

## RESOLUTION NO. RAC 08-2011

### A RESOLUTION OF THE RENT ADJUSTMENT COMMISSION OF THE CITY OF THOUSAND OAKS APPROVING A JUST AND REASONABLE RETURN RENT INCREASE FOR THE THUNDERBIRD OAKS MOBILE HOME PARK.

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 rent increase of \$322.52 per space, per month; and

WHEREAS, on August 6, 2010, City staff deemed the application complete; and

WHEREAS, on August 16, 2010, City staff mailed notice to each mobile home owner or current resident of the Park that (1) a Just and Reasonable application had been filed, (2) the amount of the requested rent adjustment, (3) the date (originally October 5, 2010), time and place of the public hearing, and (4) where information regarding the application could be obtained; and

WHEREAS, on October 8, 2010, the Park Owner submitted an amended application requesting a "Vega" adjustment to the base year. The Vega adjustment was supported by an appraisal prepared by John Neet. The amended application requested a rent increase of \$260.62 per space, per month, and superseded the prior application.

WHEREAS, as a result of the amended application, on October 21, 2010, notice of the new hearing date was mailed to each mobile home owner or current resident of the Park; and

WHEREAS, on January 10, 2011, a public hearing was held before the Thousand Oaks Rent Adjustment Commission to consider the amended application. Evidence and testimony was submitted by City staff, the applicant, a representative of some of the tenants of Thunderbird Mobile Home 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.

NOW, THEREFORE, BE IT RESOLVED by the Thousand Oaks Rent Adjustment Commission ("Commission") as follows:

SECTION 1. Findings.

Based upon substantial evidence taken from testimony received at the hearing, both oral and written, the Commission makes the following findings:

A. The Application. The amended application with the Vega adjustment submitted by the Park Owner on October 8, 2010, was a substantial modification to the original application submitted on June 4, 2010, and therefore served as a submittal of a new application for purposes of compliance with any time frames required under the Ordinance.

B. Background regarding Thunderbird Mobile Home Park

1. The Park is subject to the City's Ordinance.
2. The current average monthly space rent in the Park is \$394.03. In addition to paying space rents, the tenants pay for gas, electricity, sewer, and trash expenses, but not water expenses. The average total utility cost for the residents of the Park is \$130 per month per space.

C. 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. The Commission 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 favor a maintenance of net operating income standard ("MNOI standard") for applications seeking "just and reasonable return." However, the Guidelines allow the Commission to consider other approaches.

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

5. The Commission finds that the MNOI standard is the best methodology for considering the Park Owner's application and meets the constitutional fair return standard.

D. Expert Analysis of MNOI standard. The City retained an expert on fair return issues, Dr. Kenneth Baar, to prepare a fair return analysis (Attachment #6 to Staff Report, pages 551-613) Based on Dr. Baar's resume (Staff Report, pages 605-613), the Commission 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.

E. Analysis under the MNOI standard. In order to perform a MNOI analysis a number of determinations must be made, including:

- The applicable base year.
- The amount of the base year rent,
- The amount of the base year operating expenses,
- The inflation adjustment factor applied to the base year net operating income in order to determine what net operating income is a fair net operating income in the current year,

1. Designation of the Base Year.

a. The Guidelines state that the base year shall be 1979 when the financial information for that year is available, and when 1979 information is not available the first year for which a park owner has financial records may be used as a base year. (RAC-2, Secs. 3 and 4.)

b. The Guidelines also vest in the Commission the discretion to consider a base year other than 1979 for good cause. (RAC-5, Sec. 3.07)

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.

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, the Commission 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 Commission 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 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 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." (RAC-2, Sec. 2.05)

b. 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. (RAC-2 Sec. 3.05)

c. The Commission finds that the reasonable interpretation of the intent of these terms 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.

d. In this case, complete information on rent increases was limited to the period from 1983 to 1986.

e. 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. This increase compares with the total of 21% in rent increases authorized in 1984, 1985, and 1986. This difference provides the basis for a "Price Level Adjustment."

f. 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%). 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. The error in the estimate of the difference between actual rent increases between 1980 and 1983 and the maximum permitted increases may be substantial relative to the six percent difference (18% versus 24%). Under these circumstances, a "price level adjustment" for this period is not justified.

g. For the purposes of the MNOI analysis the 1986 base year rent is adjusted from \$273 to \$298 per space per month, resulting in an adjusted annual park rental income of \$575,736 (Staff Report, Attachment # 6 at pg. 597)

h. The Commission finds that the Price Level Adjustment above adequately provides the Park Owner an approximation of market rents 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. (RAC-2, Sec. 2.11)

b. In this case, the Park Owner reported that 1986 management and administration expenses totaled \$30,878; 5.9%% of rental income, and in 2009 management and administration expenses totaled \$167,392; 21.9% of rental income.

**Management and Administration Expenses  
Set Forth in Rent Increase Application**

Year		Mgmt & Adm. Expense	Pct. of Gross Rent
1986		30,878	5.9%
2009		167,392	21.9%

c. For the period 1986 to 2009, the Park Owner projected an increase of 442% in administration and management expenses, compared to the CPI increase of 99% during this period.

d. The Park Owner has indicated that the performance of management and administration tasks have been transferred from being performed personally by the owners to being performed by third parties who were paid.

e. For the reasons set forth in Dr. Baar's written analysis (Staff Report, Attachment #6 at pg 580), the Park Owner did not present convincing evidence that a higher level of effort and expenditure was required in order to perform management and administration in 2009 compared to 1986.

f. 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.

g. 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.

h. The Commission concludes that it is not reasonable to use the 8% management and expense cap in RAC-2, Sec. 2.11 for the reasons stated in Dr. Baar's report (Staff Report, Attachment #6 at pg. 581.)

i. In calculating the amount of the imputed management and administrative expense for 1986, it is reasonable to assume that management and administration costs increased by the same percentage as the CPI between the base year and the current year in order to maintain the same level of service. This assumption is more favorable to the Park Owner than the assumption in the Guidelines that management and administration expenses were the same percentage of rental income in 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. The result of this assumption is that in order to calculate base year management and administration expenses, current year management and administration expenses are adjusted downward by a greater amount (the CPI difference), rather than the difference in rental income. 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 assuming that management and administration expenses were the same percentage of rental income in the base year and the current year.

j. The Commission finds that 1986 management and administration expenses as imputed totaled \$84,117, as opposed to the \$30,878 amount claimed by Park Owner. The basis for this computation is set forth in footnote 75 of Dr. Baar's report (Staff Report, Attachment #6 at pg. 580), which is adopted and incorporated into this resolution by reference.

k. For the purposes of the MNOI analysis, the Commission finds that the total 1986 base year operating expenses are projected to be \$207,054. The basis for this computation is set forth in Table 1 of Dr. Baar's report (Staff Report, Attachment #6 at pg 592), which is adopted and incorporated into this resolution by reference.

### 3. An Inflation Adjustment of Base Period 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 since the base year.

c. Contrary to the Park Owner's expert, who contends that NOI would eventually become zero unless a 100% indexing were used, by definition, the MNOI standard provides that rent increases must be authorized to cover all cost increases and provide a higher net operating income than the base period net operating income. Therefore, it is a logical impossibility that NOI could ever be zero.

d. The Guidelines do not provide a rate of indexing for the MNOI standard.

e. The Commission adopts the findings in Dr. Baar's report (Staff Report, Attachment #6 at pages 586-589) 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 growth in income in an investment that typically is low-risk with a steady and consistent income stream.

f. The Commission concludes that indexing the net operating income by 50% of the percentage increase in the CPI provides a "just and reasonable return" to the Park Owner.

## SECTION 2. Authorized Rent Increase.

A. The Park Owner is entitled to 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 Table 3 of Dr. Baar's report (Staff Report, Attachment #6 at pg. 597) 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

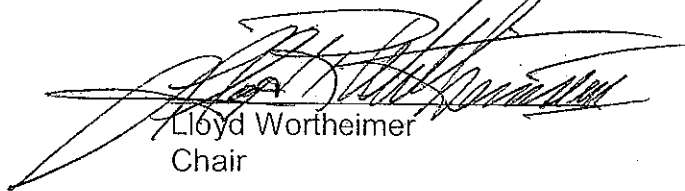
Rent Increase Required (Fair NOI – Actual Current Year NOI)		\$119,868
Rent Increase Required PerSpace Per Month (Parkwide Rent Increase/(161 spaces x 12 months))		\$62

B. 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.

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PASSED AND ADOPTED this 18th day of January, 2011.

**THOUSAND OAKS RENT  
ADJUSTMENT COMMISSION**




Lloyd Wortheimer  
Chair

ATTEST:

  
\_\_\_\_\_  
Recording Secretary

APPROVED AS TO FORM:

  
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Patrick Hehir, Assistant City Attorney