

RESOLUTION NO. 2011-025

A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF THOUSAND OAKS DENYING APPEALS AND SUSTAINING THE RENT ADJUSTMENT COMMISSION'S DECISION GRANTING A "JUST AND REASONABLE RETURN" RENT INCREASE FOR THE RANCH MOBILE HOME PARK IN AMOUNT NOT TO EXCEED \$191.95 PER SPACE PER MONTH TO BE PHASED IN OVER A SEVEN-YEAR PERIOD

WHEREAS, on June 16, 2010, an application was filed on behalf of the Ranch Mobile Home Park ("Park" or "Ranch") by the owner AVMGH, Five, Limited ("Park Owner") under §5-25.06(b) of the Mobile Home Rent Stabilization Ordinance ("Ordinance") requesting a "Just and Reasonable" rent increase of \$620.11 per space per month; and

WHEREAS the Thousand Oaks Rent Adjustment Commission ("RAC") has promulgated and adopted detailed guidelines ("Guidelines") pursuant to the Ordinance implementing the "just and reasonable return" standard; and

WHEREAS, on September 7, 2010, the Park Owner submitted an amended application requesting a revised rent increase of \$587.45 per space per month; and

WHEREAS, on December 6, 2011, RAC held a public hearing to consider the amended application. Evidence and testimony was presented by City staff. The hearing was continued to January 24, 2011; and

WHEREAS, on January 24, 2011, the Park Owner further revised the amount of the requested rent increase to \$466.12 per space per month. The Park Owner, Tenants, and members of the public presented evidence and expert testimony. The hearing was continued to February 7, 2011; and

WHEREAS, on February 7, 2011, the public hearing was closed and after considering the evidence and testimony presented, RAC adopted Resolution No. RAC 09-2011 and approved a Just and Reasonable rent increase of \$191.95 per space per month to be phased in over a seven-year period that included an interest component for the deferred rent increase at 4% annually; and

WHEREAS, on February 16, 2011, the Park Owner filed a timely appeal of RAC's decision. The appeal challenged RAC's decision on the following grounds:

1. The base year should have been 1979, not 1982.
2. Base year income should have been adjusted based on appraisal of the Park Owner, prepared by John Neet, and not in the manner advocated by City's expert, Dr. Baar.
3. The management expenses should not have been increased in the base year to account for management services provided by the Park Owner.
4. Base year net operating income should have been indexed at 100% of CPI, not 50%.
5. It was improper to phase-in the rent increase over a seven-year period; and

WHEREAS, the Association of Ranch Tenants ("Tenants") filed a timely appeal on February 28, 2011. The appeal challenged the jurisdiction of RAC to hear the application. Tenants' position was that all rent increases applicable to Ranch tenants are governed by City Council Resolution No. 84-037, and not the Ordinance. In addition, Tenants appealed certain findings made by RAC:

1. The Guidelines do not allow a "catch-up" for prior forgone rent increases.
2. The approved rent increase was not consistent with the Ordinance.
3. Any rent increase should have been based on the formula in Resolution 84-037.
4. The Base Year should have been 2009.
5. No Vega Adjustment was warranted.
6. RAC incorrectly determined current year (2009) net operating income.
7. RAC used inaccurate data for 1982 expenses.
8. Operating expenses in the current year (2009) were overstated; and

WHEREAS, Tenants and Park Owner were given ample time to analyze the application and submit evidence at the three RAC hearings; and

WHEREAS, Tenants' jurisdictional challenge was fundamental to whether RAC should have conducted a hearing on this application. Accordingly, City Council considered the jurisdictional issue first and allowed evidence outside of the administrative record to be introduced for this issue only; and

WHEREAS, City Council's decision on the remaining appeal points was based on evidence and testimony submitted at or for the RAC public hearings. The Administrative Record ("AR") for the RAC hearings has been compiled into 7-volumes (Parts A-G), tabbed and Bates stamped (CTO 00001-03341). City Council did not consider any new evidence or testimony for this portion of the appeal.

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

SECTION1. Jurisdictional Findings.

Based on the Staff Report, Administrative Record, arguments and briefs submitted by Park Owner and Tenants, and other evidence presented at the appeal hearing, City Council makes the following findings regarding RAC's jurisdiction to hear the application.

A. City Council acted pursuant to its police power in approving TPD 74-6, in interpreting Condition No. 27 of TPD-74-6 on July 27, 1976, and in setting the initial rents for the Park on September 20, 1977.

B. City Council finds that the intent of these entitlements and the initial rents was to provide rentals that were affordable to lower income residents by providing the Park Owner no more than an 11.5% rate of return on his initial investment of \$500,000 in 1977. City Council further finds that the 11.5% rate of return is a ceiling on the investment-backed expectations of the Park Owner for this Park.

C. The adoption of Resolution No. 84-037 was an exercise of City Council's police power and not an agreement between City and Park Owner.

D. Resolution No. 84-037 was not intended to apply to an application seeking a rent adjustment for a just and reasonable return.

E. Resolution No. 84-037 does not prohibit or bar Park Owner from seeking a "just and reasonable return" rent application under the Ordinance.

F. The Ordinance and Guidelines contain specific provisions to address and meet constitutional fair return standards and to process applications requesting rent adjustments for a just and reasonable return.

G. The Ordinance does not explicitly or implicitly exclude the Park, which meets the definition of "mobile home park" under the Ordinance.

H. The Ordinance applies to the Park for just and reasonable return applications.

I. Application of the Ordinance's administrative rent adjustment for a "just and reasonable return" to the Park does not contradict Resolution 84-037, but complements it.

J. Reading Resolution 84-037 and the Ordinance together, thus allowing a "just and reasonable rate of return" rent application by Park Owner, ensures that rent control at the Park meets constitutional standards.

K. Under the Ordinance, RAC has specific jurisdiction to consider applications and adjust rents to provide a just and reasonable return.

L. It was proper for RAC to hear the Park Owner's application for a "just and reasonable return" under the Ordinance.

SECTION 2. Findings on RAC Decision.

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. RAC has promulgated and adopted detailed Guidelines pursuant to the Ordinance implementing the "just and reasonable return" standard. These Guidelines are contained in resolutions RAC-2 and RAC-5 (AR Part C, Tab 7: CTO 01399-01417)

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

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

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

5. City Council finds that given the particular investment-backed expectations of the Park Owner for this Park, any just and reasonable return calculated under the MNOI methodology should provide the Park Owner no more than the equivalent of an 11.5% rate of return on net profit adjusted for inflation as calculated by Dr. Baar (no more than an increase of \$214.66 per space per month). (AR Part C, Tab 6.5: CTO 01313)

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 Part C, Tab 6.5: CTO 01272-01330) Based on Dr. Baar's resume, City Council finds that Dr. Baar has the requisite expertise to render opinions regarding what rents

provide a fair return to the Park Owner in this case and that his testimony was credible and reliable.

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 Park's base year rental income, including any adjustments
3. The Park's base year operating expenses, including any necessary adjustments
4. An inflation adjustment of base year net operating income

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)

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

c. The Park Owner was unable to provide data on actual operating expenses for the preferred base year (1979). Instead, the Park Owner "imputed" expenses for 1979 from 1982 aggregate expense data. City also had detailed expense data for the year 1999 that was provided to the City when the Park Owner applied for a rent increase in 2000.

d. Although Dr. Baar concluded that there were rationales in support of the use of 1979 or 1999 as the base year, he concluded that using 1982 as a base year was more in keeping with the intent of the Guidelines. (Baar Report at AR Part C, Tab 6.5: CTO 01315-01316). Therefore, City Council agrees with RAC and is persuaded that the City should adhere to the Guidelines to the extent such adherence provides results that are in keeping with the intent of the Ordinance and Guidelines.

e. City Council agrees with RAC and concludes that there is good cause to use 1982 as the base year since the Guidelines stipulate that the base year should have actual income and expense data for purposes of comparison with the current year (2009). Despite the lack of segregated expense data for 1982, City Council is persuaded by Dr. Baar's opinion that the aggregate expense data was sufficient for purposes of computing the MNOI calculation. (Baar Report at AR Part C, Tab 6.5: CTO 01293-01294 and 01316)

2. Base Year Rental Income

a. City Council recognizes the case of Vega v. City of West Hollywood 223 Cal.App.3d 1342 (1990) which stipulates that adjustments to base year rents are required in circumstances where base rent cannot reasonably be deemed to reflect general market condition.

b. City Council finds that actual average rent in the Park in 1982 was \$119 per space per month. City Council further finds that the initial average rent established in the Park in 1977 (\$119) was not set by general market conditions, but by conditions of entitlement approval which limited rents based on a rate of return of the initial investment of 11.5%. The initial average rent remained unchanged until 1984. Based on the appraisal prepared by James Brabant, dated November 19, 2010, the average market rent for the Park in 1979 was \$150 per space per month (Brabant appraisal at AR Part C, Tab 6.6: CTO 01353), and in 1982 projected comparable rent, as calculated by Dr. Baar, would have been \$178.50 per space per month. (Baar Report at AR Part C, Tab 6.5: CTO 01298)

c. City Council agrees with Dr. Baar that an adjustment of 1982 base year rent is necessary in order bring base year rents to a level representing general market conditions in 1982. (Baar Report at AR Part C, Tab 6.5: CTO: 01298)

d. City Council agrees with RAC that 1982 base year rents should be adjusted upward from \$119 per space per month to \$178.50 per space per month.

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)

b. Because the rents in this Park barely increased between 1982 and 2009, and an increase of management and administrative expenses during this period would have been inevitable, it is not reasonable to project management and administrative expenses as the same percentage (8%) of income in the base year (1982) and current year (2009) as outlined in Guideline § 2.11. It would be reasonable to project that administrative and management expenses increased by the CPI.

c. In this case, the Park Owner reported that 1982 total expenses were \$34,424, and 2009 total expenses were \$97,452. Therefore, operating expenses increased by 183% between 1982 and 2009 compared to

the 129.4% increase in the CPI. (Baar Report at AR Part C, Tab 6.5: CTO 01294-01295)

d. The Park Owner admitted that management tasks were performed by the Park Owner until 2006, when an off-site management company was employed to perform similar tasks. (Baar Report at AR Part C, Tab 6.5: CTO 01294)

e. Consequently, the transfer from owner management to management compensated by the owner is a change in how the cost is covered from an accounting perspective, and not a cost increase equal to the current cost.

f. Management and administrative expenses should be imputed to the base year 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.

g. Because of the gap in available information, 1982 operating expenses should be increased to a level which limits the rate of operating expense increases from 1982 to 2009 to the same rate of increase of the CPI as recommended by Dr. Baar. Under this approach, City Council agrees with RAC and finds that operating expenses should be adjusted from \$34,424 to \$42,555 in 1982. The basis for this computation is set forth in Dr. Baar's report (AR Part C, Tab 6.5: CTO and 01294-01295 and 01298).

h. City Council further finds that this adjustment to 1982 base year operating expenses offsets any overstatement of current year (2009) expenses for purposes of MNOI calculation. (Baar Testimony at AR Part E, Tab 27.1: CTO 02218-02219)

4. An Inflation Adjustment of Base Year Net Operating Income

a. Under § 5-25.06(b)(1) of the Ordinance, RAC 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 Part C, Tab 6.5: CTO 012990-01303)

c. Neither the Ordinance nor the Guidelines provides a rate of indexing base year net operating income to apply the MNOI standard.

d. City Council agrees with the findings in Dr. Baar's report (AR Part C, Tab 6.5: CTO 1304-01307) that the returns from a mobile home park investment may be attractive even 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.

e. 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

A. City Council agrees with RAC and finds that a \$191.95 per space per month rent increase represents a 144% increase over existing average rents (\$133). Such an increase, if implemented all at once, would represent a particular hardship on the tenants of the Park, many of whom are living on fixed incomes. Therefore, such an increase 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 seven-year period would alleviate this hardship while still providing the Park Owner a fair return (annual increases of \$27.42 per space per month). City Council also agrees that the phase-in should only apply to spaces occupied at the time the initial rent increase becomes effective.

B. In order to compensate Park Owner for the delay in implementing the full rent increase over a seven-year period, the Park Owner should be entitled to a 4% annual interest return on the delayed rent increase in addition to the annual rent increase. City Council finds that a 4% annual return represents an appropriate rate of return comparable to other investments of similar term and risk in the current interest rate environment and is above that 10-year treasury (risk free) rate of 3%.

SECTION 3. Decision.

Based on the findings in SECTIONS 1 and 2 above, City Council denies both appeals in their entirety and sustains the decision of RAC as set forth in Resolution RAC 09-2011. City Council further finds that RAC's decision as contained in Resolution RAC 09-2011 is in keeping with the purposes of the Ordinance.

SECTION 4. Authorized Rent Increase.

A. Amount of Increase

The Park Owner is entitled to, and is hereby granted, a rent increase of \$191.95 per space per month in order to obtain a just and reasonable return based on the findings in SECTION 2 above. The bases for this calculation are set forth in the 1982 Base Year Table of Dr. Baar's report (AR Part C, Tab 6.5: CTO 01309) and in the table below.

MNOI Fair Return Calculation

	Base Year (1982)	Current Year (2009)
Rental Income (excluding reimbursed utilities) With Base Year Rent Adjustment pursuant to MNOI analysis	\$158,508	\$117,920
Operating Expenses adjusted pursuant to MNOI analysis	\$42,555	\$97,452
Net Operating Income	\$115,953	20,468
Fair Net Operating Income (50% CPI Index) (64.7% Increase over Base Year NOI)		\$190,917
Gross Annual Rent Increase Required (Fair NOI – Actual Current Year NOI)		\$170,449
Rent Increase Required Per Space Per Month (Gross Annual Rent Increase divided by 12 months divided by 74 spaces)		\$191.95

B. Phasing of Rent Increase

1. This increase in rents shall be phased over a 7-year period (\$27.42 per space per month annually). This phase-in requirement shall only apply to spaces that are occupied at the time the initial rent increase becomes effective under subparagraph 3.

2. In order to compensate the Park Owner for the delay in implementing the full rent increase over a seven-year period, the Park Owner shall also be entitled to 4% annual interest on the delayed portion of the rent increase, which shall be amortized over the 7-year phase-in period, and in addition to the \$27.42 per space per month annual increase. In addition to the amount in Subsection 1 above, the Park Owner is therefore entitled to add the following Interest on Deferred Rent to the rent per space per month and increase the rent as shown below:

Year	Interest on Deferred Rent	Total Rent Increase
Initial increase	\$6.58 - (\$164.53x4%)	\$34.00
Second increase	\$5.48 - (\$137.11x4%)	\$32.90
Third increase	\$4.39- (\$109.69x4%)	\$31.81
Fourth increase	\$3.29- (\$82.27x4%)	\$30.71
Fifth increase	\$2.19 - (\$54.85x4%)	\$29.61
Sixth increase	\$1.10- (\$27.43x4%)	\$28.52
Seventh increase	\$0.00	\$27.42

3. The date of the initial increase in rent shall be no sooner than 90 days from the date formal notice of such increase is provided to the tenants, and the date of each subsequent increase shall not be sooner than 365 days from the date of the immediately prior increase.

PASSED AND ADOPTED this 24th day of May, 2011.



Andrew P. Fox, Mayor
City of Thousand Oaks, California

ATTEST:



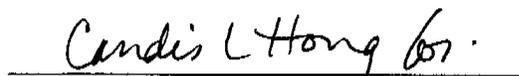
Linda D. Lawrence, City Clerk

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. 2011-025, which was duly and regularly passed and adopted by said City Council at a regular meeting held May 24, 2011, by the following vote:

AYES: Councilmembers Gillette, Glancy, Irwin, and Mayor Fox

NOES: Councilmember Bill-de la Peña

ABSENT: None

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



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

5/26/11

Date Attested