

RESOLUTION NO. 2011-013

A RESOLUTION OF THE CITY COUNCIL OF THE
CITY OF THOUSAND OAKS DENYING APPEAL
AND SUSTAINING RENT ADJUSTMENT
COMMISSION'S DECISION GRANTING "JUST AND
REASONABLE RETURN" RENT INCREASE FOR
THUNDERBIRD OAKS MOBILE HOME PARK IN
AMOUNT NOT TO EXCEED \$62.00 PER SPACE
PER MONTH

WHEREAS, on June 4, 2010, an application was filed on behalf of the Thunderbird Oaks Mobile Home Park ("Park") by the owner AVMGH Limited ("Park Owner") under §5-25.06(b) of the Mobile Home Rent Stabilization Ordinance ("Ordinance") requesting a "Just and Reasonable" rent increase of \$322.52 per space, per month; and

WHEREAS, on October 8, 2010, the Park Owner submitted an amended application requesting a revised rent increase of \$260.62 per space, per month; and

WHEREAS, on January 10, 2011, the Thousand Oaks Rent Adjustment Commission ("RAC") held a public hearing to consider the amended application. Evidence and testimony was presented to RAC by City staff, the applicant, a representative retained by some of the tenants of the Park, other tenants of the Park, and the public. The public comment portion of the hearing was closed, and the matter was continued for deliberation and decision to January 18, 2011; and

WHEREAS, on January 18, 2011, after considering the evidence and testimony presented, RAC adopted Resolution No. RAC 08-2011 and approved a Just and Reasonable rent increase of \$62 per space per month to be phased in over a two-year period (\$31 increase each year); and

WHEREAS, on January 31, 2011, the Park Owner filed a timely appeal of RAC's decision. The appeal challenged RAC's decision on the following grounds:

- The base year should have been 1979, not 1986.
- Base year income should have been adjusted based on appraisal, not the Price Level Adjustment mechanism advocated by City's expert, Dr. Baar.
- The management expenses should not have been increased in the base year to account for management services provided by the park owner.

- Base year net operating income should have been indexed at 100% of CPI, not 50%.
- It was improper to phase-in the rent increase over a two-year period; and

WHEREAS, City Council's decision on this appeal was based on evidence and testimony submitted at the RAC public hearings. The Administrative Record ("AR") for the RAC hearings has been compiled into 5-volumes (Parts A-E), tabbed and Bates stamped (CTO 00001-02663). City Council did not consider any new evidence or testimony at the appeal hearing.

NOW, THEREFORE, BE IT RESOLVED by the City Council as follows:

SECTION 1. Findings.

Based upon substantial evidence and testimony received at the RAC hearings and contained in the Administrative Record, City Council makes the following findings:

A. Provisions in the Ordinance and Regulations Governing Rent Increases

1. The Park Owner may apply for a rent adjustment based on the "just and reasonable return" standard in the Ordinance. The principal purpose of this provision is to provide rent adjustments which meet constitutional fair return standards.

2. RAC has promulgated and adopted detailed guidelines ("Guidelines") pursuant to the Ordinance implementing the "just and reasonable return" standard. These Guidelines are contained in resolutions RAC-2 and RAC-5.

3. The Guidelines authorize the use of a "maintenance of net operating income" ("MNOI") methodology and standard to evaluate applications seeking "just and reasonable return." However, the Guidelines allow the Commission, at its discretion, to consider other approaches if appropriate documentation is provided.

4. The Park Owner has requested a rent adjustment based on the MNOI standard.

5. The City Council agrees with RAC and finds that the MNOI standard is the appropriate methodology for considering the Park Owner's application and meets the constitutional fair return standard.

B. Expert Analysis of MNOI standard. The City retained an expert on fair return issues, Dr. Kenneth Baar, to prepare a fair return analysis (AR Tab 5.6: CTO 02062-02124) Based on Dr. Baar's resume, the Council finds that Dr. Baar has the requisite expertise to render opinions regarding what rents in this case provide a fair return to the Park Owner.

C. Analysis of Park Owner's request under the MNOI standard. In order to evaluate a "just and reasonable" rent adjustment application using an MNOI analysis, the following determinations must be made:

1. Designation of the appropriate base year.
2. The base year rental income, including any adjustments.
3. The base year operating expenses, including any necessary adjustments.
4. An inflation adjustment of base year net operating income.
5. Phase-in of rent Increase.

1. Designation of the Appropriate Base Year.

a. The Guidelines state that the base year shall be 1979 when the financial information for that year is available. When financial information for 1979 is not available, the first year for which a park owner has financial records may be used as a base year. (Guidelines §§3 and 4 at AR Tab 5.6: CTO 02205-02206)

b. The Guidelines also vest in the Commission the discretion to consider a base year other than 1979 for good cause. (Guidelines § 3.07 at Tab 5.6: CTO 02206)

c. The Park Owner has owned the property since 1974. Since the adoption of Resolution RAC-2 in 1981, the regulations have clearly provided that the consideration of increases in expenses and income since the 1979 base year would provide the basis for determining what net operating income and rent levels would be fair in the future.

d. The Park Owner was unable to provide data on actual operating expenses and net operating income for the base year (1979) or for any year from 1976 through 1990 other than 1986. Instead the Park Owner "imputed" expenses for 1979 from 1986 expense data.

e. Although Dr. Baar concluded that there were rationales in support of the use of 1979 as the base year, notwithstanding the Park Owner's lack of 1979 data, he also concluded that using 1986 as a base year was appropriate under the Ordinance and Guidelines. Therefore, the Council agrees with RAC and is persuaded that as a policy the Guidelines should be adhered to

the extent such adherence provide results that are in keeping with the intent of the Ordinance and Guidelines.

f. The Council agrees with RAC and concludes that there is good cause to use 1986 as the base year since the Guidelines stipulate that base year should have actual income and expense data for purposes of comparison.

2. Base Year Rental Income

a. The City's appraiser, Mr. Brabant, found that average market rent for Thunderbird Oaks in 1979 was \$205 a month and Dr. Barr found that average actual rent during 1979 was \$198. Therefore, the average 1979 rents, prior to rent control, were at market level and provided a fair return.

b. Council agrees with Dr. Baar that an adjustment of 1986 base year rent is necessary in order bring base year rents to a level representing a fair return in 1986. (Baar Report at AR Tab 5.6: CTO: 0211; Baar testimony at AR Tab 15: CTO 0234, lines 2-5; and Guidelines § 1.03 at AR Tab 5.9: CTO 02197)

c. Council adopts Dr. Baar's conclusion that the City's appraiser's finding of comparable rent for the Park in 1986 of \$320 per space per month would provide a rent in excess of that required to provide a fair return in 1986. (Baar Report at AR Tab 5.6: CTO 02112; and Baar Testimony at AR 15: CTO 02344, lines 8-17)

d. The Guidelines authorize base year "Price Level Adjustments" for individual parks to recover rent increases which were authorized but not imposed by the park owner. "Adjusted Income for Below Market Rentals" is defined in the Guidelines as an amount representing the difference between the actual rent collected and what the landlord could have collected if the units had been rented at their full market value, including "... where the increases permitted by the Rent Stabilization Ordinance or the Regulations and Guidelines of the Rent Adjustment Commission could have been made but have not been made because of the landlord rental policies and purposes." (Guideline §§2.05 and 3.04 at AR Tab 5.9: CTO 02199 and 02205)

d. All automatic rent adjustments which could have been implemented shall be added to the 1979 net operating income in order to determine what net operating income would provide a fair net operating income in the current year. (Guideline § 3.05 at AR Tab 5.9: CTO 02205-02206)

e. Based on the opinion of Dr. Baar, Council finds that the reasonable interpretation of the intent of these Guidelines sections is to provide owners with the right to implement rent increases which were permitted in prior years, but were not implemented at the time they were permitted. (Baar Report at AR Tab 5.6: CTO 02087-02088)

f. In this application, complete information on rent increases was limited to the period from 1983 to 1986. (Baar Report at AR Tab 5.6: CTO 02088)

g. From 1983 through 1986, the Park Owner increased rents by 10.3%, increasing the average rent in the park from \$246.43 to \$273.10. (Baar Report at AR Tab 5.6: CTO 02088) This increase compares with the total of 21% in rent increases authorized, and which could have been collected in 1984, 1985, and 1986. This difference provides the basis for a "Price Level Adjustment." (Baar Report at AR Tab 5.6: CTO 02088)

h. For the preceding three years (1980 to 1983) average rents increased from about \$198 to \$235, an increase of about 18%. The allowable rent increases during this period were 24% (3 x 8%). (Baar Report at AR Tab 5.6: CTO 02088) However, the Park Owner did not provide any base year rent information and the residents of the Park provided information for only a few spaces. Under these circumstances, a "price level adjustment" for the period 1980 to 1983 is not justified.

i. City Council agrees with RAC that for the purposes of the MNOL analysis a Price Level Adjustment should be applied to the 1986 base year rent resulting in an adjustment from \$273 to \$298 per space per month as calculated by Dr. Baar. (Baar Report at AR Tab 5.6: CTO 02089)

j. City Council agrees with RAC and finds that the Price Level Adjustment detailed above adequately provides the Park Owner an approximation of fair return for 1986.

3. Base Year Operating Expenses

a. The Guidelines provide that management and administrative expenses "must be calculated for both the base year and the current year at the same percentage of actual income" and the total management and administrative expenses cannot exceed 8% of income. (Guidelines § 2.11 at AR Tab 5.9: CTO 02202)

b. In this case, the Park Owner reported that 1986 management and administration expenses totaled \$30,878, which is 5.9% of rental income for that year; and in 2009 management and administration

expenses totaled \$167,392, which is 21.9% of rental income for that year. (Baar Report at AR Tab 5.6: CTO 02089-02090)

c. For the period 1986 to 2009, data submitted by the Park Owner showed that administration and management expenses increased by 449%, compared to the CPI increase of 99% during this same period. (Baar Report at AR Tab 5.6: CTO 02089)

d. The Park Owner has indicated that the performance of management and administration tasks that were performed directly by the owners in 1986 were contracted to a paid third party in 2009. (Baar Report at AR Tab 5.6: CTO02091)

e. For the reasons set forth in Dr. Baar's written analysis (Baar Report at AR Tab 5.6: CTO 02091), the Park Owner did not present evidence that a higher level of effort or increased service was required in order to perform management and administration tasks in 2009 than was required in 1986, which could have justified the higher level of expenditure in 2009.

f. The transfer of management and administration tasks performed by the owner to a paid third party only resulted in a change in how the cost of these tasks is accounted, and not a cost increase based on increased service level, which would result in an understatement of expenses in the base year.

g. The cost of management and administrative tasks performed by the Park Owner should be imputed to the base year operating expense total in order to avoid exceptionally low expenses in the base year, which would result in an unjustified overstatement of the NOI for the base year.

h. City Council agrees with Dr. Baar's conclusion that it is not reasonable to use the 8% management and expense cap in Guidelines § 2.11 for the reasons stated in Dr. Baar's report (Baar Report at AR Tab 5.6: CTO 02092).

i. In calculating the amount of the imputed management and administrative expense for 1986, it is reasonable to assume that such expenses would have increased at the same rate as the CPI between 1986 and 2009 in order to maintain the same level of service. This calculation is more favorable to the Park Owner than the method in the Guidelines that management and administration expenses are calculated using the same percentage of rental income in both the base year and the current year. It is based on the view that management and administration expenses would increase at the same rate as the CPI in order to maintain the same level of services, even if rents went up at a lower rate. As a result, overall base year operating expenses are reduced and consequently base year net operating income is increased, relative to the outcome that would result from calculating management and administration

therefore would not comply with the stated purpose of the Ordinance to safeguard residents from excessive rent increases while providing the Park Owner a just and reasonable return. Phasing in the increase over a two-year period would alleviate this hardship while still providing the Park Owner a fair return.

SECTION 2. Decision.

Based on the findings in SECTION 1 above, City Council denies the appeal in its entirety and sustains the decision of RAC as set forth in Resolution RAC 08-2011.

SECTION 3. Authorized Rent Increase.

A. Amount of Increase

The Park Owner is entitled to, and is hereby granted, a rent increase of \$62 per space per month in order to obtain a just and reasonable return based on the findings in SECTION 1 above. The bases for this calculation are set forth in Table 3 of Dr. Baar's report (Baar Report at AR Tab 5.6: CTO 02108) and in the table below.

MNOI Fair Return Calculation

	Base Year (1986)	Current Year (2009)
Rental Income (excluding reimbursed utilities) With Base Year Rent Adjustment pursuant to MNOI analysis	\$575,736	\$764,529
Operating Expenses adjusted pursuant to MNOI analysis	\$207,054	\$333,217
Net Operating Income	\$368,882	431,312
Fair Net Operating Income (50% CPI Index) (49.5% Increase over Base Year NOI)		\$551,180
Gross Annual Rent Increase Required (Fair NOI – Actual Current Year NOI)		\$119,868
Rent Increase Required Per Space Per Month (Gross Annual Rent Increase divided by 12 months divided by 161 spaces)		\$62

expenses at the same percentage of rental income in the base year and the current year. (Baar Report at AR Tab 5.6: CTO 02091)

j. City Council agrees with RAC and finds that 1986 management and administration expenses as imputed by Dr. Baar totaled \$84,117. The basis for this computation is set forth in footnote 75 of Dr. Baar's report (Baar Report at AR Tab 5.6: CTO 02091), which is adopted and incorporated into this resolution by reference.

k. For the purposes of the MNOI analysis, City Council agrees with RAC and finds that the total 1986 base year operating expenses, as adjusted, are projected to be \$207,054. The basis for this computation is set forth in Table 1 of Dr. Baar's report (Baar Report at AR Tab 5.6: CTO 02103), which is adopted and incorporated into this resolution by reference.

4. An Inflation Adjustment of Base Year Net Operating Income

a. Under the Section 5-25.06(b)(1) of the Ordinance, the Commission has the authority to grant individual park rent adjustments if the rent "otherwise permitted" does not provide for a just and reasonable rent.

b. California courts have upheld maintenance of net operating income standards which provide for indexing net operating income at 40% and 50% of the percentage increase in the CPI from the base year to the current year. (Baar Report at Tab 5.6: CTO 02094-02097)

c. Neither the Ordinance nor the Guidelines provide a rate of indexing for the MNOI standard.

e. City Council agrees with the findings in Dr. Baar's report (Baar Report at AR Tab 5.6: CTO 02097-02100) that the returns from a park investment may be attractive when net operating income increases at less than the full rate of increase in the CPI. Growth in net operating income provides the Park Owner with appreciation in valuation as well as growth in income in an investment that typically is low-risk with a steady and consistent income stream.

f. City Council agrees with RAC and concludes that indexing the net operating income by 50% of the percentage increase in the CPI will provide a "just and reasonable return" to the Park Owner.

5. Phase-In of Rent Increase

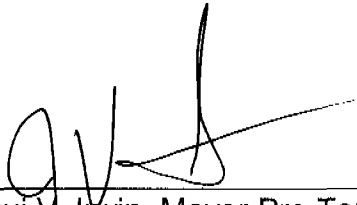
City Council agrees with RAC and finds that a \$62 per space per month rent increase represents a 15.7 % increase over existing rents (\$394). Such an increase, if implemented all at once, would represent a particular hardship on the tenants of the Park, who are seniors, many of whom living on fixed incomes, and

B. Phasing of Rent Increase

This increase in rents shall be phased over a 2-year period in an amount not to exceed \$31.00 per space per month, with the date of the initial increase to be 90 days from the date of formal notice of such increase is provided to the tenants, and the date of the subsequent increase shall be not sooner than 365 days from the date of the initial increase.

* * * * *

PASSED AND ADOPTED this 26th day of April, 2011.



Jacquie V. Irwin, Mayor Pro Tem
City of Thousand Oaks, California

ATTEST: _____



Linda D. Lawrence, City Clerk

APPROVED AS TO FORM:



Amy Albano, City Attorney

APPROVED AS TO ADMINISTRATION:



Scott Mitnick, City Manager

CERTIFICATION

STATE OF CALIFORNIA)
COUNTY OF VENTURA) SS.
CITY OF THOUSAND OAKS)

I, LINDA D. LAWRENCE, City Clerk of the City of Thousand Oaks, DO
HEREBY CERTIFY that the foregoing is a full, true, and correct copy of Resolution
No. 2011-013, which was duly and regularly passed and adopted by said City
Council at a special meeting held April 26, 2011, by the following vote:

AYES: Councilmembers Gillette, Glancy, Bill-de la Peña, and Irwin

ABSTAINING: Mayor Fox

NOES: None

ABSENT: None

IN WITNESS WHEREOF, I have hereunto set my hand and affixed the
official seal of the City of Thousand Oaks, California.

4/28/11
Date Attested

Linda D. Lawrence
Linda D. Lawrence, City Clerk
City of Thousand Oaks, California