justifiable rent increase.

In Berkeley, rent increases cannot exceed more than \$25 if the tenant is over 62 and whose income is at or below 30 percent of the Oakland PMSA median income, or 150 percent of the total SSI payment. In addition, any tenant receiving general assistance, AFDC payments, or SSI/SSDI payments qualifies under this limit on rent increases.

San Jose allows hearing officers to take into account economic hardship when determining allowable rent increases. A tenant whose household income and monthly housing expense meet the criteria for the Section 8 program are deemed to be suffering from economic hardship.

b. General Rent Increase Limits

Some cities, such as San Francisco, West Hollywood, and Oakland, limit rent increases for all tenants.

San Francisco limits rent increases to five or ten percent of the tenant's rent or \$30, whichever is greater. The amount of the increase depends upon the size of the property and the amount of capital improvement cost passed through to tenants. A landlord can raise rents in subsequent years to make up for a certified increase that exceeds these amounts.

West Hollywood limits rent increases to 12 percent in the first year after the rent increase is approved. In the second year, the full rent increase is allowed, with interest on the delayed full increase in rent.

In Oakland, no more than 12 months of capital improvement costs can be passed on to a tenant in a 12-month period. In other words, landlords cannot combine costs of capital improvements from separate years and pass through these costs to tenants in one year.

4. Tenant Relocation

Under certain circumstances, all cities allow landlords to relocate tenants to conduct major capital improvement or rehabilitation work.

Generally, conditions for allowing tenant displacement are restrictive. In summary, most cities allow tenant displacement under the following circumstances:

- substantial repairs are ordered by a government agency, i.e. code compliance;
- the unit must be demolished because it is uninhabitable; and/or,
- a government agency has determined that the work cannot be completed unless the tenant is relocated.

In most cases, a landlord is required to find a replacement unit and/or provide relocation benefits for a displaced tenant.

Santa Monica and West Hollywood do not require payment of temporary relocation costs. However, landlords are required to provide a tenant with a comparable unit in a comparable area of the city. In addition, the tenant's rent payment to the landlord stays the same. The landlord is responsible for making up the rent differential, if any.

In West Hollywood's case, if a tenant must be relocated permanently (because the unit must be vacated for more than six months or demolished), then a relocation payment must be paid to the tenant. The payment ranges from \$2,000 to \$4,700, depending upon the number of bedrooms of the unit the tenant is currently occupying. Tenants who are seniors, handicapped, low income (at or below 80 percent of area median income), or who have one more minor, dependent children, receive a \$5,000 relocation payment.

In San Francisco, landlords must pay a tenant \$1,000 for moving and relocation expenses. A landlord cannot relocate a tenant unless a comparable unit owned by the landlord is available. A landlord may offer a non-comparable unit, with an adjustment to the rent based on condition, size, and other amenities of the unit.

A tenant cannot be required to vacate a unit for more than three months. In addition, landlords cannot relocate tenants who are:

- 60 years of age or older and has been residing in the unit for 10 years or more;
- disabled and has been residing in the unit for 10 years or more (a person who is disabled or blind as determined by SSI/SSP to qualify for that program); or,
- catastrophically ill and has been residing in the unit for five years or more (suffering from a life threatening illness as certified by a primary care physician).

Berkeley requires landlords to pay tenants' initial storage and moving costs, and up to \$200 per month in rent differential. These relocation benefits are limited to three months.

5. Tenant First Right of Refusal

Most cities require a landlord to provide a tenant displaced from a unit because of capital improvement work with a first right of refusal to return to his/her original unit. There is no vacancy decontrol for these tenants. In other words, the rent charged to the tenant remains the same, with adjustments based on the capital improvement costs.

In some cases, cities do not allow for vacancy decontrol even when a tenant decides not to move back into his/her apartment after capital improvement work is completed. For example, Berkeley keeps rent controls in place whether or not an original tenant moves back after completion of capital improvement work. West Hollywood employs the same practice. These cities do not allow vacancy decontrol under these circumstances to eliminate landlords' financial incentive to remove tenants.

IV. Economic Analysis

A. Cost Escalation of Threshold Requirements

The current dollar thresholds used to define “major rehabilitation” were last adjusted by the City Council in 1982. Because of increases in inflation over the past 20 years, it is appropriate to consider adjusting the dollar thresholds to reflect costs in 2002.

DRA compiled historical cost increases as defined under three different indexes:

- Consumer Price Index;
- RS Means Construction Cost Estimates; and,
- Engineering News-Record Construction Cost Index.

DRA obtained data on the Consumer Price Index (CPI) for the period 1982 through 2001 for the Los Angeles County-Orange County-Riverside County region. **Table 16** shows the increase in the regional CPI, using a base of \$1 for 1982.

RS Means is a leading firm providing construction cost estimates. RS Means provides regional construction cost estimates on residential and commercial buildings. Table 2 summarizes increases in RS Means’ construction cost estimates for Los Angeles for the period 1982 through 2001, assuming a base of \$1 for 1982.

The Engineering News-Record provides construction cost indexes based on a 20-city average of costs. Therefore, the figures provided in **Table 16** are based on a 20-city average and are not regionally adjusted for Los Angeles. These figures summarize increases in the Engineering News-Record Construction Cost Index for the period 1982 through 2001, assuming a base of \$1 for 1982.

Table 17 summarizes calculations of the current RSO thresholds adjusted for historical increases in these indexes.

Table 16

**Cumulative Increase in Consumer Price Index, RS Means Construction Cost Estimates,
Engineering News-Record Construction Cost Index
1982-2001**

Year	Cumulative Increase in CPI	Cumulative Increase in RS Means Construction Cost Estimates	Cumulative Increase in Engineering News- Record Construction Cost Index
1982	Base Year	Base Year	Base Year
1983	+ \$0.02	+ \$0.11	+ \$0.06
1984	+ \$0.06	+ \$0.14	+ \$0.08
1985	+ \$0.11	+ \$0.17	+ \$0.10
1986	+ \$0.15	+ \$0.21	+ \$0.12
1987	+ \$0.20	+ \$0.24	+ \$0.15
1988	+ \$0.25	+ \$0.27	+ \$0.18
1989	+ \$0.32	+ \$0.30	+ \$0.21
1990	+ \$0.40	+ \$0.33	+ \$0.24
1991	+ \$0.45	+ \$0.37	+ \$0.26
1992	+\$0.51	+ \$0.41	+ \$0.30
1993	+ \$0.54	+ \$0.43	+ \$0.36
1994	+ \$0.57	+ \$0.47	+ \$0.41
1995	+ \$0.59	+ \$0.49	+ \$0.43
1996	+ \$0.62	+ \$0.51	+ \$0.47
1997	+ \$0.64	+ \$0.54	+ \$0.52
1998	+ \$0.67	+ \$0.56	+ \$0.55
1999	+\$0.71	+ \$0.59	+ \$0.58
2000	+ \$0.76	+ \$0.61	+ \$0.63
2001	+ \$0.82	+ \$0.63	+ \$0.66

(1) Base Year = 1982, \$1.00

Table 17

**Calculations of RSO Thresholds for Major Rehabilitation,
Based on Increases in Consumer Price Index, RS Means Construction Cost Estimates,
Engineering News-Record Construction Cost Index
1982-2001**

RSO Major Rehabilitation Threshold	Thresholds Based on Increase in CPI	Thresholds Based on Increase in RS Means Construction Cost Estimates	Thresholds Based on Increase in Engineering News-Record Construction Cost Index
Total Rehabilitation Work Threshold: \$10,000/unit	\$18,222	\$16,329	\$16,580
Primary Work Threshold: \$9,000/unit	\$16,400	\$14,696	\$14,922

B. Relocation Benefits

Table 18 compares the average rents of rent-stabilized and non-stabilized properties in the City of Los Angeles, based on market data provided by REALFACTS for September, 2002. Except for studio units, average per square foot rents for non-stabilized properties are 11 to 23 percent higher than for comparable stabilized properties.

Table 19 estimates temporary relocation benefits based on the difference in average rents for non-stabilized units and stabilized units for studio, one-bedroom and two-bedroom two bath units. Temporary relocation benefits are estimated for 45-day and 3-month periods. On an average basis, monthly rent differentials are relatively small, therefore temporary relocation benefits for three months are estimated at only \$135 for studio units, \$402 for one-bedroom units and \$369 for two-bedroom/two-bath units.¹

For tenants who have been in their units for a long-time and are therefore paying much lower than average rents, the costs associated with temporary relocation benefits will be much higher. Based on the assumptions in **Table 18** for long-term tenants, temporary relocation costs for three months are estimated to range from \$1,700 for studio units to \$3,300 for two-bedroom/two-bath units.

C. Cost Recovery through Rent Increases

As noted earlier, it is generally recognized by housing policy analysts that the regulation of residential rents may create financial disincentives for owners to invest in maintenance and capital improvements of their units. The primary way to incent owners to invest in their properties is to allow rent increases associated with rehabilitation work.

1. Capitalization Rate Approach

DRA analyzed the relationship between rent increases and landlord investment based on the approach used by multifamily lenders and investors. While each landlord will have its own investment objectives, many or most property owners will borrow funds for major rehabilitation of their properties. Typically, this will involve a construction loan during the rehabilitation, followed by refinancing of the first mortgage to a higher amount upon completion. Lenders and investors will determine the amount they will lend based on, among other things, the increase in property value associated with the rehabilitation. This increase in value is calculated using a capitalization rate approach. The “capitalization rate” is the ratio of net operating income to project fair market value, or sales price, exhibited in the market and reflects the rate of return required by investors in rental property.

¹ REALFACTS data show large differences in average rents for two-bedroom/one bath and three bedroom/two bath units. However, two bedroom/one bath and three bedroom units only comprise 3.5 percent and 3.6 percent of the units in the REALFACTS database, respectively. Given the small sample size, the rent differentials for these unit sizes are considered less reliable than for studio, one-bedroom and two-bedroom/two-bath units, which comprise the majority of units in the REALFACTS data.

Table 18
RENT STABILIZATION ORDINANCE MAJOR REHABILITATION PROGRAM
COMPARISON OF RENTS
RENT-STABILIZED AND NON-RENT STABILIZED PROPERTIES
September, 2002

AVERAGE UNIT SIZE (SQUARE FEET)

	<u>Non-Rent Stab.</u>	<u>Rent Stabilized</u>	<u>Difference</u>	<u>% Differ.</u>
Studio	498	472	26	5.2%
1 BR/1 BA	726	745	-19	-2.6%
2 BR/1 BA	960	847	113	11.8%
2 BR/2 BA	1,068	1,121	-53	-5.0%
3 BR/2 BA	1,502	1,709	-207	-13.8%

AVERAGE MONTHLY RENT

	<u>Non-Rent Stab.</u>	<u>Rent Stabilized</u>	<u>Difference</u>	<u>% Differ.</u>
Studio	\$975	\$930	\$45	4.6%
1 BR/1 BA	\$1,319	\$1,185	\$134	10.2%
2 BR/1 BA	\$1,883	\$1,275	\$608	32.3%
2 BR/2 BA	\$1,816	\$1,693	\$123	6.8%
3 BR/2 BA	\$3,350	\$2,591	\$759	22.7%

AVERAGE MONTHLY RENT PER SQUARE FOOT

	<u>Non-Rent Stab.</u>	<u>Rent Stabilized</u>	<u>Difference</u>	<u>% Differ.</u>
Studio	\$1.96	\$1.97	-\$0.01	-0.6%
1 BR/1 BA	\$1.82	\$1.59	\$0.23	12.5%
2 BR/1 BA	\$1.96	\$1.51	\$0.46	23.3%
2 BR/2 BA	\$1.70	\$1.51	\$0.19	11.2%
3 BR/2 BA	\$2.23	\$1.52	\$0.71	32.0%

Source: RealFacts city-wide averages for September, 2002; David Paul Rosen & Associates

Table 19
RENT STABILIZATION ORDINANCE MAJOR REHABILITATION PROGRAM
ESTIMATED RELOCATION BENEFITS

**ESTIMATED AVERAGE RELOCATION BENEFITS BASED ON DIFFERENCE IN AVERAGE RENTS
BETWEEN RENT-STABILIZED AND NON-RENT STABILIZED PROPERTIES**

	2002 Market Rents			Temporary Relocation Benefits for:	
	<u>Non-Rent Stab.</u>	<u>Rent Stabilized</u>	<u>Difference</u>	<u>45 Days</u>	<u>3 Months</u>
	Studio	\$975	\$930	\$45	\$68
1 BR/1 BA	\$1,319	\$1,185	\$134	\$201	\$402
2 BR/2 BA	\$1,816	\$1,693	\$123	\$185	\$369

ESTIMATED RELOCATION BENEFITS FOR LONG-TERM TENANTS

	2002	Assumed	<u>Difference</u>	Temporary Relocation Benefits for:	
	Market Rent	Rent of Long-		<u>45 Days</u>	<u>3 Months</u>
	<u>Non-Rent Stab.</u>	<u>Time Tenant</u>			
Studio	\$975	\$400	\$575	\$863	\$1,725
1 BR/1 BA	\$1,319	\$500	\$819	\$1,229	\$2,457
2 BR/2 BA	\$1,816	\$700	\$1,116	\$1,674	\$3,348

Source: RealFacts city-wide averages for September, 2002; David Paul Rosen & Associates

Applying this approach, the increased operating income (rent increase) is capitalized at an assumed capitalization rate percent (based on recent property sales comparables) to determine the increased value of the developed property associated with an assumed rent increase. Alternatively, multiplying the capitalization rate by an assumed dollar investment generates the rent increase required by investors.

Cap rates move in the opposite direction to sales prices. Cap rates drop in “hot” real estate markets as prices rise faster than project net operating income. Alternatively, cap rates rise when prices fall in market and economic downturns. DRA reviewed data on capitalization, or “cap” rates for Los Angeles County Apartments provided by the Richard S. Ziman Center for Real Estate at the Anderson School of UCLA at the Fourth Annual Multifamily Housing Forecast Conference held on September 18, 2002. According to these data, capitalization rates in Los Angeles County over the past decade ranged from 7 percent to nearly 11 percent. From 1999 to 2001, cap rates remained in the 9 percent range. In 2002, capitalization rates have hovered around 8 percent.

Table 20 calculates the rent increase required to support the investment at assumed levels of rehabilitation cost per unit, using the capitalization rate approach.

Table 21 estimates the financially supportable investment using the capitalization rate approach, assuming rent increases are limited to 10 percent of the existing rents.

2. Alternative Approaches to Calculating Allowable Rent Increases

As described in Section III of this report, the cities with rent control programs that DRA surveyed used variations of three basic methodologies in calculating allowable rent increases associated with capital improvements:

- amortizing capital improvement costs;
- calculating net operating income; and,
- multiplying a fixed percentage to capital improvement costs.

Cities differ in the amortization periods used to amortize capital improvement costs. Oakland uses a five-year amortization period for all capital improvements, except if the capital improvements are financed with a loan with a term greater than five years. In the latter case, the allowable increases equals the monthly loan payment divided by the number of units that benefit from the capital improvement. DRA considers five years an unreasonably short amortization period for major rehabilitation primary work items.

San Francisco uses a ten-year amortization period for the improvements considered primary work in the RSO. New York City amortizes costs using a detailed list of the estimated life of different capital improvements, which range from ten to 35 years. Santa Monica’s amortization schedule for capital improvements ranges from five to 20 years.

Table 20
RENT STABILIZATION ORDINANCE MAJOR REHABILITATION PROGRAM
RENT INCREASES BASED ON COSTS OF PRIMARY REHABILITATION WORK
AND TEMPORARY RELOCATION BENEFITS
CAPITALIZATION RATE APPROACH

Total Eligible Costs (1)	Annual Rent Increases based on a Capitalization Rate of: (2)			
	7.50%	8.00%	8.50%	9.00%
\$9,000	\$56	\$60	\$64	\$68
\$12,000	\$75	\$80	\$85	\$90
\$15,000	\$94	\$100	\$106	\$113
\$20,000	\$125	\$133	\$142	\$150
\$21,000	\$131	\$140	\$149	\$158
\$25,000	\$156	\$167	\$177	\$188

(1) Eligible costs are assumed to include temporary relocation costs plus primary rehabilitation work.

(2) Equals capitalization rate multiplied by total eligible costs divided by 12 months.

Source: David Paul Rosen & Associates

Table 21
RENT STABILIZATION ORDINANCE MAJOR REHABILITATION PROGRAM
ESTIMATED SUPPORTABLE INVESTMENT WITH 10 PERCENT RENT INCREASE
CAPITALIZATION RATE APPROACH

Unit Bedroom/ Bath Count	Assumed Current Rent	Maximum Rent Increase @ 10%	Capitalized Value of Rent Increases Based on a Capitalization Rate of:				Estimated Monthly Rent Increase During Relocation (1)	Estimated Relocation Costs (3 Months)	Moving Allowance	Supportable Rehabilitation Cost at Cap. Rate of (2) 8.50%
			7.50%	8.00%	8.50%	9.00%				
Average Market Rent, Non-Stabilized Units										
Studio	\$975	\$97.50	\$15,600	\$14,625	\$13,765	\$13,000	\$45	\$135	\$400	\$13,230
1 BR/1 BA	\$1,319	\$131.90	\$21,104	\$19,785	\$18,621	\$17,587	\$134	\$402	\$400	\$17,819
2 BR/2 BA	\$1,816	\$181.60	\$29,056	\$27,240	\$25,638	\$24,213	\$123	\$369	\$400	\$24,869
Estimated Rent, Long-Term Tenants										
Studio	\$400	\$40.00	\$6,400	\$6,000	\$5,647	\$5,333	\$575	\$1,725	\$400	\$3,522
1 BR/1 BA	\$500	\$50.00	\$8,000	\$7,500	\$7,059	\$6,667	\$819	\$2,457	\$400	\$4,202
2 BR/2 BA	\$700	\$70.00	\$11,200	\$10,500	\$9,882	\$9,333	\$1,116	\$3,348	\$400	\$6,134

(1) Equals difference between assumed current rent and average rent for non-stabilized units from REALFACTS.

(2) Equals capitalized value of rent increase at 8.5% capitalization rate less 3 months relocation cost and moving expenses.

Source: David Paul Rosen & Associates

Cities also vary in their treatment of interest costs. New York permits no interest costs to be passed on in rent increases. San Francisco permits landlords a reasonable rate of interest, limited to no more than ten percent. If the landlord does not prove actual interest, an imputed interest rate of 5.0 percent is allowed on items with a 10-year amortization, based on the average of the twelve most recent monthly rates for ten-year Treasury Securities. Oakland permits actual interest paid on loans used to finance improvements, as described above. DRA recommends allowing interest at an indexed rate, at a spread of 1 to 2 percent above 10-year Treasuries, to provide a reasonable return to landlords.

Two cities surveyed, West Hollywood and Santa Monica, permit increases in net operating income, at 40 percent and 60 percent of the CPI, respectively, in addition to amortized improvement and financing costs. DRA does not recommend employing a net operating income approach, as it raises a number of issues and problems. The first problem is defining net operating income. West Hollywood and Santa Monica do not include replacement reserves in the definition of net operating income, but this encourages property owners to defer property maintenance. Even if replacement reserve deposits were included in the definition of net operating income, the City has no control or assurance that these funds will be used for the property.

Another problem with the net operating income approach is that LAHD staff would have to rely on financial information from owners or require an audited financial statement. Most RSO buildings are small buildings under twelve units. Many are owned by unsophisticated “mom and pop” property owners. Small buildings may not merit the expense of an audit. An additional problem is the LAHD staff time and experience required to analyze developer net operating income projections.

Table 22 compares rent increases calculated under the capitalization and amortization approaches at different levels of eligible (rehabilitation and relocation) costs. Under the amortization approach, rent increases are calculated at amortization periods of 15, 20 and 25 years assuming interest at 5.0 percent and 6.0 percent, representing spreads of approximately 1 and 2 points, respectively, above the current 10-year Treasury rate.

Assuming an amortization period of 20 years and an interest rate of 6.0 percent, the amortization approach yields similar monthly rent increases to the capitalization approach using an 8.5 percent cap rate. At 5.0 percent interest and a 20-year amortization, the calculated rent increases from the amortization approach are similar to those under the capitalization approach using about an 8.0 percent cap rate.

Table 22
RENT STABILIZATION ORDINANCE MAJOR REHABILITATION PROGRAM
COMPARISON OF RENT INCREASES UNDER
CAPITALIZATION AND AMORTIZATION APPROACHES

Total Eligible Costs (1)	Annual Rent Increases based on a Capitalization Rate of: (2)				Annual Rent Increase Based on Amortization Plus Interest at 6.0 Percent (3)				Annual Rent Increase Based on Amortization Plus Interest at 5.0 Percent (3)			
	7.50%	8.00%	8.50%	9.00%	10 Yr	15 Yr	20 Yr	25 Yr	10 Yr	15 Yr	20 Yr	25 Yr
\$9,000	\$56	\$60	\$64	\$68	\$100	\$76	\$64	\$58	\$95	\$71	\$59	\$53
\$12,000	\$75	\$80	\$85	\$90	\$133	\$101	\$86	\$77	\$127	\$95	\$79	\$70
\$15,000	\$94	\$100	\$106	\$113	\$167	\$127	\$107	\$97	\$159	\$119	\$99	\$88
\$20,000	\$125	\$133	\$142	\$150	\$222	\$169	\$143	\$129	\$212	\$158	\$132	\$117
\$21,000	\$131	\$140	\$149	\$158	\$233	\$177	\$150	\$135	\$223	\$166	\$139	\$123
\$25,000	\$156	\$167	\$177	\$188	\$278	\$211	\$179	\$161	\$265	\$198	\$165	\$146

(1) Eligible costs are assumed to include temporary relocation costs plus primary rehabilitation work.

(2) Equals capitalization rate multiplied by total eligible costs divided by 12 months.

(3) Equals monthly payment required to amortize eligible costs over stated amortization period with stated interest rate.

The 5.0% and 6.0% rates represent spreads of approximately 1% and 2%, respectively, over the current 10-year Treasury rate (February, 2003).

Source: David Paul Rosen & Associates

V. Policy Options and Recommendations

A. Policy Options

DRA held meetings and teleconferences with landlord and tenant stakeholder representatives to hear concerns with the existing provisions of the major rehabilitation program and solicit input on DRA's draft recommendations.

Table 23 presents a matrix of key policy issues and options for the major rehabilitation program. The matrix presents current and proposed program provisions, landlord concerns and tenant concerns for each issue, based on our interviews with tenant and landlord representatives and the results of DRA's economic analysis.

DRA's recommendations (detailed below) are intended to balance the interests of tenants in maintaining affordable rents with incentives for landlords to invest in their property to maintain the condition of the housing stock, consistent with the intent of the RSO. DRA's key recommendations include the use of temporary relocation and rent increases to allow cost-recovery of primary rehabilitation work only. By eliminating the ability of landlords to use the major rehabilitation program to evict tenants and by limiting rent increases to cost recovery for primary rehabilitation work, DRA believes the proposed revisions to the major rehabilitation program will eliminate incentives for speculators to use the program to reposition properties to the luxury rental market in areas of high or rapidly increasing rents. A cap on each unit's rent increase equal to 10 percent of the pre-major rehabilitation rent is proposed to limit the impact on tenants, although DRA acknowledges that this cap will serve to limit investment in the properties. We believe that demolition of RSO buildings located in high rent market areas of the City, as allowed under the Ellis Act, may accelerate with these restrictions on major rehabilitation evictions and rent increases.

Rent increases will be averaged across properties. Rents on some units may be close to market, while others for long-term tenants may be much lower. The Census data on tenure suggest that, given the high rate of turnover, a large number of tenants in rent-stabilized units are paying rents close to market. This is supported by the relatively modest differences in the average rent for rent-stabilized and non-stabilized units. However, in some buildings with a preponderance of long-term tenants, the 10 percent rent increase may have the perverse effect of limiting investment to a level below the current threshold.

Table 23
RENT STABILIZATION MAJOR REHABILITATION PROGRAM
POLICY OPTIONS

Program Element	Tenant Concerns/ Recommendations	Landlord Concerns/ Recommendations	Policy Options
<p>1. Dollar Cost Threshold Requirements</p> <ul style="list-style-type: none"> • \$10,000 total cost • \$9,000 primary work • Unit must be rendered uninhabitable for 45 days or more 	<ul style="list-style-type: none"> • Program does not define basis for what renders the units uninhabitable for a period of not less than 45 calendar days; City basically accepts landlord’s claim 	<ul style="list-style-type: none"> • A dollar cost threshold is not necessarily related to the need for tenant to be relocated during rehabilitation work; e.g. if asbestos and lead are involved laws require that tenants must be moved • It is more appropriate to use a per SF dollar threshold to account for variation in unit size 	<ul style="list-style-type: none"> a. Maintain current thresholds b. Escalate cost thresholds based on CPI to: <ul style="list-style-type: none"> • \$18,000 total cost • \$16,000 primary work c. Eliminate or reduce threshold if asbestos, lead hazards exceed established standards

Table 23
RENT STABILIZATION MAJOR REHABILITATION PROGRAM
POLICY OPTIONS

Program Element	Tenant Concerns/ Recommendations	Landlord Concerns/ Recommendations	Policy Options
<p>2. <i>Proposed New Element:</i> Cost recovery through permanent rent increase</p>	<ul style="list-style-type: none"> • Landlords use major rehabilitation evictions to reposition inventory to luxury housing and raise rents 	<ul style="list-style-type: none"> • Lack of ability to pass through costs creates disincentive for landlord investment leading to degradation of existing housing stock and/or demolition of existing buildings 	<ul style="list-style-type: none"> a. 100% cost pass-through b. 100% cost pass-through on primary work only c. Cost pass-through with caps or limits on dollar amount and time
<p>3. Relocation benefits: \$5,000 for qualified tenants (62 years or older, households with minors); \$2,000 otherwise</p>	<ul style="list-style-type: none"> • Current benefits are insufficient for tenants to afford replacement housing • Voluntary vacancies should be disallowed within a certain time period before and after landlord applies for major rehabilitation evictions to prevent constructive evictions 	<ul style="list-style-type: none"> • If prior tenants are given first preference to return, landlords should be allowed to screen out “bad” tenants 	<ul style="list-style-type: none"> a. Increase permanent relocation benefit b. Temporary relocation with cost eligible for rent increase c. Temporary relocation with cost not eligible for rent increase

Table 23
RENT STABILIZATION MAJOR REHABILITATION PROGRAM
POLICY OPTIONS

Program Element	Tenant Concerns and Recommendations	Landlord Concerns/ Recommendations	Policy Options
<p>4. 25% of units must be rented at prior rent level if 4 or more units are rehabilitated within two years</p>	<ul style="list-style-type: none"> • Landlords rehabilitate three units at a time to avoid set-aside requirements • All tenants should be allowed to return at pre-eviction rents 	<ul style="list-style-type: none"> • Lack of ability to pass through costs creates disincentive for landlord investment leading to degradation of existing housing stock and/or demolition of existing buildings 	<p>a. Apply set-aside to total units in project (at same or different percentage)</p>

B. Recommendations

The following recommended changes to the major rehabilitation program are based on a combination of economic data analysis, case studies of other cities with rent stabilization rehabilitation provisions, and a consensus approach with the Advisory Committee that seeks to balance competing interests with the Advisory Committee. These recommendations are supported by consensus of the Advisory Committee as a fair compromise among competing interests. They represent a middle ground that is limited on both ends of the spectrum of preserving affordability for low income tenants and stimulating investment in rent-stabilized properties.

Within the context of the Rent Stabilization Ordinance, the goals of the major rehabilitation program should be to: (1) to encourage needed investment in the rent-stabilized housing stock without allowing speculation and gentrification; and (2) to protect in-place tenants from excessive rent increases and unnecessary eviction. To better meet these goals, the Advisory Committee recommends the following changes and additions to the major rehabilitation program:

Recommendation #1: No eviction of in-place tenants for rehabilitation work. Tenants do not relinquish their "lease" on rehabilitated units that must be vacated for repairs. Tenants may be temporarily relocated so repairs may be completed. However, all tenants have the right to return to their unit. Vacating the unit is no longer mandatory to qualify for major rehabilitation.

Anecdotal evidence, supported by the geographic distribution of major rehabilitation applications, suggests that landlords may have employed, or attempted to employ, the major rehabilitation provisions of the RSO to improperly evict long-term, low-rent paying tenants and reposition their markets as high-rent buildings through high-end renovations. This is not consistent with the goals of the RSO. Prohibiting evictions will remove landlords' incentives to use, or threaten to use, the major rehabilitation program in this manner.

The geographic distribution of major rehabilitation applications in the last several years indicates they are in higher rent areas of the City where market pressures to reposition properties as high-rent buildings are strong. Of the 373 affected units in major rehabilitation applications processed between 1999 and July 31, 2002, 32 percent (120 units) were in the downtown area. Another 32 percent (117 units) were in the Wilshire, Westlake and Hollywood areas. The other largest concentrations of major rehabilitation units were in Venice (12 percent, 46 units) and West Los Angeles (4 percent, 16 units).

Recommendation #2: Temporary relocation with the right to return for all relocated tenants. A landlord must provide for the relocation of tenants, including costs for two moves, in a comparable unit and comparable area of the City. Prior to receiving a building permit, landlords must provide an acceptable means and methods plan for

relocating affected tenants. For relocations under 30 days, or for longer periods with the tenant's consent, the landlord can put up a tenant in a hotel plus pay for food costs.

Temporary relocation is needed at times for the safety of in-place tenants, such as when asbestos or other safety hazards exist or the scope of the primary work is extensive.

The rent stabilization provisions of all of the other cities surveyed provide for temporary relocation in certain circumstances, specifically when substantial repairs are ordered by a government agency and/or a government agency has determined that the work cannot be completed unless the tenant is relocated. In Santa Monica, West Hollywood, and San Francisco, landlords are required to provide comparable units in a comparable area of the city or to make up any rent differential. In San Francisco, a tenant cannot be required to vacate a unit for more than three months and landlords must pay each tenant \$1,000 for moving and relocation expenses.

Recommendation #3: Either LAHD/RSD staff or a third party LAHD/RSD contractor to certify new rents upon tenants' return. The new rent must be certified by LAHD or its contractor prior to issuance of final inspection on building permit. LAHD/RSD will make the Final Determination as to whether tenants must vacate the unit for the rehabilitation work to proceed. LAHD/RSD will support a landlord's effort to enforce a determination that a unit must be vacated in order to perform the work in the event of tenant non-compliance after a reasonable notice has been given. Failure by landlords to pay for relocation costs, certify new rents, or comply with allowed rent increases will result in penalties, fines, and/or liens.

Landlords have not been applying for re-rental certificates as required under the major rehabilitation program, and to document their compliance with the 25 percent set-aside requirement at former rent levels. Increased monitoring and enforcement provisions are required to ensure that landlords comply with the recommended new provisions.

Recommendation #4: Permanent relocation for cases who cannot be expected to move twice. (The amount of permanent relocation benefits should be evaluated in the context of the entire RSO). Tenants entitled to permanent relocation benefits would be limited to designated cases, similar to those recommended in San Francisco: tenants over the age of 62 who have been in their unit for 10 years; tenants who are disabled and have been in their unit for 10 years; tenants who suffer from a severe illness and have been in their unit for at least 5 years.

Recommendation #5: Increases in the floor rents for investment in “primary work” items, plus temporary and/or permanent relocation costs, calculated by amortizing the dollar amount of construction and relocation costs plus compound interest at an indexed rate. Determine an amortization schedule and finance index by regulation. Monthly dollar rent increases should be capped at 10 percent of current tenant rent. Only one 10 percent rent increase is allowed per tenancy, except for items that have reached the end of their amortized life per the schedule published by regulation. The 10 percent cap applies to primary work items that must be repaired or replaced again. Increases to be applied at rate of 5 percent of pre-rehabilitation rent upon re-occupancy, and 5 percent of pre-rehabilitation rent on next rent anniversary date. Annual rent adjustments apply per current RSO in addition to these “pass through” rent increases.

The 10 percent cap on the rent increase represents the best compromise solution that could be agreed upon by the Advisory Committee. Landlord representatives prefer a higher rent cap or no cap to encourage rehabilitation of the housing stock. Tenant representatives prefer a lower rent cap or no rent increase at all to preserve affordability for lower income tenants.

The major rehabilitation rent increase remains in force permanently in the event the unit is not vacated by the tenant last occupying the unit pre-rehabilitation. After three years, the unit rent is subject to decontrol upon the next vacancy.

DRA analyzed the permitted rent increases and supportable investment under a capitalization rate approach, which models investment under financial underwriting standards, and an amortization approach used by several cities surveyed, including San Francisco, Oakland, San Jose and New York. DRA determined that these approaches can provide a reasonable return to landlords on their investment. The amortization approach was determined to be easier to understand and to implement. An amortization period of 20 years and an interest rate equal to the ten-year Treasury rate plus a one-percent spread was determined to be equivalent to a 9 percent cap rate.

DRA also analyzed the net operating income approach used in Santa Monica and West Hollywood which allows increases in net operating income on top of the amortized costs of improvements to be passed through in the form of rent increases.

The proposed 10 percent cap on rent increases and the two-year phase-in resulted from the consensus building approach used with the Advisory Group. The cap will effectively limit the dollar investment in rehabilitation and relocation to the amount of investment financially supported by the permitted rent increase.

Recommendation #6: Failure for a landlord to pay all of the temporary or permanent relocation benefits required, or failure of the landlord to certify a proper new rent, will subject the landlord to a lien filed by the City equivalent in seniority to a tax lien, and subject the owner to fines and penalties as specified in the RSO.

As noted above, landlords have not been applying for re-rental certificates as required under the major rehabilitation program, and to document their compliance with the 25 percent set-aside requirement at former rent levels. Increased monitoring and enforcement provisions are required to ensure that landlords comply with the recommended new provisions.

Recommendation #7: Eliminate current thresholds for primary work as defined by the major rehabilitation program.

The 10 percent cap on rent increases will create a limit on the amount investors will be willing to invest, therefore increasing the thresholds will reduce the “window” of investment. Since evictions will be prohibited and permitted rent increases will be tied to the costs of rehabilitation work and relocation costs, the thresholds for the major rehabilitation are no longer considered necessary. The goal of removing the thresholds is to incent lower cost primary work to help extend the useful life of rent-stabilized buildings.

Recommendation #8: Review and revision, as needed, of the primary work definition in the RSO to ensure that it effectively limits allowed improvements to those required to extend useful life of the building, and prohibit those that would reposition the building to a higher rent market.

Continue current RSO policy prohibiting landlords from passing through rent increases for costs to correct code violations, except for changes to the building code per current RSO. Continue current City policy of aggressive code enforcement through the Systematic Code Enforcement Program (SCEP) and Rent Escrow Account Program (REAP). Landlords who allow their properties to fall into continued disrepair, as determined by the REAP program or some other standard, must repair their buildings to defined standards with no rent increase allowed. Disallowing landlords to pass through rent increases for code violations will discourage landlords from deferring maintenance and allowing buildings to deteriorate.

**Appendix B:
Case Study Provisions for
Major Rehabilitation**

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SANTA MONICA RENT CONTROL CHARTER AMENDMENT

Information Coordinator: Joe Jaurequi, (310) 458-8751

A. Definition of Capital Improvements

A capital improvement is the addition or replacement of a long-term betterment to the property. Factors to consider in determining whether an expense is a capital improvement include:

- the nature and extent of the work performed;
- the amount of the expense, with expenses exceeding \$200 per benefited unit generally considered a capital improvement; and,
- the likelihood that the expense will recur annually.

Capital improvement expenses with a total cost of less than \$200 per benefited unit may be considered as a repair to be expensed in one year, at the discretion of a hearing examiner or of the Rent Board.

B. Calculating Rent Increases Based on Amortization of Cost of Capital Improvements and Net Operating Income

Rent increases are allowed based on the net operating income of the building. In summary, when rent control was established in 1979, landlords registered their units with the City. Apartment buildings constructed after 1979 are not subject to the rent control ordinance. As part of their registration, landlords were required to disclose their net operating income (not incorporating mortgage costs). The rent control ordinance allows landlords to increase their NOI by 40 percent of CPI annually to allow the landlords a fair rate of return on their developments. NOI is determined by calculating rental income, less operating expenses and less the amortization of the cost of renovation.

The ordinance incorporates the following definitions:

- net operating income equals gross income less operating expenses.
- gross income equals rental income at 100% paid occupancy, laundry income, cleaning fees or services, garage and parking fees, plus all other income or consideration received or receivable for or in connection with the use or occupancy of rental units and housing services, less uncollected rents due to vacancy and bad debts.

- operating expenses shall include the following:
 - property taxes;
 - utility expenses;
 - insurance; and,
 - management expenses (contracted or owner performed).

Mortgages are not incorporated in the calculation of NOI, so any refinancing by the owner does not affect the calculation of NOI. Therefore, there is no need to certify that the refinancing is for capital improvements to the building only.

For capital improvements that only affect a portion of the units, the cost of a capital improvement is permanently added to the maximum allowable monthly rent according to the following formula:

cost of capital improvement, divided by the amortization period, divided by 12.

The amortization schedule for improvements ranges from 5 to 20 years, depending on the type of improvements. For example, most appliances have an amortization period of 5 years, while expenses related to foundation work have an amortization period of 20 years. The complete amortization schedule appears at the end of this report.

The increase in the maximum allowable rent based on the amortization of major capital improvement costs does not decrease upon expiration of the amortization periods.

Rent increases are allocated as follows:

- rent increases for unit-specific capital improvements are allocated to that unit;
- rent increases for building-wide or common area capital improvements are allocated equally among all units;
- rent increases resulting from the NOI analysis are allocated equally among all units.

C. Limitations on Rent Increases

Santa Monica limits the amount of rent increases to low and moderate income tenants. In summary, no annual increase can exceed the greater of:

- 12 percent of current rent;
- 2 times the Employment Cost Index; or,
- \$50 per month.

The tenant, however, must demonstrate economic hardship. Economic hardship is defined as:

- the tenant is a very low income senior or disabled; or,
- the gross household income is 120 percent or lower of area median income and the household pays more than 30 percent of income toward housing costs.

A landlord can increase rents in subsequent years to make up for any justifiable rent that is subject to these limitations.

D. Tenant Eviction and Relocation

Evictions due to renovations are not allowed in Santa Monica, with the following exceptions:

- substantial repairs are ordered by a government agency (code compliance);
- repairs cannot be completed with the tenant in the unit;
- a government agency has determined that the work will take more than 6 months; or,
- the unit must be eradicated or demolished because it is uninhabitable.

If a landlord chooses to conduct renovations, and the tenant must be relocated for longer than 30 days, the landlord must provide for the relocation of the tenant in a comparable unit and comparable area of the City. These are judgment calls based more on the good faith efforts of the landlord. For relocations under 30 days, the landlord can put up a tenant in a hotel and also pay for food costs. Santa Monica is very strict regarding tenant relocation. Prior to receiving a building permit, the landlord must provide an acceptable means and methods plan that details his/her plan for relocating tenants.

The tenant has the right to move back into the renovated apartment. Initially, the tenant pays the same rent they were paying before moving out. However, the landlord can petition for a rent increase.

E. Amortization Schedule for Capital Improvements

<u>Improvement</u>	<u>Years</u>	<u>Improvement</u>	<u>Years</u>
Air Conditioners	10	Fire Alarm System	10
Appliances		Fire Sprinkler System.....	20
Refrigerator.....	5	Fire Escape	10
Stove.....	5	Flooring/Floor Covering	
Garbage Disposal	5	Hardwood	10
Water Heater	5	Tile and Linoleum	5
Dishwasher	5	Carpet	5
Microwave Oven.....	5	Carpet Pad.....	5
Washer/Dryer	5	Subfloor.....	10
Fans	5	Fumigation: Tenting	5
Cabinets.....	10	Furniture	5
Carpentry	10	Automatic Garage Door Openers	10
Counters	10	Gates	
Doors.....	10	Chain Link.....	10
Knobs.....	5	Wrought Iron	10
Screen Doors.....	5	Wood.....	10
Earthquake Expenses		Glass	
Architectural & Engineering Fees	5	Windows.....	5
Emergency Services		Doors	5
Clean-up.....	5	Mirrors	5
Fencing and Security	5	Heating	
Management.....	5	Central	10
Tenant Assistance.....	5	Gas	10
Structural Repair and Retrofitting		Electric	10
Foundation Repair	10	Solar.....	10
Foundation Replacement.....	20	Insulation	10
Foundation Bolting	20	Landscaping	
Iron or Steel Work.....	20	Planting.....	10
Masonry-Chimney Repair.....	20	Sprinklers.....	10
Shear Wall Installation	10	Tree Replacement	10
Electrical Wiring.....	10	Lighting	
Elevator.....	20	Interior	10
Fencing		Exterior.....	10
Chain.....	10	Locks	5
Block	10	Mailboxes.....	10
Wood.....	10	Meters.....	10

<u>Improvement</u>	<u>Years</u>
Plumbing	
Fixtures	10
Pipe Replacement	10
Re-Pipe Entire Building	20
Shower Doors.....	5
Painting	
Interior	5
Exterior.....	5
Paving	
Asphalt.....	10
Cement	10
Decking	10
Plastering	10
Pumps: Sump	10
Railings.....	10
Roofing	
Shingle/Asphalt.....	10
Built-up, Tar and Gravel.....	10
Tile	10
Gutters/Downspouts.....	10

<u>Improvement</u>	<u>Years</u>
Security	
Entry Telephone Intercom.....	10
Gates/Doors.....	10
Fencing	10
Alarms.....	10
Sidewalks/Walkways.....	10
Stairs	10
Stucco.....	10
Tilework.....	10
Wallpaper	5
Window Coverings	
Drapes.....	5
Shades.....	5
Screens.....	5
Awnings	5
Blinds/Miniblinds	5
Shutters	5

SAN FRANCISCO

RENT STABILIZATION and ARBITRATION ORDINANCE

A. Proposition H

In November of 2000, San Francisco voters passed Proposition H. Proposition H would not allow landlords to permanently increase rents because of capital improvement costs. Landlords immediately filed a lawsuit — Case No. 316-928 entitled Quigg v. City and County of San Francisco, et al. — to prevent implementation of Proposition H. The court ruled Proposition H unconstitutional and ordered the parties to negotiate a compromise.

In February 2003, the rent control ordinance will reflect the terms of the compromise. This report reflects these terms.

B. Definition of Capital Improvements and Substantial Rehabilitation

Capital improvements are defined as those improvements that materially add to the value of the property, appreciably prolong its useful life, or adapt it to new uses, and which may be amortized over the useful life of the improvement of the building. Capital improvements do not include normal routine maintenance and repair.

Repairs incidental to a capital improvement project, or replacement of an item normally considered a capital improvement, are also defined as capital improvements. Capital improvements otherwise eligible are not eligible if the landlord charges a use fee (such as coin-operated washers and dryers).

Substantial rehabilitation means the renovation, alteration or remodeling of a building with uninhabitable residential rental units of 50 or more years of age and requiring substantial renovation to conform to contemporary standards for decent, safe and sanitary housing. Cosmetic improvements alone such as painting, decorating and minor repairs, or other work which can be performed without having the units vacated, do not qualify as substantial rehabilitation. Improvements will not be deemed substantial unless the cost of the work for which the landlord has not been compensated by insurance proceeds equals or exceeds 75 percent of the cost of newly constructed residential buildings of the same number of units and type of construction, excluding land costs and architectural/engineering fees. The determination of this estimated cost is based on construction cost data reported by Marshall and Swift and Valuation Engineers. Landlords are required to deposit with the Rent Board an amount that covers the cost of hiring an estimator in case an estimator is needed to arrive at construction cost estimates.

C. Calculation of Rent Increases Due to Capital Improvements or Substantial Rehabilitation

Generally, allowable rent increases due to capital improvement or substantial rehabilitation costs vary according to the number of units in a property. The allowable rent increase is based on the straight-line amortization of the costs of capital improvements or substantial rehabilitation, with all or a portion of these amortized costs passed through to tenants.

With regard to apportioning costs, the most reasonable method that takes into account the extent to which each unit benefits from the improvements or work is used. Methods that may be appropriate, depending on the circumstances, include allocation based on the square footage in each unit, the rent paid for each unit, and equal division among all units. When improvements do not benefit all units, only those units that benefit may be charged the additional rent. Costs attributable to routine repair and maintenance are considered part of the costs of operating and maintenance.

1. Properties with 6 Units or More

For properties with 6 units or greater, only 50 percent of the amortized cost of capital improvements may be passed through to the tenants. However, 100 percent of the cost of capital improvements related to seismic work and energy conservation may be passed through to tenants. The costs of energy conservation work must be approved by the Commission on the Environment (currently, a new EPA EnergyStar-compliant refrigerator is the only item approved for certification).

Alternatively, a tenant may elect to have 100 percent of the certified capital improvement or substantial rehabilitation costs passed through to the tenant, with an annual rent increase limitation of 5 percent and a total limitation of 15 percent of the tenant's base rent.

2. Properties with 1 to 5 Units

For properties with 1 to 5 units, 100 percent of the amortized cost of capital improvements may be passed through to the tenants.

3. Amortization Schedules

The City uses an amortization schedule to determine allowable rent increases due to capital improvements or substantial rehabilitation. The following is the amortization schedule for developments with 6 units or more.

7-Year Amortization Schedule

- appliances (such as new stoves, disposals, refrigerators, washers, dryers and dishwashers);

- fixtures (such as garage door openers, locks, light fixtures, water heaters and blankets, shower heads, time clocks and hot water pumps; and,
- other improvements (such as carpeting, linoleum, and exterior and interior painting of common areas).

If the appliance is a replacement for which the tenant has already had the benefit, the cost will not be amortized as a capital improvement, but will be considered part of operating and maintenance expenses. Appliances may be amortized as capital improvements when part of a remodeled kitchen; based upon an agreement between the tenant and landlord; and/or a new service or appliance the tenant did not previously have.

10-Year Amortization Schedule

- Major improvements to the structure of the building such as:
 - new foundation;
 - new floor structure;
 - new ceiling or walls – new sheetrock;
 - new plumbing (new fixtures, or piping);
 - weather-stripping, ceiling insulation, seals and caulking;
 - new furnaces and heaters;
 - new wiring;
 - new stairs;
 - new roof structure – new roof cover;
 - new windows;
 - fire escapes, central smoke detection system;
 - new wood or tile floor cover;
 - new partitioning sprinkler;
 - boiler replacement;
 - air conditioning – central system;
 - exterior siding or stucco;
 - elevators;
 - additions such as patios or decks;
 - central security system;
 - new doors;
 - new mail boxes;
 - new kitchen cabinets; and,
 - sinks.

20-Year Amortization Schedule

- Seismic work.

4. Financing Costs

A landlord is entitled to a reasonable rate of interest for financing improvements or rehabilitation. Interest is limited to no more than 10 percent. Interest is amortized over a period equal to the amortization period of the improvement.

The landlord has the burden of proof to establish the actual rate of interest. In cases where the landlord does not incur or prove any actual interest expense on funds used for capital improvements or rehabilitation work, the landlord is entitled to an allowance of imputed interest. The imputed interest rate for capital improvement petitions for the period March 1, 2002 through February 28, 2003 is:

- 7-year amortizations: 5.4%
- 10-year amortizations: 5.0%

The 7-year rate is the average of the 12 most recent monthly rates for 7-year Treasury Securities. The 10-year rate is the average of the 12 most recent monthly rates for 10-year Treasury Securities.

D. Rent Increase Limits

For properties with 6 or more units, rent increases may not exceed 10 percent of a tenant's base rent or \$30, whichever is greater. A landlord may accumulate any certified increase that exceeds this amount and impose the increase in subsequent years.

For properties with 1 to 5 units, capital improvement rent increases are limited to 5 percent of the tenant's base rent or \$30, whichever is greater.

E. Tenant Relocation

A landlord is allowed to temporarily remove a unit from housing use to carry out capital improvements or rehabilitation work. Any tenant who vacates the unit under such circumstances has the right to reoccupy the unit at the prior rent. The tenant will vacate the unit only for the minimum time required to complete the work. A tenant cannot be required to vacate a unit in excess of 3 months.

A landlord may not recover possession of a unit if a comparable unit owned by the landlord is vacant and available. If a non-comparable unit becomes available before the recovery of possession, the landlord must offer that unit to the tenant at a rent based on the rent that the tenant is paying, with upward or downward adjustments allowed based upon the condition, size, and other amenities of the replacement unit.

A landlord cannot recover possession of a unit from a tenant in the rental unit if the tenant is:

- 60 years of age or older and has been residing in the unit for 10 years or more;
- disabled and has been residing in the unit for 10 years or more (a person who is disabled or blind within the meaning of SSI/SSP and who is determined by SSI/SSP to qualify for that program); or,
- catastrophically ill and has been residing in the unit for 5 years or more (disabled as defined above and suffering from a life threatening illness as certified by his or her primary care physician).

Landlords must pay a tenant actual costs up to \$1,000 for moving and relocation expenses. These moving and relocation expenses include, but are not limited to, the following expenses reasonably related to the tenant's move from, as well as back to, the unit following completion of capital improvement or rehabilitation work by the landlord:

- transportation of persons and property to and from the unit from which the tenant is displaced, and packing, crating, unpacking and uncrating personal property;
- storage of personal property as necessary in connection with relocation;
- insurance of personal property while in storage or transit;
- reasonable replacement value of property lost, stolen, or damaged (through no fault or negligence of the tenant) in the process of moving;
- the cost of disconnecting, dismantling, removing, reassembling, reconnecting and reinstalling personal property, including connection charges imposed by public utilities for starting utility service; and,
- the difference in rent for the period of displacement calculated by subtracting the monthly rent paid by the tenant for the unit from which the tenant is being displaced from the monthly rent to be paid by the tenant in the unit to which he or she is moving.

WEST HOLLYWOOD RENT STABILIZATION ORDINANCE

Legal Services Officer: Ralph Winter, (323) 848-6450

A. Definition of Major Capital Improvements

The West Hollywood Rent Stabilization Ordinance incorporates a list of items that qualify as major capital improvements. This list is shown in the next section.

A landlord must demonstrate that the capital expenditure was necessary or reasonable to maintain and/or improve the property and resulted in real benefit to the tenants of the property as opposed to merely increasing the value of the property to the benefit of the landlord without commensurate benefit to the tenants.

B. Maximum Allowable Rent Increases

In general, if a rent-stabilized unit becomes vacant, a landlord can set the rent at whatever amount prospective tenants are willing to pay. The rent initially charged the new tenant by the landlord establishes the Maximum Allowable Rent (MAR) for the tenancy. The housing services supplied by the landlord as a basis for the MAR are also established at this time by what is in the lease or what is provided in the unit at or after move-in.

Under the West Hollywood Rent Stabilization Ordinance, landlords are assured that the net operating income from their property may increase at 60 percent of the percentage increase in the Consumer Price Index over time. If this has not been the case between the base year (1983 generally) and the current year, the landlord may apply to adjust the Maximum Allowable Rents on a property. In calculating the net operating income for the property, landlords may include both incurred and planned costs from repairs or capital expenditures that diminish the operating income of the property. Costs of building improvements, major repairs, replacement and maintenance, except those costs compensated through insurance proceeds, are amortized.

The following is a list of major capital improvements and their amortization schedule:

<u>Improvement</u>	<u>Years</u>	<u>Improvement</u>	<u>Years</u>
Air Conditioner.....	10	Heating	10
Appliances (other than those listed)	7	Insulation	10
Cabinets.....	10	Landscaping	10
Carpentry	10	Locks	7
Carpeting	7	Painting (interior)	4
Dishwasher	7	Painting (exterior).....	7
Doors.....	10	Paving.....	10
Dryer	7	Plastering	10
Electric Wiring.....	15	Plumbing.....	10
Elevator.....	20	Pumps.....	10
Fan	10	Refrigerator.....	10
Fencing.....	10	Roofing	10
Fire Alarm System.....	10	Security Entry Telephone Intercom.....	10
Fire Escape.....	10	Smoke Detector	5
Floor Covering (linoleum or vinyl)	7	Stove.....	10
Flooring	7	Stucco.....	10
Furniture	7	Washing Machine.....	7
Garbage Disposal	7	Water Heater	7
Gates	10	Window Coverings	7
Gutters.....	10		

Capital improvement costs attributable to specific units are added to the maximum allowable monthly rent applicable to a given rental unit according to the following formula:

cost of capital improvement apportioned to the rental unit, divided by
amortization period, divided by 12.

Reasonable costs incurred in financing capital expenditures are added to the Maximum Allowable Rent for a given rental unit according to the following formula:

cost of financing of the capital expenditure apportioned to the rental unit,
divided by the greater of the:

- amortization period of the expenditure; or,
- actual length of financing (in years) divided by 12.

In the event that the costs of an allowable capital expenditure are financed by an individual or entity affiliated with the landlord, by the landlord, or otherwise arranged through other than arm's-length negotiation, recovery of financing costs through a rent increase is equal to an interest rate of 5.5 percent per year.

C. Maintenance Standards

To insure that West Hollywood's rental housing stock remains in good condition, and that landlords do not compensate for rent regulation by neglecting necessary maintenance, landlords are required to comply with certain maintenance standards. Landlords must:

- maintain both common areas and individual units in compliance with existing property maintenance, fire, health, and building safety codes;
- replace carpets, linoleum/vinyl and window coverings provided by the landlord in the rental unit and common areas every 7 years;
- paint rental units and interior common areas every 4 years;
- paint exterior common areas every 7 years; and,
- maintain all provided appliances in good working condition.

This maintenance must be completed unless the landlord can demonstrate that the work is not necessary. Maintenance work is considered necessary when paint is discolored, faded, cracked or peeling; or when carpet or draperies are torn, worn, faded, or badly stained.

D. Rent Increase Limits

If an increase is granted for the MAR of each or certain units, the increase in the tenant's rent is limited to 12 percent the first 12 months after the MAR increase is approved. In the second year, the rent may be increased to the fully corrected MAR and the landlord may receive interest on the delayed full increase in rents for the next 12 months. This interest is removed from the unit's MAR after the 12 months end.

E. Tenant Relocations Permitted by the Ordinance

There are limited reasons for which a tenant may be relocated from a unit without being at fault. One reason is that the landlord needs to conduct substantial repairs ordered by an authorized government agency to bring the property into compliance with applicable codes and laws affecting the health and safety of these tenants, and the agency has ordered that this work cannot be completed while the tenant occupies the premises. Generally, however, landlords may not relocate tenants simply in order to rehabilitate or remodel a rental unit. Major remodeling or rehabilitation projects that require a vacant unit would need to wait until the unit is voluntarily vacated. Landlords may only force a tenant to vacate a unit in order to repair or renovate it if:

- repairs were ordered by Building and Safety, Health Department, Fire Department or other authorized governmental agency to comply with existing codes; and,

- the repairs cannot be completed with the tenant in the unit or the unit has been ordered demolished or removed from residential use; and,
- the required work will take more than 6 months; and,
- the landlord has obtained all permits required to do the work from the City of West Hollywood and the County of Los Angeles; or,
- the unit must be eradicated or demolished because it is uninhabitable or not permitted and the landlord has obtained any required demolition permits.

When the unit is rented after completion of capital improvement work, the former tenant has the right to move back into the unit. The rent for the unit will not be decontrolled during vacancy following a no-fault termination of a tenancy. The landlord will only be able to ask for the current MAR or less from the next tenant following such a termination. Therefore, the landlord does not have a financial incentive to remove the tenant.

In cases of temporary relocation, a tenant pays the same rent to the landlord, while the landlord is obligated to provide reasonable accommodations for the tenant. In many cases, an in-house mediator at Rent Stabilization works with the landlord and tenant to determine reasonableness of accommodations.

In cases where a government agency orders a unit vacated for longer than 6 months, a relocation fee must be paid. The landlord must provide the tenant with a 60-day notice. The 60-day noticing period has not begun until the landlord pays the tenant the appropriate relocation fee. If the unit was red-tagged or otherwise vacated by an authorized agency in less than 60 days, the landlord's responsibility to pay reasonable costs for hotel or other vacant apartment does not end until the relocation fees have been paid.

When a government agency orders a unit vacated for a period longer than 6 months, the relocation fee is determined by the size of the unit from a tenant is being displaced. The fee is as follows:

Size of the unit, by number of bedroom:

- Studio \$2,000
- 1 Bedroom..... \$3,000
- 2 Bedrooms \$4,300
- 3 or more Bedrooms \$4,700

For tenants who are seniors, persons with whom one or more minor, dependent children reside, handicapped, or low-income persons as defined by Health and Safety Code Section 50079.5 (approximately 80 percent of area median income, adjusted for household size), the relocation fee is \$5,000. Seniors are persons 62 years or older. "Disabled tenant" is defined in the Ordinance as a person who has a physical or mental impairment that

substantially limits one or more major life activities, and who identifies himself or herself as disabled.

Once the work has been performed, the landlord must offer the relocated tenant the right of first refusal to move back into the unit. Only if the tenant refuses the offer can the unit be rented to someone else.

The rent remains at the Maximum Allowable Rent that existed when the tenant was relocated plus any general adjustments that became available while the unit was not rented. When the owner gives a notice to change the terms of tenancy by terminating it, the unit is not decontrolled during vacancy. Therefore, if the relocated tenant chooses not to move back into the unit, the landlord must charge the MAR plus general adjustment to the new tenant who moves in when the work is completed.

If the work ordered by a government agency will take less than 6 months or to fumigate for termites or other pests or vermin (if such fumigation cannot be completed while the unit is occupied), the landlord may take temporary repossession of the unit. To do so, the landlord must pay for reasonable costs for temporary housing in a hotel or a vacant apartment.

CITY of BERKELEY'S RENT STABILIZATION and EVICTION for GOOD CAUSE PROGRAM

Contact: Tom Brougham, (510) 644-6128

A. Definition of Capital Improvements and Major Repairs

A capital improvement is any improvement to a unit or property that:

- materially adds to the value of the property;
- appreciably prolongs its useful life or adapts it to new use;
- has a useful life of more than one year; and,
- has a direct cost of \$200 or more per unit affected, or \$1,500, whichever is less.

In addition, capital improvements:

- are necessary to bring the unit or property into compliance with new code requirements, or significantly improve the security of the property or any unit;
- significantly improve the seismic safety of the rental property or increase the energy efficiency of the rental property (including any improvement to allow a significantly more accurate allocation of utility costs); or,
- are provided by the landlord in good faith to primarily benefit tenants. There is a presumption that a specific capital improvement is provided if it has been approved in writing by tenants in a majority of the units affected.

Major repairs are defined as:

- a new roof covering all or substantially all of a building or a structurally independent portion of a building;
- a significant upgrade of the foundation of all or substantially all of a building or a structurally independent portion of a building;
- a new or substantially new plumbing, electrical or heating system for all or substantially all of a building;
- exterior painting or replacement of siding on all or substantially all of a building; and

- repairs reasonably related to correcting and/or preventing the spread of defects which are noted as findings in a Wood Destroying Pest and Organisms Inspection Report issued by a pest control company registered in Branch 3 of the State of California Structural Pest Control Board, provided that any expenditure for such repairs exceeds the lesser of \$6,000 or the product of \$1,000 times the number of units in the property.

Routine repair, replacement, or maintenance is not considered capital improvements or major repairs, including but not limited to the following items:

- interior and exterior painting;
- plastering and replacing broken windows;
- replacement of drapes and carpets;
- cleaning;
- fumigation;
- routine landscaping;
- repair of all standard services, including electrical repairs, plumbing repairs, and carpentry; and,
- repair and replacement of furnished appliances.

B. Increase in Rent from Capital Improvements and Major Repairs

1. Permanent Increase in Rents, Capital Improvements

When a landlord demonstrates that an improvement affecting a rental unit qualifies as a capital improvement, the rent for the unit can be permanently increased by a maximum of 1.042 percent of the cost of the improvement attributable to that unit. The cost of repairs necessarily performed in conjunction with the approved capital improvement is included in the cost of the capital improvement.

This percentage figure was determined by City staff based on a review of past projects. Previously, the City used a methodology with an NOI calculation and amortization schedules for capital improvements. They moved to the percentage of cost model because of Costa-Hawkins. Their reasoning is that Costa-Hawkins introduces a new variable that affects a landlord's ability to recover costs. In other words, landlords are able to recover costs through vacancy decontrol and not just through a permanent rent increase. Unfortunately, it is impossible to predict future rental income based on turnover rates. To deal with this issue, the City looked at actual projects over the past 3 to 4 years and determined that a percentage permanent rent increase of approximately 1 percent of capital costs is necessary for a landlord to recover costs.

2. Permanent Increase in Rents, Major Long-Term Repairs

A landlord's expenditure for any of the major long-term repairs listed above, to the extent that they are reasonably necessary for the proper maintenance of the property, qualifies for a permanent increase in the rent ceiling.

The increase for exterior painting and siding is equal to the cost of the major repair amortized over 10 years, with interest at 7.5 percent. The monthly increase is equal to 1.187 percent of the cost of the major repair.

The increase for the other major repairs listed above is equal to the cost of the major repair amortized over 15 years, with interest imputed at 7.5 percent. The monthly increase is equal to 0.927 percent of the cost of the major repair. A landlord can seek an adjustment based on net operating income.

Landlords must provide supporting documentation to substantiate the nature and cost of the claimed improvement. Documentation may include copies of invoices, signed contracts, material and labor receipts, self labor logs, proof of entitlement to skilled labor rate (if claimed), canceled checks or any other items of documentation accepted and used in the normal course of business.

C. Limit on Rent Increases – Special Populations

The sum of all rent ceiling increases may be no greater than \$25 for the following populations:

- Any tenant over the age of 62 whose household income does not exceed 30 percent of the Oakland PMSA median income of a household of the same size, as estimated by HUD annually; or 150 percent of the total SSI payment (i.e. federal and state components) in California, effective January 1, 1996, adjusted by the COLA, for a person or persons living in their own household; whichever is more for a household of the same size.
- Any tenant receiving general assistance pursuant to California Welfare & Institutions Code sections 17000 et seq., Aid to Families with Dependent Children or any successor program, Supplemental Security Income or Social Security Disability Insurance.

D. Tenant Displacement and Relocation

Berkeley allows landlords to displace tenants to improve their properties if, by the determination of the building permit department, a tenant cannot stay in the development as the work occurs.

Under that scenario, a tenant is entitled to the following relocation benefits:

- Initial storage and moving costs; and,
- Up to \$200 per month in rent differential.

The relocation benefits are limited to 3 months.

Tenants have the right to return to the unit. The City has interpreted Costa-Hawkins such that even if a new tenant moved in, the rent charged remains the same as if the original tenant moved back. Therefore, there is no financial incentive to displace the original tenant.

CITY of OAKLAND

RESIDENTIAL RENT ADJUSTMENT PROGRAM

City Attorney's Office: Richard Illgen, (510) 238-6517

A. Definition of Capital Improvements

Capital improvement costs are those improvements that materially add to the value of the property and appreciably prolong its useful life or adapt it to new building codes. Those improvements must primarily benefit the tenant rather than the landlord.

Eligible capital improvements include, but are not limited to, the following items:

- Improvements that primarily benefit the tenant rather than the landlord (for example, the remodeling of a lobby would be eligible as a capital improvement, while the construction of a sign advertising the rental complex would not be eligible). However, the complete painting of the exterior of a building, and the complete interior painting of internal dwelling units are eligible capital improvement costs.
- Equipment permanently fixed in place or relatively immobile (for example, draperies, blinds, carpet, sinks, bathtubs, stoves, refrigerators, and kitchen cabinets are eligible capital improvements; hot plates, toasters, throw rugs, and hibachis would not be eligible as capital improvements).
- Repairs completed in order to comply with the Oakland Housing Code may be considered capital improvements. If the repairs are considered as "Priority 1 or 2" condition(s), then the repairs may not be considered as capital improvements.
- Use of a landlord's personal appliances, furniture, etc., or those items inherited or borrowed are not eligible for consideration as capital improvements.
- Normal routine maintenance and repair of the rental unit and the building is not a capital improvement cost, but a housing service cost.

A Priority 1 condition indicates a major hazardous or uninhabitable condition(s). The condition must be abated immediately by correction, removal, or disconnection. A Priority 2 condition indicates major hazardous or inhabitable conditions that can be deferred through agreement with the Code Enforcement section. A schedule of Priority 1 and Priority 2 conditions are incorporated at the end of this report.

B. Increase in Rent from Capital Improvements

Generally, capital improvement costs can be passed through to tenants. Items defined as capital improvements will be given a useful life period of 5 years and are amortized over that period. Therefore, a monthly rent increase of $1/60^{\text{th}}$ of the average per-unit capital improvement cost is allowable. The landlord may divide the total cost of the capital improvement by 60 and then divide this monthly increase equally among the units that benefit from the improvement. The rent increase justified by capital improvements is reduced from the allowable rent in the 61st month.

If capital improvements are financed with a loan and the term of financing exceeds 5 years, the formula for the allowable increase is the monthly loan payment divided by the number of units that benefit from the capital improvement.

Capital improvement costs are calculated according to the following rules:

- For mixed-use structures, only the percent of residential square footage will be applied in the calculations of capital improvement costs. The same principle is applied to landlord-occupied dwellings.
- If a unit is occupied by an agent of the landlord, this unit must be included when determining the average cost per unit (for example, if a building has 10 units, and a nonpaying manager occupies one, any capital improvement cost is divided by 10, not 9, in determining the average rent increase).
- Equipment otherwise eligible as a capital improvement will not be considered if a "use fee" is charged (i.e., coin-operated washers and dryers).

C. Rent Increase Limits

Credit for capital improvements will only be given for improvements that have been completed and paid for within the 24-month period prior to the date of the proposed rent increase. However, no more than 12 months of capital improvement costs may be passed on to a tenant in any 12-month period. For example, in year one, a landlord makes a capital improvement by replacing a roof. In year two, the landlord makes another capital improvement by painting the exterior of the building. The landlord would not be able to pass on the roof and exterior painting capital improvement costs during the same year, but would have to pass them on in separate years, subject to the 24-month time limitations.

The rent increase justified by capital improvements is reduced from the allowable rent in the 61st month.

D. Tenant Relocation

Tenant displacement is governed by the City's Just Cause for Eviction ordinance. Tenant relocation benefits are regulated by the City's Code Enforcement Relocation Ordinance.

Under the Just Cause ordinance, an owner may seek temporary possession of a unit to undertake substantial repairs if the repairs cannot be completed while the unit is occupied and:

- the repairs are necessary either to bring the property into compliance with applicable codes and laws affecting the health and safety of tenants of the building; or,
- the repairs are necessary under an outstanding notice of code violations affecting the health and safety of tenants of the building.

A tenant cannot be displaced for a period in excess of 3 months unless the owner receives the permission of the Rent Board. Upon completion of the needed repairs, the owner must offer the displaced tenant the first right to return to the unit at the same rent with a rental agreement of substantially the same terms.

Property owners must pay relocation benefits to a tenant who must move because of the City's enforcement of housing and building codes. If the owner refuses to make the payment, the City may choose to make the payment to the displaced tenant and then place a lien on the property to recover these costs.

If the displacement is permanent (the move is for 60 days or longer), a tenant is entitled to a payment equal to twice the HUD Fair Market Rent figure for a unit of comparable size to the vacated unit, plus a payment of \$200.

If the displacement is temporary (the move is for less than 60 days), an eligible tenant may recover their actual and reasonable moving expenses and the cost of temporary housing accommodations incurred as a result of the displacement.

If immediate displacement of the tenant is required (the tenant has less than 30 days notice to move), the tenant is entitled to an additional \$500 payment from the owner.

E. Definition of Priority 1 and Priority 2 Conditions

The following conditions describe 5 major hazard conditions classified as Priorities 1 & 2:

Mechanical

<u>Priority 1</u>	<u>Priority 2</u>
A. Unvented heaters	A. Damaged gas appliance
B. No combustion chamber, fire or vent hazard	B. Flame impingement, soot
C. Water heaters in sleeping rooms, bathrooms	C. Crimped gas line, rubber gas connections
D. Open gas lines, open flame heaters	D. Dampers in gas heater vent pipes, no separation or clearance through or near combustible surfaces
	E. Water heater on garage floor

Plumbing

<u>Priority 1</u>	<u>Priority 2</u>
A. Sewage overflow on surface	A. Open sewers or waste lines
	B. Unsanitary, inoperative fixtures, leaking toilets
	C. T&P systems, newly or improperly installed

Electrical

<u>Priority 1</u>	<u>Priority 2</u>
A. Bare wiring, open splices, unprotected knife switches, exposed energized electrical parts	A. Stapled, cord wiring, extension cords
B. Evidence of overheated conductors, including extension cords	B. Open junction boxes, switches, outlets
C. Extension cords under rugs	C. Over-fused circuits
	D. Improperly added wiring

Structural

Priority 1

- A. Absence of handrail, loose, weakly-supported handrail
- B. Broken glass, posing potential injury immediate
- C. Hazardous stairs
- D. Collapsing structural members

Priority 2

- A. Garage wall separation
- B. Uneven, walks, floors, tripping hazards
- C. Loose or insufficient supporting structural members
- D. Cracked glass, leaking roofs, missing doors (exterior) and windows
- E. Exit, egress requirements; fire safety

Other

Priority 1

- A. Wet garbage
- B. Open wells or unattended swimming pools
- C. Abandoned refrigerators
- D. Items considered by field person to be immediate hazards

Priority 2

- A. Broken-down fences or retaining walls
- B. High, dry weeds, next to combustible surfaces
- C. Significant quantity of debris
- D. Abandoned vehicles

CITY of SAN JOSE

APARTMENT RENT ORDINANCE

A. Definition of Capital Improvements and Rehabilitation

Capital improvements are defined as improvements that:

- materially add to the value of the property;
- appreciably prolong its useful life, or adapt it to new uses; and,
- are required to be amortized over the useful life of the improvement of the building using the straight-line depreciation provisions of the Internal Revenue Code.

Cost of rehabilitation is defined as the costs of any rehabilitation or repair work done on or in a rental unit or common area to:

- comply with an order issued by the San Jose Building Department, San Jose Director of Neighborhood Preservation, or the Fire Department; or,
- repair damage resulting from fire, earthquake, or other natural disaster.

B. Rent Increase Limits

With capital improvement costs incurred in the 12 months prior to a rent increase, these costs are averaged on a per-unit basis and amortized over at least 60 months. Supporting documents, such as receipts, invoices, and/or accepted bid or contracts, are needed to support the capital improvement costs.

With rehabilitation expenses incurred in the 12 months prior to the rent increase, the expenses are averaged on a per-unit basis and amortized over at least 36 months. Supporting documents, such as receipts, invoices, and/or accepted bid or contracts, are needed to support the rehabilitation expenses.

San Jose's rent stabilization ordinance generally limits rent increases to 8 percent annually, although this amount can be exceeded with the pass-through of costs from increases in operating and maintenance expenses, capital improvements, and rehabilitation expenses. Any increase in excess of 8 percent is subject to a hearing. Generally, proposed rental increases not exceeding 5 percent of monthly rent plus pass-through of costs of capital improvements, increased costs of maintenance and operation, and/or costs of rehabilitation, are allowable. Financing costs related to maintenance and upkeep of the units are

allowable pass-throughs to tenants. Financing costs from increased debt not traceable to maintenance and upkeep are not allowable pass-throughs to tenants.

In cases where a landlord requests a rent increase in excess of 8 percent, a Hearing Officer may also consider the economic and financial hardship imposed on a tenant. A Hearing Officer can make the determination that a proposed increase constitutes an unreasonably severe financial or economic hardship on a particular tenant, and is empowered to disallow the increase beyond 8 percent. Any tenant whose household income and monthly housing expense meet the criteria established by the Housing Assistance Payments Program under Section 8, existing housing provisions of the Housing and Community Development Act of 1974 (P.L. 93-383) are deemed to be suffering under financial and economic hardship which must be weighed in the Hearing Officer's determination of allowable rent increases.

C. Tenant Relocation

San Jose's rent control ordinance does not require a landlord to show just cause in order to evict a tenant. However, San Jose recently passed an ordinance where property owners have 2 options for removing tenants from rent-controlled units through "no cause" notices to vacate. For tenants living in a rent-controlled unit 1 year or more, the owner may choose one of the following options to end a tenancy:

- Issue a 90-day "no cause" notice in a slow market, or 120 days in a tight market (defined as a 3 percent vacancy rate or less as determined by the Director of Housing).
- Issue a 60-day "no cause" notice with an offer to go to mediation/arbitration.

If an arbitrator finds that a lease will terminate in 90 days or less, the arbitrator may base a ruling by weighing the hardship to the tenant of a quick eviction against the hardship to the landlord of keeping the tenant in the unit, subject to the landlord's rights to continue to make a reasonable income from the unit.

If a tenant can demonstrate certain specific hardships, such as living in the unit for 3 or more years, significant illness, or other factors, the tenant is eligible to have the move out date extended by an additional 60 days (for a total of 120 days).

NEW YORK CITY RENT STABILIZATION CODE

A. Definition of Major Capital Improvements

Under the New York City Rent Stabilization Code, a major capital improvement must meet all of the following criteria:

- the improvement is deemed depreciable under the Internal Revenue Code, other than for ordinary repairs;
- the improvement is for the operation, preservation and maintenance of the structure;
- it improves the building or the building complex and directly or indirectly benefits all tenants, with the same work performed in all similar components of the building or building complex; and,
- the item being replaced meets the requirements set forth in the City's useful life schedule.

A schedule of major capital improvements and useful life appears at the end of this report.

A landlord may secure a waiver of the useful life requirements if the owner demonstrates that 1 or more of the following circumstances exist:

- the item or equipment cannot be repaired and must be replaced during its useful life because of a fire, vandalism or other emergency, or "act of God" resulting in an emergency.
- the item or equipment needs to be replaced because it is beyond repair, spare parts are no longer available, or required repairs would cost more than 75 percent of the cost of the total replacement of the item. Certification by a licensed engineer or architect is considered proof of such condition(s). The owner may also be required to submit proof that the item or equipment was properly maintained. Such proof may include receipts for repairs and parts or maintenance logs.

B. Allowable Rent Increases

A landlord is entitled to a rent increase with the installation of new equipment or improvements. The increase in the monthly stabilization rent may be up to 1/40th of the total cost, including installation but excluding finance charges, for installation of new equipment. For major capital improvements, the increase in the rent may be up to 1/84th of the total cost (7-year amortization). Any increase due to interest expense related to capital improvements is not allowed.

C. Rent Increase Limits

An increase is not collectible during the term of a lease, unless a specific provision in the tenant's lease authorizes an increase during its term. An increase is also not allowed if government grants are used to finance the major capital improvements. Low interest rate loans are not considered grants.

D. Conditions for Tenant Displacement

An owner is allowed to permanently displace a tenant if the owner will demolish his/her building. In addition, an owner is allowed to displace a tenant if the owner is required to eliminate inadequate, unsafe or unsanitary conditions and demolish or rehabilitate the unit. In this instance, an owner is required to:

- prove that it has a commitment for the required financing to demolish or rehabilitate the unit;
- prove that any rehabilitation requires the temporary removal of the tenant; and,
- agree to offer (and will offer) the tenant the right of first occupancy following any rehabilitation at an initial rent as determined by the applicable law.

E. Tenant Relocation

An owner is required to pay all reasonable moving expenses as well as a reasonable stipend and/or relocate the tenant to a suitable housing accommodation at the same or lower regulated rent in a closely proximate area. If no such housing accommodation is available at the same or lower regulated rent, the owner may be required to pay the difference in rent between the subject housing accommodation and the new housing accommodation for a period as determined by the City.

If an owner seeks to demolish the building, an owner must pay all reasonable moving expenses and provide the tenant a reasonable period of time to vacate the unit. An owner must:

- relocate the tenant to a suitable housing accommodation at the same or lower legal regulated rent in a closely proximate area, or in a new residential building if constructed on the site, in which case suitable interim housing must be provided at no additional cost to the tenant. In addition to reasonable moving expenses, a landlord must pay a \$5,000 stipend;

- where an owner provides relocation of the tenant to a housing accommodation at a higher rent, the owner may be required to pay the tenant a stipend equal to the difference in rent multiplied by 72 months. In addition, the owner must pay reasonable moving costs; or,
- pay the tenant a stipend, which is the difference between the tenant's current rent and an amount calculated using the City's demolition stipend chart. This difference is to be multiplied by 72 months.

F. Useful Life Schedule for Major Capital Improvements

<u>Replacement Item or Equipment</u>	<u>Years</u>	<u>Replacement Item or Equipment</u>	<u>Years</u>
Boilers and Burners		Kitchen Upgrading	
Cast Iron Boiler	35	Metal/Wood Cabinets.....	20
Package Boiler	25	Ranges.....	20
Steel Boiler	25	Refrigerators.....	15
Burners.....	20	Sinks	20
Windows		Water Tanks	
Aluminum	20	Metal.....	25
Wood.....	25	Wood	20
Steel.....	25	Waste Compactors.....	
Storm	20	10	
Vinyl.....	15	Air Conditioners	
Roofs		Individual Units/Sleeves	
2 Ply (asphalt)	10	10	
3-4 Ply (asphalt).....	15	Central System	
5 Ply (asphalt).....	20	15	
Shingle.....	20	Branch Circuitry Fixtures	
Single-Ply Rubber	20	15	
Single-Ply Modified Bitumen	10	Aluminum Siding.....	
Quarry Tile.....	20	25	
Pointing	15	Vinyl Siding.....	
Rewiring	25	15	
Intercom System	15	Catwalk.....	
Mailboxes	25	25	
Plumbing/Repiping		Chimney	
Galvanized Steel.....	25	Steel	
TP Copper	30	25	
Brass cold water.....	15	Brick	
Fixtures	25	25	
Elevators		Courtyards/Walkways/Driveways	
Major Upgrade	25	Cement.....	
Controllers and Selector	25	15	
Doors		Asphalt.....	
Apartment Entrance	25	10	
Lobby/Vestibule.....	15	Fire Escapes.....	
Bathroom Upgrading		25	
Toilets and Valves.....	20	Fuel Oil Tanks	
Bathroom and Sinks.....	20	In Vaults	
Vanity	20	25	
		Underground	
		20	
		Water Heating Units	
		Hot Water/Central Heating	
		20	
		Hot Water Heater (Domestic).....	
		10	
		Parapets	
		Brick	
		25	
		Resurfacing Exterior Walls.....	
		25	
		Solar Heating System	
		25	
		Structural Steel.....	
		25	
		Television Security.....	
		10	

For major capital improvements not listed above, the owner must provide evidence that the useful life of the item or equipment being replaced has expired.

G. Definitions of Major Capital Improvements

This section describes in detail major capital improvement expenses eligible for reimbursement through rent increases:

Air conditioner — new central system; or individual units set in sleeves in the exterior wall of every housing accommodation; or air conditioning circuits and outlets in each living room and/or bedroom (see Rewiring).

Aluminum siding — installed in a uniform manner on all exposed sides of the building (see Resurfacing).

Bathroom modernization — complete renovation including new sinks, toilets, bathtubs and/or showers and all required trims in every housing accommodation; or any individual component or fixture if done building wide.

Boiler and/or burner — new unit(s) including electrical work and additional components needed for the installation.

Boiler room — new room where none existed before; or enlargement of existing one to accommodate new boiler.

Catwalk — complete replacement.

Chimney — complete replacement, or new one where none existed before, including additional components needed for the installation.

Courtyard, driveways and walkways — resurfacing of entire original area within the property lines of the premises.

Doors — new lobby front entrance and/or vestibule doors; or entrance to every housing accommodation, or fireproof doors for public hallways, basement, boiler room and roof bulkhead.

Elevator upgrading — including new controllers and selectors; or new electronic dispatch overlay system; or new elevator where none existed before, including additional components needed for the installation.

Fire escapes — complete new replacement including new landings.

Gas heating units — new individual units with connecting pipes to every housing accommodation.

Hot water heater — new unit for central heating system.

Incinerator upgrading — including a new scrubber.

Intercom system — new replacement; or one where none existed before, with automatic door locks and push-button speaker boxes and/or telephone communication, including security locks on all entrances to the building.

Kitchen modernization — complete renovation, including new sinks, counter tops and cabinets in every housing accommodation; or any individual component or fixture if done building-wide.

Mailboxes — new replacements and relocated from outer vestibule to an area behind locked doors to increase security.

Parapet — complete replacement.

Painting and waterproofing — as necessary on exposed sides of the building.

Repiping — new hot and/or cold water risers, returns, and branches to fixtures in every housing accommodation, including shower bodies, and/or new hot and/or new cold water overhead mains, with all necessary valves in basement.

Resurfacing of exterior walls — consisting of brick or masonry facing on entire area of all exposed sides of the building.

Rewiring — new copper risers and feeders extending from property box in basement to every housing accommodation; must be of sufficient capacity (220 volts) to accommodate the installation of air conditioner circuits in living room and/or bedroom.

Roof — complete replacement or roof cap on existing roof installed after thorough scraping and leveling as necessary.

Solar heating system — new central system, including additional components needed for the system.

Structural steel — complete new replacement of all beams including footing and foundation.

Television system — new security monitoring system including additional components needed for the system.

Waste compactor — new installation(s) serving entire building.

Waste compactor room — new room where none existed before.

Water sprinkler system (for fire control purposes) — new installation(s).

Water tank — new installation(s).

Windows — new framed windows.