

SANTA MONICA RENT CONTROL BOARD ADMINISTRATION MEMORANDUM

DATE: May 1, 2008
TO: Santa Monica Rent Control Board
FROM: Tracy Condon, Administrator
FOR MEETING OF: May 8, 2008 and Public Hearing on June 5, 2008
RE: 2008 Annual General Adjustment
Apartment Operating Cost Increases (March 2007 - March 2008)

Summary

The recommended annual general adjustment for 2008 is 2.7%. It is based on actual increases in various expense components of the rent dollar using a formula of the “component ratio to gross rent”, or what is also referred to as the “pie” methodology (because each individual category of expense was assigned a portion or “slice” of the total rent dollar).

This year’s recommended general adjustment looks at operating expense increases from March 2007 to March 2008. Components accounting for more than 70% of the rent dollar are adjusted based on the increases in the consumer price index for the Los Angeles-Anaheim-Riverside area. The remaining components (28.76% of the rent dollar) are not tied directly to the CPI but are adjusted based on a variety of methods including actual rate changes and set percentages.

Recommendation

Staff recommends that the Rent Control Board set a public hearing on June 5, 2008 for consideration of a 2.7% General Rent Adjustment. It is also recommended that the Board agendaize for a future meeting, consideration of an alternative methodology to calculate the annual general adjustment as a percentage of the CPI. (See pages 17-18 for additional information on this recommendation.)

Note: Units with market rate increases implemented from September 1, 2007 through August 31, 2008 are not eligible for the 2008 general adjustment. Recent market rate rentals will have taken operating cost increases into account when establishing a new rental rate.

Methodology

The 2008 General Adjustment Report was prepared using the methodology and survey data previously developed by Dr. Kenneth Baar. At the direction of the Board, Dr. Baar developed a methodology for calculating the annual General Adjustment with the following features:

1. Division of the rent dollar into categories of expense, including “hard expenses” (taxes, utilities, City services), and “calculated expenses” (management, maintenance and other operating costs, and net operating income).
2. Identification of the “component ratio to gross rent” by dividing the dollar amount of each component of the rent dollar for the hypothetical average apartment by the total rent dollars. These ratios represent the percentage of the average rent dollar devoted to each expense category. See Tables A and B, pages 14 and 15.
3. Survey of utility companies and government agencies to determine actual increases (or decreases) in costs to property owners in the last year.

For this report, staff collected data from Southern California Gas, Southern California Edison, the U.S. Bureau of Labor Statistics and the City of Santa Monica (Water Department, Solid Waste Department and Fire Department).

In 2002, Dr. Baar prepared the General Adjustment Report for the Board. Dr. Baar analyzed various approaches to calculating the general adjustment and also completed an extensive review of the components currently used to determine the general adjustment. Dr. Baar’s report recommended some modifications to several of the components. Beginning in 2003, subsequent General Adjustment Reports incorporated many of the modifications recommended by Dr. Baar.

Calculation of the 2008 General Adjustment

Many of the components which make up the rent dollar are affected by increases in the Consumer Price Index in the Los Angeles Area. Following are the increases for the various indices used in this year's general adjustment report:

<u>March 2007 – March 2008</u>	CPI for All Urban Consumers: 3.3% increase CPI for All Urban Consumers – All items less shelter: 3.1%
<u>February 2006– February 2007</u>	CPI for Urban Wage Earners and Clerical Workers: 3.4%

The components increased by the CPI for All Urban Consumers (3.3%) are self labor, cash flow and management costs. (Management is ultimately adjusted to 5% of the rent dollar after the general adjustment is calculated.) The components increased by the CPI “less shelter” (3.1%) are maintenance and insurance. The water and sewer component is adjusted by the February-February increase in CPI for urban wage earners and clerical workers pursuant to a current Santa Monica City Ordinance. The remaining components, including property taxes, refuse, water and sewer, gas, electricity and Fire and Life Safety Inspections, are based on either established set increases or actual changes in rates. Details for each component follow.

Component Calculations

Property Taxes

Property tax increases post-Proposition 13 are limited to a 2% increase per year, except when properties are reassessed to market value, which occurs upon a transfer. Staff typically uses the 2% limit in calculating the property tax component of the rent dollar. To use an average of property tax increases due to transfers each year would substantially over-compensate owners of properties which have not been sold, as those owners continue to operate with property tax bills which typically increase by no more than 2%. Increases significantly greater than 2% were used in 1989, 1992 and again in 2002. In 2002 the increase used was 28.6% and was based on Dr. Baar's analysis of property tax bills for a random sample of 272 properties. The significant increase was related to a reassessment of properties that transferred ownership since 1995, when vacancy decontrol was enacted statewide.

Following the significant increase in this component in 2002, staff has been using 2% for the property tax component in the general adjustment. The table below reflects the 2% increase projected for 2008.

Year	Average Monthly Property Tax Bill Per Unit
1978	\$19.20
2001	44.74
2002	57.53
2003	58.68
2004	59.85
2005	61.05
2006	62.27
2007	63.52
2008	64.79

	2007 Average Monthly (per unit) Property Tax Bill	Rate Increase 2007-2008	Cost Increase Apt./Month	Estimated 2007 cost
Property Tax	\$63.52	2%	\$1.27	\$64.79

Refuse Collection

Refuse collection charges consist of fixed charges per apartment and collection fees dependent upon the type of refuse container and the frequency of collection.

There are several types of containers and various options as to the frequency of collection. Over the years, the Rent Control Board has reviewed refuse bills for a variety of apartment buildings and has calculated average expenditure levels. The “typical” configuration (type of refuse container and frequency of pick-up) used for this report is based on a ten-unit building using two 2-yard bins picked up once a week.

Between 1999 and June 2004, the fixed charge (monthly fee per apartment) did not vary and held at \$3.00. In 2005 and 2006 the rates were increased effective July 1 of each year to \$3.30 and \$3.53, respectively. Effective July 1, 2007, the monthly rate was set at \$3.65 which reflects a 3.4% increase. Collection rates were also increased by 3.4% effective July 1, 2007¹. The table shows the impact of the rate increases on the overall cost for a hypothetical typical apartment.

Monthly Refuse Collection Charges Per Apartment
(Hypothetical 10 Unit Building)

	<u>Monthly Fee per Apartment</u>	<u>Bin Charge</u>	<u>Total Bill</u>
April 2004	3.00	11.20	14.20
April 2005	3.00	11.40	14.40
April 2006	3.30	12.54	15.84
April 2007	3.53	13.42	16.95
April 2008	3.65	13.88 ¹	17.53

The difference between the 2007 total bill calculated as \$16.95 and the projected cost of \$17.53 for 2008 reflects a 3.4% increase.

	2007 Average Monthly Cost Per Apt. Unit	Percent Cost Increase 2007-2008	Cost Increase Apt./Month	Estimated 2008 cost
Refuse Collection	\$16.95	3.4%	\$0.58	\$17.53

¹ The rate for the class MSQ - one 2-yard bin picked up once weekly was increased from \$134.18 to \$138.74 per two month period. The analyses developed by staff assume two bins for such a ten-unit building, resulting in a cost of \$138.74 per month or \$13.88 per unit/per month.

Fire and Life Safety Inspection Fee

This component was added for the first time in the 2005 general adjustment calculation. Fire and Life Safety Inspections are required of all apartment buildings in Santa Monica. Since January 2004, property owners have been charged a fee for the inspection. The 2005 annual cost of the inspection was a flat fee of \$60 per building.² The average number of units per building used in the Board’s General Adjustment Reports is six units per building. Therefore, a monthly per unit cost of \$0.83 per unit (\$60 divided by 6 units divided by 12 months) was set in 2005 and established the “base” cost for this component. The fee has not changed and the 2008 cost for this component remains \$0.83 per unit.

	2007 Cost Per Apt. Unit	Cost Increase Apt./Month	Estimated 2008 cost
Average Fire & Life Safety Inspection Expense	\$0.83	\$0.0	\$0.83

Water and Sewer

Water and sewer charges are considered together, as the costs for both are made up of usage fees related to water consumption and meter charges based on the size of the water meter. Two factors influence the average water/sewer costs used in the general adjustment calculation: water consumption and actual water and sewer rates.

Water Consumption

Staff has monitored water consumption over the years, as consumption is directly related to actual water and sewer costs. Since 1997, staff has tracked water consumption rates and water/sewer and refuse costs on two sets of randomly selected properties. (Tracking began on one set of properties in 1992.) This research has led to some modifications over the years to the average consumption rate (measured in HCF – hundred cubic feet). The 1999/2000 General Adjustment Report modified the average consumption rate to 4.6 HCF which reflected a reduction in consumption. Staff used 4.6 HCF as the average consumption rate until 2006. In the 2006 General Adjustment Report, staff found that an upward adjustment to the average consumption rate was warranted and increased the rate to 4.85 HCF.

This year, staff again reviewed the water consumption rates and costs of water/sewer and refuse bills for the two sets of properties. Currently, the two sets include 55 and 73 properties. Staff believes these properties provide a good representation of water consumption in controlled rental units.

² City Council resolution 9858 adopted on June 17, 2003 established the fees.

The table below shows the average water consumption for the two groups of properties tracked since 1997.

Water Consumption Table

Year*	Avg. HCF 1 st Group	Avg. HCF 2 nd Group
1997	4.83	4.56
1998	4.65	4.54
1999	4.66	4.51
2000	4.65	4.34
2001	4.77	4.42
2004	5.30	4.61
2005	5.04	4.52
2006	4.96	4.68
2007	5.00	4.71
2008	4.81	4.64

*The study was not performed in 2002 and 2003.

In 2006, the average consumption rate used to calculate average water and sewer costs was raised from 4.6 HCF to 4.85 HCF. As shown above, the average HCFs for both groups (4.81 HCF – first group and 4.64 HCF second group) reflect a slight decrease in consumption over the averages for the groups last year. The combined average of both groups for 2008 is 4.71 HCF. The combined average for the two groups of properties from 2004 through 2008 is 4.83 HCF. At this time, the data continues to support the use of 4.85 HCF as the average consumption rate and the water and sewer costs projected for 2008 are based on that average. If, over the course of time, the rate of water consumption continues to decrease, staff will adjust the average consumption rate accordingly.

Water and Sewer Average Costs

Pursuant to City Council Resolution (CCS) 9409, increases in water and sewer rates have been tied to increases in the CPI for Urban Wage Earners and Clerical Workers from February to February of each year.³ In 2007, the City’s Water Department relied on the February 2006 to February 2007 CPI for Urban Wage Earners and Clerical Workers to establish a new rate structure effective July 1, 2007. The CPI reported a 3.4% increase for that time period. The Water Department increased the water and sewer rates by 3.4% effective July 1, 2007.

³ CCS No. 9409 (Sec. 4 June 22, 1999) (establishing an Annual Consumer Price Index Increase on Water Rates and Fees).

The table below sets out the combined water and sewer expenses. The 2007 and 2008 costs reflect the use of 4.85 HCF as the average rate of consumption. The water and sewer expense for 2008 has been projected using the 3.4% CPI increase.

	2007 Average Monthly Cost Per Apt. Unit	Overall Percent Cost Increase 2007-2008	Cost Increase Apt./Month	Total Estimated 2008 cost
Water/Sewer Expense	\$22.74	3.4%	\$0.77	\$23.51

On April 22, 2008, during a study session with the City Council, the City’s Water Department presented alternate proposals for possible rate changes. The proposals seek a change in the rate structure for both sewer and water rates, which if adopted, would result in rate changes effective August 2008 (projected date). Generally, adjustments in the various components used in the Board’s General Adjustment Reports are based on changes over the prior twelve months, rather than on increases/decreases proposed for the future. If new rate structures are implemented, the effect of those changes will be considered in future general adjustment reports.

Gas – Common Areas Only

Average Costs

In more than two-thirds of all apartments, the apartment owners pay for hot water heating through master metered service, while the tenant usually pays for gas heat for the unit on an individual meter.

In the 2002 General Adjustment Report, Dr. Baar recommended modification of the average gas component to equal \$9.62.⁴ Per Dr. Baar’s recommendation, the 2003 General Adjustment Report modified the gas expenditure for 2002 to equal \$16.03 (\$9.62 gas cost plus 10% tax and other incidental costs gas users are required to pay) and projected the costs for 2003 using \$16.03 as the base with an average use of 16.036 therms. Staff continues to use the average of 16.036 therms to project any changes to the average gas expense component.

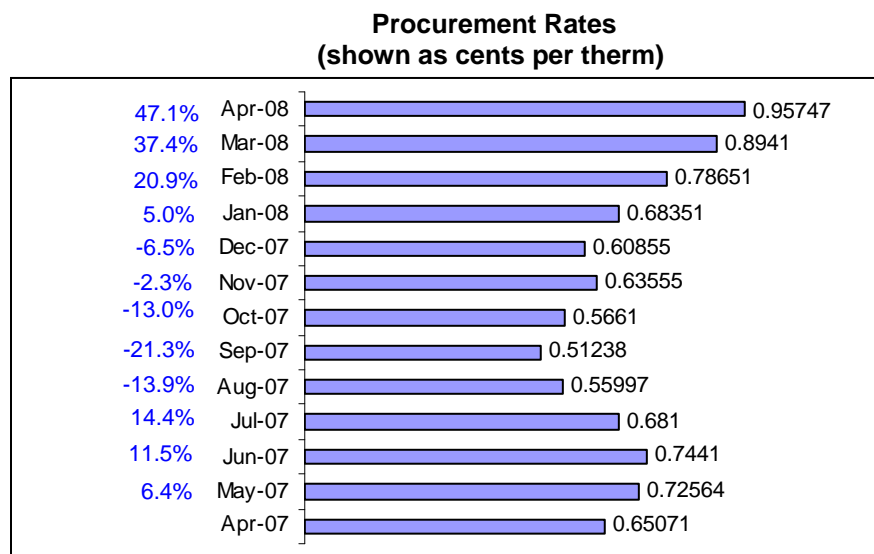
To determine changes in the gas cost, staff has used one of two methods. One method was to look at the difference between the gas cost per therm in April of the previous year and April in the current year to determine the increase or decrease for this expense. In recent years, staff has used an average of gas costs in a twelve month period to calculate changes in gas rates. The cost of gas is based on two components, the procurement cost, which changes monthly, and the transmission charge, which remains constant throughout the year. The

⁴ His recommendation was based on the results of a survey of average cost data from Southern California Gas for the period April 2001 through March 2002. The data consisted of a random sample of 258 buildings with 3369 apartment units and indicated the average monthly cost for gas was \$9.62 per apartment unit. Dr. Baar recommended that if no other data could be developed, the gas component should be modified to reflect the \$9.62 average cost.

monthly changes to the procurement rate can result in widely varying costs from month to month. The pattern of rate changes that occurs over a twelve month period is a factor in determining which method is more appropriate to use. In 2005, 2006 and 2007 staff determined it was more appropriate to use an average of gas costs, as the monthly procurement rates varied so widely during the twelve month period ending in April for each of those years.

Although the monthly procurement rates have become somewhat more stable, there were significant rate variations during the twelve months ending in April 2008 as shown on the table below. For this reason, staff has again used the average of gas costs for a twelve-month period to estimate the cost for 2008.

Last year the monthly procurement rates from April 2007 back through May 2006 ranged from a high of \$0.73 in March 2007 to a low of \$0.41 in October 2006. Currently, the monthly procurement rates from April 2008 back through May 2007 range from a high of \$0.96 in April 2008 to a low of \$0.51 in September 2007. As was the case last year, the percent increase for each of the last twelve months beginning with April 2008 as compared to April 2007 has also varied greatly, from a low of 13.9% below the April 2007 rate to a high of 47.1% above the April 2007 rate. The following graph demonstrates the pattern of procurement rate changes as compared to April 2007. The percentages in blue on the left side show the % changes.



The twelve month average procurement cost from April 2008 back through May of 2007 is .696240. The annual transmission charge for this period is .291270. The total monthly cost per therm is .987510 (.696240 + .291270). This is the amount used to calculate the estimated cost for gas for 2008. This amount is .091537⁵ cents per therm more than last year's per therm cost and will result in an overall increase in the estimated cost for 2008. The 2008 estimated cost is shown in the table that follows.

⁵ 2008 per therm cost of \$0.987510 less 2007 per therm cost \$0.895973

Common Area Gas Expense

	2007 Average Monthly Cost per Apt. unit	Rate Change 2007-2008	Cost Increase Apt./Month	Estimated 2008 cost
Common area average gas expense	\$22.11 ⁶	7.4%	\$1.64	\$23.75 ⁷

Electricity – Common Areas Only

From June 1996 through 2000, electricity rates were frozen at the 1996 rate levels. In 2001, the Public Utilities Commission authorized a significant increase in rates which was reflected in the 2001 general adjustment report. By 2002, that exceptional rate increase had been rolled back. In Dr. Baar's 2002 general adjustment report, the average cost for electricity was also rolled back which reset the average monthly cost per unit for common area electricity back to \$10.68. The general adjustment reports for 2003 and 2004 did not project any additional changes to this component.

On April 11, 2005 Southern California Edison issued Regulatory Advice letter #1886-E. That letter made reference to Assembly Bill (AB)1X which required a roll-back to the February 2001 rates for Tier 1 (baseline) and Tier 2 (non-baseline level 1). The February 2001 rates were set at 11.808 per kWh (baseline, Tier 1) and 13.741 per kWh (Tier 2). The rates for Tiers 1 and 2 have been limited to the 2001 levels from 2005 through the present. Advice letters 2220-E and 2225-E filed by Southern California Edison in February and March of this year confirm that the rates for Tiers 1 and 2 remain limited to the 2001 levels. Per a representative of Southern California Edison, as of April 2008, the rates for Tiers 3 and 4 have decreased slightly. However, decreases on the higher tiers do not impact the monthly cost for this component, as only Tiers 1 and 2 are used in the analysis.

Consumption

For purposes of this report, staff has used a consumption level for electricity of 1638 kWh per month for a 6-unit building which includes electricity usage for the common areas as well as within the six units.⁸ Of the 1638 kWh, 1140 hours are billed at baseline rates, and 498 hours billed at non-baseline rates. The non-baseline rates are calculated using the lowest level of the non-baseline rate schedule which is Tier 2.

⁶ April 2007 Cost \$15.81 (16.036 therms x .895973 baseline rate = \$14.37 + \$1.44 [10% tax]) + incidentals \$6.30 (daily service rate [30 days x .16438] + State Regulatory Fee [16.036 therms x .00076] + Low Income Discount Rate Surcharge [16.036 therms x .0491] = \$5.73 + \$0.57 [10% tax]) = **Total cost \$22.11.**

⁷ April 2008 Cost \$17.42 (16.036 therms x .987510 baseline rate = \$15.84 + \$1.58 [10% tax]) + incidentals \$6.33 (daily service rate [30 days x .16438] + State Regulatory Fee [16.036 therms x .00068] + Low Income Discount Rate Surcharge [16.036 therms x .05074] = \$5.75 + \$0.58 [10% tax]) = **Total cost \$23.75.**

⁸ These consumption levels have been used in prior general adjustment reports and are based on a 1983 Southern California Edison survey which showed consumption level for electricity in a 6-unit building to be 1638 kWh per month.

Average Costs

In order to determine the rate of increase (or decrease) for this component, staff uses the average cost for electricity per unit in a six unit building, including the cost for usage within apartments as well as common areas. The amounts for common areas alone are relatively small. Thus, the larger figure provides a more stable basis for determining the rate of increase or decrease. The resulting rate change is then applied to the monthly per unit cost of the common area usage.

The table below shows the average cost per unit including both common areas and individual units in a six unit building. As of 2005, the rates for Tier 1 (baseline) and Tier 2 (non-baseline) were fixed at the February 2001 levels pursuant to AB1X. The rates for Tier 1 (baseline) and Tier 2 (non-baseline) remain fixed for 2008. Therefore, no increase is projected for this component for 2008. The projected average cost for 2008 remains at \$37.24.

Electricity Rates for Apartment Owners
with Individually Metered Units (per kWh)

	<u>Baseline</u>	<u>Non-Baseline</u>	<u>Avg. Cost</u>
April 1978	3.2	4.2	\$ 10.80 ⁹
June 1996-April 2000	12.0	14.2	38.03 ¹⁰
April 2001	13.0	19.66	52.10
April 2002-2004	12.0	14.2	38.03
April 2005	11.808	13.741	37.24
April 2006	11.808	13.741	37.24
April 2007	11.808	13.741	37.24
April 2008	11.808	13.741	37.24 ¹¹

The following table shows the 2007 cost for common area usage and reflects no change in rates for 2008. The estimated 2008 unit cost for common area usage remains at \$10.46.

	2007 Average Monthly Cost per Apt. unit	Rate Change 2007-2008	Cost Change Apt./Month	Estimated 2008 unit cost
Common area average electricity expense	\$10.46	0%	\$0.00	\$10.46

⁹ Original bill of \$10.29 + 5% tax = \$10.80

¹⁰ $1140 \times .12009/6 = \$22.82 + 498 \times .14174/6 = \11.75 ; $\$22.82 + \$11.75 = \$34.57 \times 10\% \text{ tax} = \38.03 .

¹¹ $1140 \times .11808/6 = \$22.44 + 498 \times .13741/6 = \11.41 ; $\$22.44 + \$11.41 = \$33.85 \times 10\% \text{ tax} = \37.24 .

Maintenance and Other Operating Expenses

Information for this expenditure specific to Santa Monica is not available.¹² Therefore, the Board adjusts this category by the change in the Consumer Price Index, less shelter. The March 2007 – March 2008 percent increase for this index was 3.1%. The effect of this increase on the maintenance component is shown below:

	2007 Average Monthly Cost Per Apt. Unit	CPI all items less shelter Pct. Increase	Cost Increase Apt./Month	Estimated 2008 Cost
Maintenance	\$108.70	3.1%	\$3.37	\$112.07

Insurance

Since 1998, the Board has used the change in the Consumer Price Index, less shelter to calculate the annual increase for this component.¹³ The March 2007 – March 2008 percent increase for this index was 3.1%. The effect of this increase on the insurance component is shown below:

	2007 Average Monthly Cost Per Apt. Unit	CPI all items less shelter Pct. Increase	Cost Increase Apt./Month	Estimated 2008 Cost
Insurance	\$30.98	3.1%	\$0.96	\$31.94

Self Labor

The Board uses the change in the Consumer Price Index for All Urban Consumers to adjust the self labor component for purposes of calculating the annual general adjustment. The March 2007 – March 2008 percent increase for this index was 3.3%. The effect of this increase on the self labor component is shown below:

	2007 Average Monthly Cost Per Apt. Unit	CPI all items Pct. Increase	Cost Increase Apt./Month	Estimated 2008 Cost
Self Labor	\$54.95	3.3%	\$1.81	\$56.76

¹² For the 2002 report, Dr. Baar obtained data from Apartment Industry Sources for the Los Angeles area for the year 2000. The data indicated the costs for maintenance and other expenses per unit ranged from \$68 - \$126. Although this information was not specific to Santa Monica, the monthly cost used by the Board for this component falls within that range.

¹³ In 1997, the Board commissioned Thomas D. Stringer of Stringer Appraisals to prepare a report on insurance costs. Based on that report and other information gathered by the Board, staff separated the insurance component from the maintenance component and set the average monthly cost per apartment at \$23.96. The component was again adjusted in 1998 based on a subsequent report by Mr. Stringer.

Cash Flow Adjustment

The Board uses the change in the Consumer Price Index for All Urban Consumers to adjust the cash flow component for purposes of calculating the annual general adjustment. The March 2007 – March 2008 percent increase for this index was 3.3%. The effect of this increase on the cash flow component is shown below:

	2007 Average Monthly Cost Per Apt. Unit	CPI all items Pct. Increase	Cost Increase Apt./Month	Estimated 2008 cost
Cash Flow	\$265.80	3.3%	\$8.77	\$274.57

Management

Management costs are fixed at 5% of gross rent pursuant to Rent Board Regulation 4101(c)(1). For purposes of calculating the annual general adjustment, the Board uses the change in the Consumer Price Index for All Urban Consumers. The March 2007 – March 2008 percent increase for this index was 3.3%. The effect of this increase on the management component is shown below:

	2007 Average Monthly Cost Per Apt. Unit	CPI all items Pct. Increase	Cost Increase Apt./Month	Estimated 2008 Cost
Management	\$37.98	3.3%	\$1.25	\$39.23

Table A

**Calculation of Annual General Adjustment
Percentage and Dollar Amounts**

Rent Increases Required to Cover Operating Cost Increases and Index Cash Flow

Operating Expense	2007 ratio to gross rent (a)	Estimated cost 2007*	Percent increase 2007-2008 (b)	Percent Increase Required (a) x (b)	Estimated cost 2008 (c)	Rent Adjustment required (d)
Property Taxes	0.0836	\$63.52	2.0%	0.1673%	\$64.79	\$1.27
Refuse	0.0223	16.95	3.4%	0.0759%	17.53	0.58
Fire & Life Safety Inspection Fee	0.0011	0.83	0.0%	0.0000%	0.83	0.00
Water & Sewer	0.0299	22.74	3.4%	0.1018%	23.51	0.77
Gas	0.0291	22.11	7.4%	0.2154%	23.75	1.64
Electricity	0.0138	10.46	0.0%	0.0000%	10.46	0.00
Maintenance	0.1431	108.70	3.1%	0.4437%	112.07	3.37
Insurance	0.0408	30.98	3.1%	0.1264%	31.94	0.96
Self Labor	0.0723	54.95	3.3%	0.2387%	56.76	1.81
Debt Service	0.1639	124.51	0.0%	0.0000%	124.51	0.00
Cash Flow	0.3500	265.80	3.3%	1.1548%	274.57	8.77
Management	0.0500	<u>37.98</u>	3.3%	0.1650%	<u>39.23</u>	<u>1.25</u>
Totals		\$759.53		2.69%	\$779.95	\$20.42

*The amounts reflect the 2.3% general adjustment authorized by the Board in 2007 and an adjustment to Management to reflect 5% of the total cost.

Table B

**Calculation of Annual General Adjustment
Percentage and Dollar Amounts rounded to 2.7%**

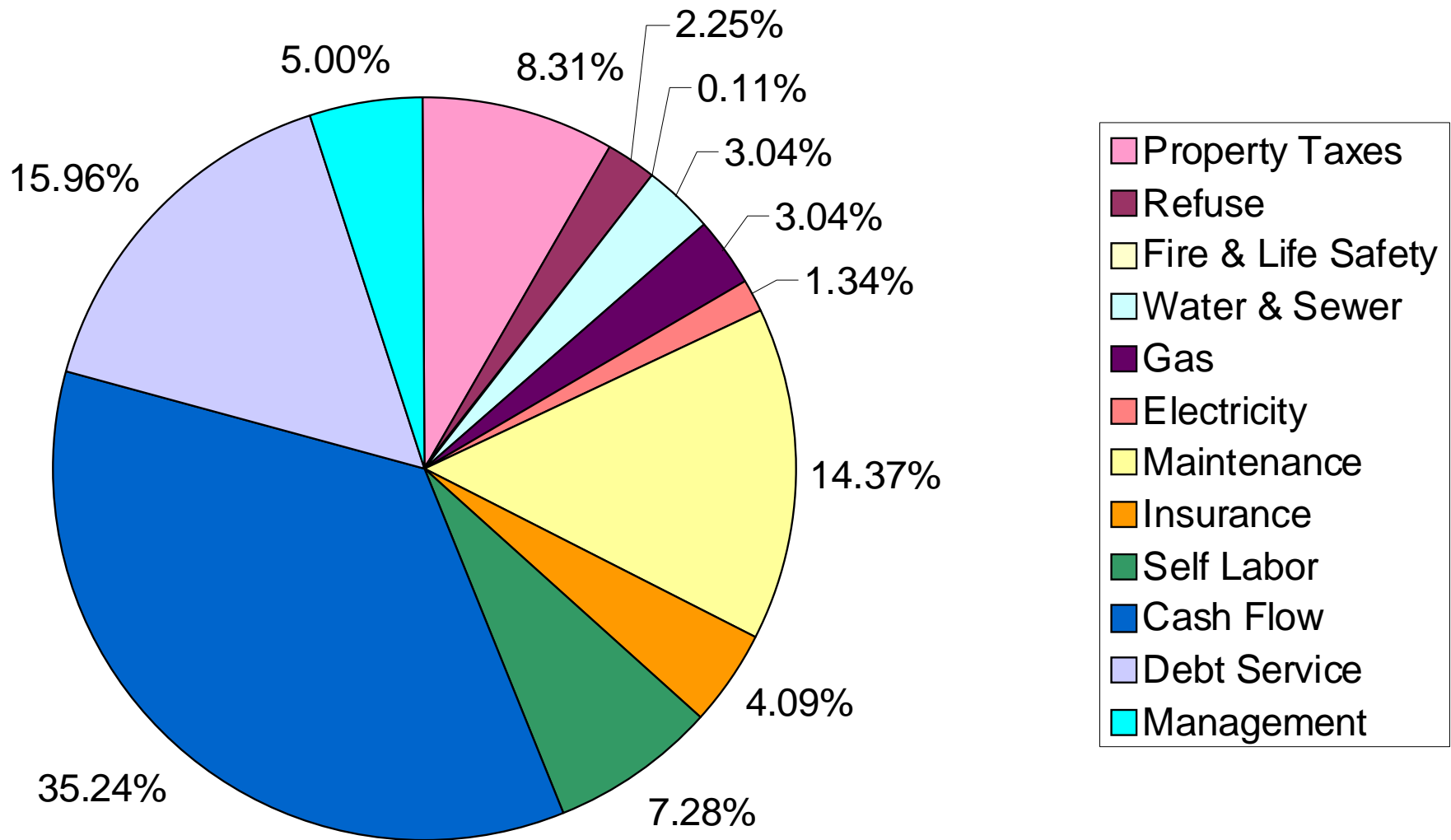
Rounding to 2.7% is accomplished by adjusting management cost to equal 5% of the total rent* and then adjusting cash flow to accommodate the change. The percent increases shown below for cash flow and management are the adjusted figures.

Rent Increases Required to Cover Operating Cost Increases and Index Cash Flow

Operating Expense	2007 ratio to gross rent (a)	Percent increase 2007-2008 (b)	Percent Increase Required (a) x (b)	Estimated cost 2008 (c)	Rent Adjustment required (d)
Property Taxes	0.0836	2.0%	0.1673%	\$64.79	\$1.27
Refuse	0.0223	3.4%	0.0759%	17.53	0.58
Fire & Life Safety Inspection Fee	0.0011	0.0%	0.0000%	0.83	0.00
Water & Sewer	0.0299	3.4%	0.1018%	23.51	0.77
Gas	0.0291	7.4%	0.2154%	23.75	1.64
Electricity	0.0138	0.0%	0.0000%	10.46	0.00
Maintenance	0.1431	3.1%	0.4437%	112.07	3.37
Insurance	0.0408	3.1%	0.1264%	31.94	0.96
Self Labor	0.0723	3.3%	0.2387%	56.76	1.81
Debt Service	0.1639	0.0%	0.0000%	124.51	0.00
Cash Flow	0.3500	3.4%	1.1968%	274.89	9.09
Management	0.0500	2.7%	0.1345%	<u>39.00</u>	<u>1.02</u>
Total Rent Increase			2.70%	\$780.04	\$20.51

*Management costs are fixed at 5% of gross rent pursuant to Rent Board Regulation 4101(c)(1)

2008 Rent Dollar Components



Alternate Methodology

The net result of the “component ratio to gross rent analysis” is a general adjustment calculation of 2.69% which staff recommends the Board round to 2.7%. Most California jurisdictions which have rent control ordinances calculate their annual rent increases based on percentage increases in the CPI as shown in Chart A below. A majority of the components currently used in the Board’s general adjustment analysis rely on the CPI index as shown in Chart B. The chart reflects the 2008 rent dollar components based on the recommended 2.7% general adjustment. For 2008, 71.27% of the rent dollar is adjusted by the CPI, while 28.73% of the rent dollar is not tied to CPI.

Appendix 1 presents a comparison of the general adjustments authorized by the Board since 1979 and the percentage of CPI increase for that time period. The total of all general adjustment increases authorized from 1979 through 2007 is 95.65% which is 75.55% of the total CPI increases for the same time period (126.6%). There is only a difference of .7% between the total of all the general adjustments authorized (95.65%) and 75% of the total CPI figures beginning in 1979 (94.95%). Using a percentage of the CPI, rather than the current “pie” methodology, could be an alternative method of calculating the annual general adjustment.

Chart A

Annual Rent Increase Standards under California Apartment Rent Control Laws

<u>Jurisdiction</u>	<u>Annual Rent Adjustment</u>	<u>2008 GA</u>
Berkeley	65% of CPI	2.2% January 2008
Beverly Hills	CPI (12 mo. total, year-to-year % change)	3.6% March 2008
East Palo Alto	CPI (lower of all-items & rent residential index)	Not available yet – September 2008
Hayward	5%	5.0% April 2008
Los Angeles	CPI (12 mo. average, year-to-year % change)	3.0% July 2008
Oakland	CPI (12 mo. avg. all-items & less shelter, year-to-year % change)	3.2% July 2008
San Francisco	60% of CPI	2.0 % March 2008
San Jose	8%	8.0% Annually
West Hollywood	75% of CPI	Not available yet – September 2008

Chart B

CPI and non-CPI adjusted Components for 2008 recommended General Adjustment of 2.7%

<u>Components Adjusted by CPI</u>	<u>Operating Cost Weight</u>	<u>Measure of Cost Increase</u>
Water & Sewer	3.04%	Rates determined by CPI (all items)
Refuse	2.25%	Rates determined by CPI (all items)
Maintenance	14.37%	CPI all items less shelter
Insurance	4.09%	CPI all items less shelter
Self Labor	7.28%	CPI all items
Cash Flow	35.24%	CPI all items
Management	<u>5.0%</u>	CPI all items
	71.27%	Total adjusted by CPI

<u>Components Not Adjusted by CPI</u>	<u>Operating Cost Weight</u>	<u>Measure of Cost Increase</u>
Property Tax	8.31	2% per year or actual increases
Fire & Life Safety	0.11	Rates set per City Council Resolution
Gas	3.04	Southern California Gas Co.
Electricity	<u>1.34</u>	Southern California Edison Co.
	12.80%	Total adjusted by various factors
Debt Service	<u>15.96%</u>	Debt service is not adjusted
	28.76%	Total not adjusted by CPI

Appendix 1

GA and CPI Comparison 1979 - 2007

	CPI Increase	75% of CPI	GA Increase	GA Percentage of CPI
1979	8.8%	6.60%	7.0%	79.55%
1980	18.4%	13.80%	6.5%	35.33%
1981	9.1%	6.83%	5.5%	60.44%
1982	8.8%	6.60%	5.5%	62.50%
1983	0.3%	0.23%	4.5%	1500.00%
1984	4.7%	3.53%	4.0%	85.11%
1985	4.6%	3.45%	3.0%	65.22%
1986	4.3%	3.23%	2.5%	58.14%
1987	4.0%	3.00%	4.0%	100.00%
1988	4.4%	3.30%	3.0%	68.18%
1989	4.6%	3.45%	3.0%	65.22%
1990	6.6%	4.95%	6.0%	90.91%
1991	3.9%	2.93%	3.5%	89.74%
1992	4.2%	3.15%	3.0%	71.43%
1993	3.0%	2.25%	3.0%	100.00%
1994	1.8%	1.35%	2.0%	111.11%
1995	1.4%	1.05%	1.5%	107.14%
1996	1.7%	1.28%	1.6%	94.12%
1997	1.6%	1.20%	2.0%	125.00%
1998	1.0%	0.75%	1.0%	100.00%
1999	2.2%	1.65%	1.0%	45.45%
2000	3.5%	2.63%	3.0%	85.71%
2001	3.2%	2.40%	4.2%	131.25%
2002	2.8%	2.10%	1.75%	62.50%
2003	3.9%	2.93%	3.00%	76.92%
2004	1.8%	1.35%	1.30%	72.22%
2005	4.0%	3.00%	3.00%	75.00%
2006	4.7%	3.53%	4.00%	85.11%
2007	3.3%	2.48%	2.30%	69.70%
TOTAL	126.6%	94.95%	95.65%	
		GA Percentage of CPI		75.55%