

SANTA MONICA RENT CONTROL BOARD ADMINISTRATION MEMORANDUM

TO: Santa Monica Rent Control Board
FROM: Tracy Condon, Administrator
FOR MEETING OF: May 20, 2010
PUBLIC HEARING: June 1, 2010
RE: 2010 Annual General Adjustment
Apartment Operating Cost Increases (March 2009 - March 2010)

Summary

The Rent Control Law requires the Board to adjust rent ceilings each year to reflect changes in owners' operating expenses. This adjustment is called the annual general adjustment, or "GA." The recommended GA for 2010 is 2%.

Actual and estimated changes in operating expenses from March 2009 to March 2010 are researched and evaluated using a formula of general application known as the "component ratio to gross rent", or "pie methodology". Each individual category of an owner's operating expenses is assigned a portion or "slice" of the total rent dollar.

Actual changes in costs for refuse, water and sewer, gas, electricity, and fire and life safety inspections are used to adjust these components. Property taxes are usually adjusted by 2%, except when supplemental adjustments have been authorized. Inflation-related adjustments are made to the remaining components: management, self labor and cash flow (CPI—All Items index) and maintenance and insurance (CPI—All Items, Less Shelter index). Debt Service is not adjusted.

This year, the Board engaged a consultant to conduct supplemental studies on actual property tax and estimated insurance costs for owners of Santa Monica's controlled rental units.

Recommendation

Staff recommends the Rent Control Board set a public hearing on Tuesday, June 1, 2010 for consideration of a 2% general rent adjustment (GA).

Note: Units with market rate increases implemented from September 1, 2009 through August 31, 2010 are not eligible for the 2010 general adjustment. Owners with recent market rate rentals will have taken operating costs into account when establishing a new rental rate.

The 2009 General Adjustment

When the Board established last year's GA, the inflation rate was negative, something which had not occurred since the mid 1950s. With both Consumer Price Indexes negative¹, a 0% GA would have been justified. This also would have been consistent with last year's 0% cost of living adjustment for Social Security.

Given the rarity of this level of decline in the consumer price index, staff proposed a one-time alternative approach in the treatment of those components normally adjusted by the CPI. For the 2009 general adjustment, staff recommended that no adjustment be made to the maintenance, insurance, self labor, cash flow and management components. The Board granted a 1% GA with the understanding that the negative CPI adjustments would be subtracted from the 2010 GA calculation, giving owners the total increase to which they are entitled over the two-year period, while spreading out the increase to avoid an economically-difficult spike in rent for tenants.

2010 Methodology

This year's GA calculation follows the long-standing methodology developed by Dr. Kenneth Baar at the Board's direction in 1983. (More information about the methodology is contained in Appendix 1.) The Consumer Price Indexes (CPI) used in the Board's formula for 2010 have shown improvement since last year.² For the components adjusted by the CPI, staff applied the decreases that would have resulted from the application of the negative consumer price indexes in 2009 before applying this year's increases.

During last year's general adjustment discussions, some public comments focused on whether the Board's historical adjustments have adequately compensated Santa Monica owners for property taxes and insurance. Earlier this year, the Board authorized staff to contract with a consultant to provide additional data and analysis regarding the actual cost of property taxes for owners of Santa Monica's controlled units and estimated local insurance costs. Staff selected Seifel Consulting Inc. (Seifel), a group that has performed similar studies for other local government agencies including the Santa Monica Redevelopment Agency and Berkeley's Rent Stabilization Board. This group worked with Dr. Kenneth Baar in 2002 when he prepared Santa Monica's GA analysis and is familiar with the Board's formula.

Seifel performed a review of actual property tax and insurance costs to evaluate whether the standard and periodic supplemental adjustments used for these components have kept pace with actual costs borne by local owners. Their findings are reflected in the sections discussing these two components and their report is included as Appendix 2.

¹ Consumer Price Index (Los Angeles-Riverside-Orange County), All Urban Consumers, (CPI-U), 12-Months Percent Change from March 2008 – March 2009

- All Items Index = -1.0%
- All Items, Less Shelter Index = -2.7%

² Consumer Price Index (Los Angeles-Riverside-Orange County), All Urban Consumers, (CPI-U), 12-Months Percent Change from March 2009 – March 2010

- All Items Index = 1.9%
- All Items, Less Shelter Index = 4.1%

Dollar Value General Adjustment Components

The recommended 2% GA results in a rent of \$804 for the hypothetical average apartment used in the calculation. (See Table A on page 13.) In the Board's "pie methodology", the "slices" represent the percentage of the average rent dollar available for each expense category as shown in the pale yellow column (1) in the table below.

The bright yellow column (A) represents the hypothetical average unit with a rent of \$804. The light blue column (B) reflects the current median maximum allowable rent (MAR) of \$799 for all units that have not received any market rate increases. The purple column (C) reflects the current median MAR of \$1,260 for all units (long-term controlled and market rate), and the orange column (D) reflects the current median MAR of \$1,650 for units rented at market.

The columns show the dollar amounts available for each of the operating expense components when the same ratios (pie slices) are applied to various median rent levels. As the rent level increases, the amount available for each of the expenses rises proportionately. For example, on the unit with a MAR of \$804 the general adjustment formula provides \$73.76 available for the property tax expense; while on a rent of \$1,650, \$151.47 is available.

Component	(1) 2010 Ratio to Gross Rent	(A) 2010 Rent \$803.62	(B) Median No Market Rents \$799.00	(C) Median All Units \$1,260.00	(D) Median Market Units \$1,650.00
Property Taxes	9.18%	\$73.76	\$73.35	\$118.88	\$151.47
Refuse	2.31%	\$18.54	\$18.46	\$29.91	\$38.12
Fire & Life Safety	0.11%	\$0.91	\$0.88	\$1.42	\$1.82
Water & Sewer	3.84%	\$30.84	\$30.68	\$49.73	\$63.36
Gas	2.44%	\$19.64	\$19.50	\$31.60	\$40.26
Electricity	1.60%	\$12.86	\$12.78	\$20.72	\$26.40
Maintenance	14.12%	\$113.51	\$112.82	\$182.85	\$232.98
Insurance	4.39%	\$35.30	\$35.08	\$56.85	\$72.44
Self Labor	7.13%	\$57.26	\$56.97	\$92.33	\$117.65
Debt Service	15.49%	\$124.51	\$123.77	\$200.60	\$255.59
Cash Flow	34.40%	\$276.47	\$274.86	\$445.48	\$567.60
Management	5.00%	\$40.18	\$39.95	\$64.75	\$82.50
Total Rent 2009 w/ 1.0% GA		\$787.86	\$799.00	\$1,295.00	\$1,650.00
Total Rent 2010 w/ 2.0% GA		\$803.62	\$814.98	\$1,320.90	\$1,683.00
Dollar difference		\$15.76	\$15.98	\$25.90	\$33.00

COMPONENT CALCULATIONS

This section analyzes cost changes for each operating component. Table A on page 13 shows the changes to each component and the overall calculation of the GA of 2%. The pie chart on page 14 shows the “pie slice size” for each expense component after applying the recommended adjustments.

Components Analyzed by Seifel Consulting Inc.
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Property Taxes

Property tax increases post-Proposition 13 are limited to a 2% increase in assessed value per year, except when properties are reassessed, which normally occurs upon a transfer. The 2% limit is generally used in adjusting the property tax component of the rent dollar.

Following additional analysis on the property tax component, in 1989, 1992 and 2002 larger increases were applied to this component to compensate for increases in taxes associated with property sales. In 1989 and 1992, the component was increased by 6% to account for properties that had changed ownership between 1982 – 1989 and 1989 – 1991, respectively. In 2002, the component was increased by 28.6% due to the reassessment of properties that transferred ownership since 1995, when vacancy decontrol was enacted statewide. The 2002 increase was based on Dr. Baar’s analysis of property tax bills for a random sample of 272 of Santa Monica’s controlled properties.

For this year’s report, Seifel conducted a comprehensive analysis of the property tax component by analyzing data from the Board’s records and public information available from the tax assessor’s office for 3,158 controlled buildings with 26,478 units. The property tax data is based upon the assessed values reflected in the 2009 property tax bills.

The consultant’s table below shows that the per unit property tax expense varies significantly based on the time period in which buildings were sold and reassessed. (See Appendix 2 for the full report.) Properties purchased in the decade before 1980 have a median tax expense of \$32.84 per unit per month, whereas properties purchased since 2005 have a median tax per unit per month of \$221.00.

Table 1A Apartment Property Taxes by Timeframe of Prior Purchase Santa Monica Rent Control Board

Purchase Year	Total Buildings	Total Units	Percent of All Units Sold	Median Tax Per Unit Per Month	Average Tax Per Unit Per Month	Average Monthly Rent/Unit	Average Ratio of Tax to Rental Income
sale date	233	1,763	6.7%	\$24.15	\$31.39	\$1,142	2.9%
1969 and prior	164	1,323	5.0%	\$25.06	\$27.56	\$1,149	2.6%
1970-1979	550	4,689	17.7%	\$32.84	\$39.80	\$1,289	3.3%
1980-1989	681	5,763	21.8%	\$65.80	\$71.63	\$1,308	6.0%
1990-1994	213	1,743	6.6%	\$82.68	\$89.61	\$1,349	7.3%
1995-1999	407	3,712	14.0%	\$86.14	\$95.14	\$1,420	7.4%
2000-2004	523	4,418	16.7%	\$142.39	\$162.68	\$1,496	11.8%
2005-2009	387	3,067	11.6%	\$221.00	\$238.93	\$1,502	17.4%
Total	3,158	26,478	100.0%	\$73.76	\$100.65	\$1,356	7.7%

The consultant's recommendation is to increase the property tax component from the 2009 amount of \$66.09 to \$73.76 which is the median tax paid per unit per month. The recommendation states, "We suggest using the median rather than the mean or average to account for the fact that recently sold properties skew the average data such that it is not representative of the property tax paid on most units."³ Staff agrees with the recommendation and believes the overall median tax amount of \$73.76 found by the consultant should be used for this component for 2010.

The 2009 component cost of \$66.09 must be increased by \$7.67 to reach the recommended 2010 cost of \$73.76. While the amount of \$73.76 over-compensates owners of properties purchased prior to 1990, it is somewhat less than the expense for purchases made through 1999 and is significantly less for purchases made since 2000. It may be assumed that owners who purchased properties since vacancy decontrol/re-control began in 1999 did so with increased expectations of potential rental income. Presumably, purchase prices decisions would have been made accordingly.

As stated previously, it is not possible for the Board's formula of general application to address the range of expenses incurred by each property owner. Overall, for 51.2% of all units sold, the amount of \$73.76 is greater than the median and average tax per unit per month. Because the Board's formula is one of general application there will always be property owners who are over-compensated and those whose expenses are greater than the component cost.

It has been eight years since the last significant adjustment was made to this component and staff believes an increase is warranted at this time. The amount recommend by the consultants is \$73.76. This amount is reflected in the following table and represents an increase of 11.61%.

	2009 Average Monthly (per unit) Property Tax Bill	Percentage Increase 2009-2010	Cost Increase Apt/Month	Estimated 2010 cost
Property Tax	\$66.09	11.61%	\$7.67	\$73.76

**Average Monthly Property Tax Bill per Unit
Years with Special Adjustments over 2%**

1978	Component established	\$19.20
1989	6% increase	\$32.67
1992	6% increase	\$37.44
2002	28.6% increase	\$57.53
2010	11.6% increase	\$73.76

³ From Page 3 of Seifel Consulting Inc. Report – Appendix 2
Annual General Adjustment 2010

Insurance

Prior to 1997, the GA analysis considered the insurance and maintenance components together and the CPI, Less Shelter index was used to calculate the annual increase or decrease for the combined component. In 1997, the Board commissioned Thomas D. Stringer of Stringer Appraisals to survey local insurance costs to determine whether local costs were adequately represented in the Board's GA analysis.

Based on Stringer's analysis, and other information gathered by the Board, the 1997 general adjustment report found that an increase of 27.8% for insurance was warranted. To apply the increase only to the insurance component, insurance was separated from the maintenance component. This resulted in an average monthly cost per apartment for insurance of \$23.96. The component was again adjusted in 1998 by 4.26% based on information contained in a subsequent report by Stringer.

Comments by the public during last year's Board discussions about the general adjustment as well as some data reviewed by staff suggested that an upward adjustment to the insurance component may be warranted. Staff had difficulty obtaining information about insurance costs specific to Santa Monica and did not have sufficient information to conclude that an increase to the insurance adjustment was warranted for 2009.

For this year's analysis, Seifel Consulting Inc. was asked to conduct a study of insurance costs for Santa Monica multi-family dwellings. The consultants analyzed actual insurance data for 2008 and 2009 for a group of Santa Monica properties and also reviewed data from the Institute of Real Estate Management (IREM).

Institute of Real Estate Management (IREM)

The IREM data (see Table 1 of the Seifel report [Appendix 2]) is based on costs for apartment buildings with 12-24 units in the Los Angeles area. However, according to Seifel, the sample size is small. Due to these limitations, Seifel could not rely on the data. Additionally, the IREM data does not reflect costs for the Santa Monica area specifically.

Therefore, the consultants did not base their recommendation on this information as explained on page 1 of their report. They state, "...average expense levels reported for Los Angeles may not reflect averages or trends in Santa Monica apartment insurance costs, due to differences in the age and/or type of buildings. Moreover, the sample size for IREM data for apartment buildings with 12 to 24 units in the Los Angeles area is quite small and the data is therefore an imperfect indicator of insurance costs."

The consultants determined the data on the Santa Monica properties was the best indicator of actual local insurance costs. That data is discussed below.

Santa Monica Data

Local 2009 insurance costs for 441 apartment units within 26 buildings and 2008 costs for 417 units in 23 buildings were provided by a large property management company and an owner of a large number of controlled units.

Table 2A of the Seifel report shows the average cost per unit for various building sizes and the overall average cost for all the buildings included in the report. As the table shows, building size has a significant impact on the average per unit insurance cost: the smaller the building the greater the average unit cost.

Table 2A
Monthly Insurance Costs per Unit by Building Size, 2008-2009
Santa Monica Rent Control Board

	Sample Size (# Units)	Average Monthly Insurance Cost Per Unit				Weighted Average ^a
		4-11 unit buildings	12-24 unit buildings	25+ unit buildings	All buildings	
2008	417	\$37.30	\$25.16	\$21.57	\$28.60	\$35.22
2009	441	\$36.68	\$29.53	\$23.40	\$31.10	\$35.30
Buildings by Size ^b		84%	12%	4%	100%	

a. Adjusted to reflect the size of buildings subject to rent control in Santa Monica.

b. Share of buildings with 4 or more units subject to rent control in Santa Monica (2,770 buildings).

Source: Sullivan-Dituri Co. and Community Corporation of Santa Monica (April 2010).

The average cost for all buildings is \$31.10. The consultant does not recommend using this figure (which is less than the \$31.94 used in 2009 for this component) as the proportion of buildings reflected in the sample data is not representative of the composition of all buildings in Santa Monica with 4 or more units.

For a more accurate representation of Santa Monica's controlled housing stock, the consultants relied on the data provided by the Board for the property tax analysis but narrowed it to include only buildings with 4 or more units (2,770 buildings met that criterion). The composition of the controlled housing stock by building size is: 84% of buildings have 4-11 units; 12% have 12-24 units; and 4% have 25 or more units. Given that the average per unit cost is higher for smaller buildings, the consultants used a weighted average analysis to calculate an average cost. Based on their findings, their recommendation is to increase the insurance component from \$31.94 to \$35.30. This is a 10.52% increase. Staff agrees with the recommendation and has calculated the 2010 estimated cost using that figure.

	2009 Average Monthly Cost Per Apt. Unit	Percent Change	Cost Change/ Apt./Month	Estimated 2010 Cost
Insurance	\$31.94	10.52%	3.36	35.30

Components Adjusted by Actual Changes in Costs

A summary of the 2010 estimated costs for components adjusted by actual cost changes follows. Detailed information about each of these components is found in Appendix 3.

Refuse Collection

Refuse collection charges consist of a fixed charge per apartment and collection fees based on the type of refuse container used and the frequency of collection. Effective July 1, 2009, the monthly fixed charge rate and the collection fees were increased by 2%.

The 2009 total bill was projected at \$18.18. Applying the 2.0% increase results in the projected cost of \$18.54 for 2010.

	2009 Average Monthly Cost Per Apt. Unit	Percent Cost Increase 2009-2010	Cost Increase Apt/Month	Estimated 2010 cost
Refuse Collection	\$18.18	2.0%	\$0.36	\$18.54

Fire and Life Safety Inspection Fee

Fire and Life Safety Inspections are required for all apartment buildings in Santa Monica. Since January 2004, property owners have been charged a fee for the inspection. The cost of the inspection is a flat fee per building regardless of size. Last year's estimated cost for this component was set at \$0.89 (based on a \$64.34 flat fee). In July 2009 the inspection fee was increased to \$65.62. Based on that increase, the monthly per unit cost for 2010 is projected to be \$0.91 (\$65.62 divided by 6 units divided by 12 months). This represents a 2.2% increase in the cost for this component.

	2009 Cost Per Apt. Unit	Percent Cost Increase 2009-2010	Cost Increase Apt/Month	Estimated 2010 cost
Average Fire & Life Safety Inspection Expense	\$0.89	2.2%	\$0.02	\$0.91

Water and Sewer

On July 8, 2008, the City Council adopted a five-year rate schedule for water and sewer (wastewater). The new schedule reflects a change in the rate schedule to a commodity-only structure (based only on water usage). The fixed bi-monthly service charge was eliminated and a four tier commodity schedule was established. (Previously a three tier schedule was in use.) This change was made to promote water efficiency and conservation.

Pursuant to City Council Resolutions (CCS) 10322 and 10372, the first rate increase under the new schedule was implemented as of August 1, 2008. The Resolutions set forth the maximum increases that would be allowed for 2009 through 2012. In July 2009, the Water Department implemented the second of the five increases and water rates were increased by 10.5% and sewer rates (wastewater) were increased by 18%. This year's GA reflects the total increase of 10.5% on water rates and 18% on sewer rates.

The table below reflects the 10.5% increase to the 2009 water expense of \$12.69 and the 18% increase to the 2009 sewer expense of \$14.25. The last line in the table sets out the combined water and sewer expenses. The net effect of the combined increases is \$3.90 or a 14.48% increase. The 2009 and 2010 costs reflect an average consumption factor of 4.85 HCF per unit per month. (Details about water consumption are detailed in Appendix 3.)

	2009 Average Monthly Cost per Apt	July 1, 2009 rates	Cost Increase Apt/Month	Estimated 2010 cost
Average water expense	\$12.69	10.5%	\$1.33	\$14.02
Average sewer expense	<u>\$14.25</u>	18%	<u>\$2.57</u>	<u>\$16.82</u>
Total Water/Sewer Expense	\$26.94	14.48%	\$3.90	\$30.84

Gas – Common Areas Only

Average Costs

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

The average gas expense includes the actual cost of gas which is made up of a procurement cost (cost of the gas itself which changes monthly) and a transmission charge (cost for delivering gas to homes), several incidental charges, and a 10% Santa Monica Utility Tax. The 2010 projected cost of gas including the incidental charges and the utility tax reflects a decrease of **-17.77%** from the cost for 2009.

Total Monthly Gas Cost

The gas cost and incidental charges for 2009 and 2010 are shown below. The 2010 estimated cost is shown in the table that follows.

	2009	2010
Gas	\$17.31	\$12.92
Incidentals	<u>6.56</u>	<u>6.72</u>
	\$23.88 ⁴	\$19.64 ⁵

	2009 Average Monthly Cost per Apt. unit	Rate Change 2009-2010	Cost Increase Apt/Month	Estimated 2010 cost
Common area average gas expense	\$23.88	-17.77%	-\$4.24	\$19.64

⁴ April 2009 Cost \$17.31 (16.036 therms x .981505 baseline rate = \$15.74 + \$1.57 [10% tax]) + incidentals \$6.56 (daily service rate [30 days x .16438] + State Regulatory Fee [16.036 therms x .00068] + Low Income Discount Rate Surcharge [16.036 therms x .06384] = \$5.97 + \$0.59 [10% tax]) = **Total cost \$23.88.**

⁵ April 2010 Cost \$12.92 (16.036 therms x .732281 baseline rate = \$11.74 + \$1.17 [10% tax]) + incidentals \$6.72 (daily service rate [30 days x .16438] + State Regulatory Fee [16.036 therms x .00068] + Low Income Discount Rate Surcharge [16.036 therms x .07269] = \$6.11 + \$0.61 [10% tax]) = **Total cost \$19.64.**

Electricity – Common Areas Only

Average Costs

Last year staff increased the average cost for this component to reflect the conversion of properties with “house meters” from Schedule D to the GS-1 rate schedule. The result was an increase of 21.49% to the 2008 cost resulting in the estimated cost for 2009 of \$12.71.

To determine the 2010 cost for this component, the current composite cost for the GS-1 schedule (17.5 cents per kWh) was compared to last year’s cost (17.3 cents per kWh). The difference is an increase of 1.16%. When applied to the 2009 cost of \$12.71 the result is \$12.86. This is the amount projected for 2010.

	2009 Average Monthly Cost per Apt. unit	Rate Change 2009-2010	Cost Change Apt/Month	Estimated 2010 per unit cost
Common area average electricity expense	\$12.71	1.16%	\$.15	\$12.86

Components Adjusted by Changes in the Consumer Price Index

As stated earlier, due to the unusual negative CPI indexes last year, no adjustment was made to the following components instead of applying the CPI amounts of **-2.7%** and **-1%**. This was done with the understanding that the 2009 decreases would be factored in when calculating the costs for these components for the 2010 GA.

The following tables show the result of applying the negative CPI amounts from 2009 to the 2008 average costs and then applying the March 2009 – March 2010 CPI amounts for CPI–All Items, Less Shelter (4.1%) and CPI–All Items (1.9%).

Components Adjusted by the CPI Less Shelter Index (March 2009 - March 2010 = 4.1%)

The two components usually adjusted by this index are insurance and maintenance and other operating expenses. Since Seifel’s analysis is used to adjust the insurance component for 2010, only the maintenance component is adjusted by this CPI factor this year.

Maintenance and Other Operating Expenses

Information for this component specific to Santa Monica is not available.⁶ Therefore, the Board adjusts this category by the most-recently reported change in the Consumer Price All Items, Less Shelter. To calculate the estimated cost for 2010, the CPI index for 2009 of **-2.7%** was applied to the 2008 cost, and then the 4.1% current annual change in the CPI was applied to the result. This is shown in the following table. The difference between the

⁶ 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 at that time for this component fell within that range.

component cost used in 2009 of \$112.07 and the estimated 2010 cost of \$113.51 is \$1.44 (a net increase of 1.285%).

Maintenance		Percent Change	Cost Change/ Apt./Month	
2008 & 2009 Cost adjusted by -2.7%	\$112.07	-2.7%	-\$3.03	\$109.04
Adjusted cost plus 4.1% increase	109.04	4.1%	\$4.47	\$113.51

Maintenance	2009 Average Monthly Cost Per Apt. Unit	Percent Change	Cost Change/ Apt./Month	Estimated 2010 Cost
	\$112.07	1.28%	\$1.44	113.51

Components Adjusted by the CPI All Items Index (March 2009 - March 2010 = 1.9%)

The following tables show the result of applying the 2009 CPI—All Items index of -1% to the 2008 average costs and then applying the current increase for CPI—All Items of 1.9%.

Self Labor

The difference between the cost used in 2009 of \$56.76 and the estimated cost of \$57.26 is \$0.50 (a net increase of 0.88%).

Self Labor		Percent Change	Cost Change/ Apt./Month	
2008 & 2009 Cost adjusted by -1.0%	\$56.76	-1.0%	-\$0.57	\$56.19
Adjusted cost plus 1.9% increase	56.19	1.9%	\$1.07	\$57.26

Self Labor	2009 Average Monthly Cost Per Apt. Unit	Percent Change	Cost Change/ Apt./Month	Estimated 2010 Cost
	\$56.76	0.88%	\$0.50	\$57.26

Cash Flow Adjustment

The difference between the cost used in 2009 of \$274.50 and the estimated cost of \$276.92 is \$2.42 (a net increase of 0.88%)

Cash Flow		Percent Change	Cost Change/ Apt./Month	
2008 & 2009 Cost adjusted by -1.0%	\$274.50	-1.0%	-\$2.74	\$271.76
Adjusted cost plus 1.9% increase	271.76	1.9%	\$5.16	\$276.92

Cash Flow	2009 Average Monthly Cost Per Apt. Unit	Percent Change	Cost Change/ Apt./Month	Estimated 2010 Cost
	\$274.50	0.88%	\$2.42	\$276.92

Management

The difference between the cost used in 2009 of \$39.39* and the estimated cost of \$39.74 is \$0.35 (a net increase of 0.88%).

Management		Percent Change	Cost Change/ Apt./Month	
2008 & 2009 Cost adjusted by -1.0%	\$39.39	-1.0%	-\$0.39	\$39.00
Adjusted cost plus 1.9% increase	\$39.00	1.9%	\$0.74	\$39.74

Management	2009 Average Monthly Cost Per Apt. Unit	Percent Change	Cost Change/ Apt./Month	Estimated 2010 Cost
	\$39.39*	0.88%	\$0.35	\$39.74

*Management costs are fixed at 5% of gross rent pursuant to Rent Board Regulation 4101(c)(1). After the adjustment is applied to this component, it is readjusted to be set at 5% of the current gross rent.

Table A

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

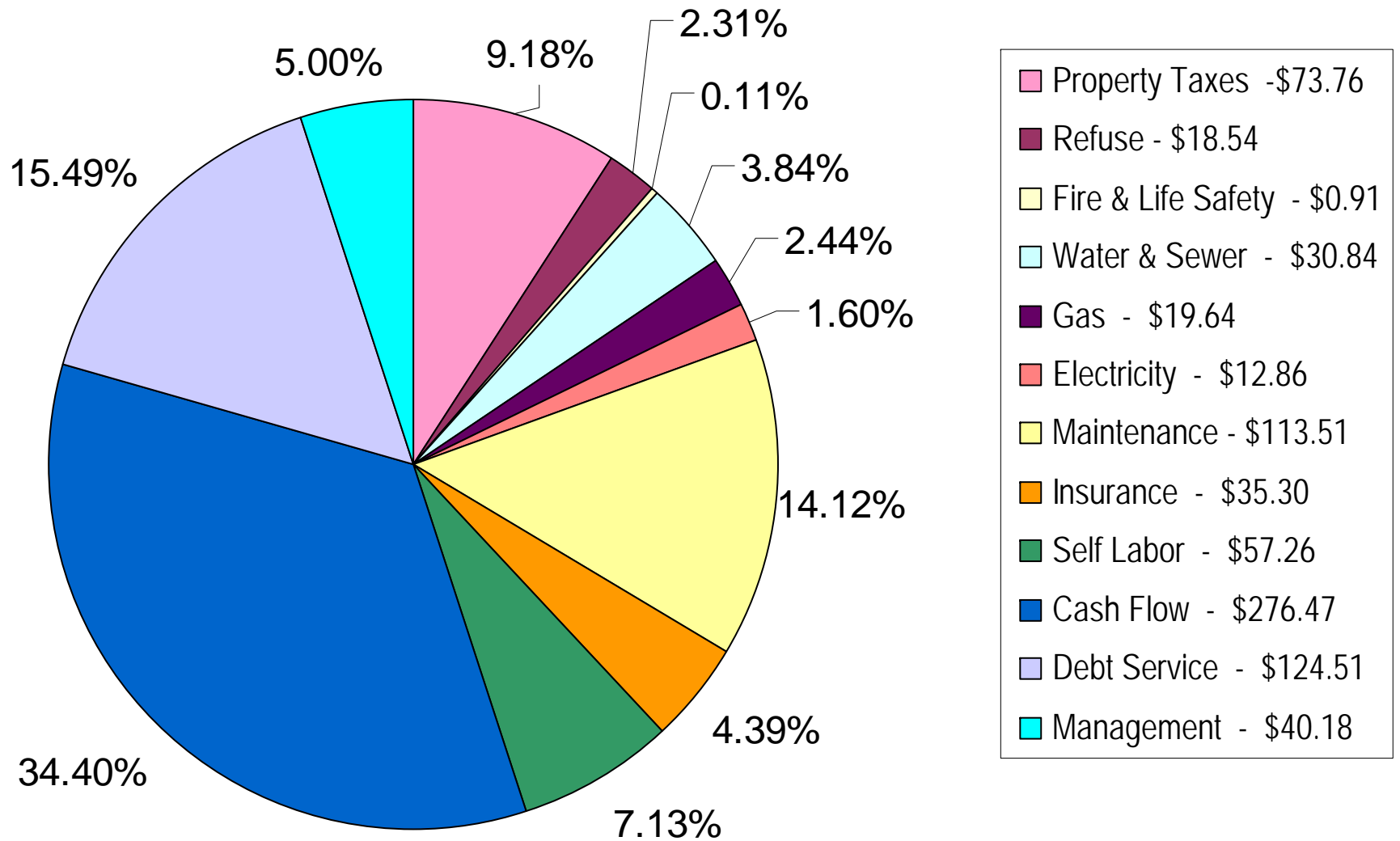
Rent Increases Required to Cover Operating Cost Increases and Index Cash Flow

Operating Expense	2009 ratio to gross rent (a)	Estimated cost 2009*	Percent increase 2009-2010 (b)	Percent Increase Required (a) x (b)	Estimated cost 2010 (c)	Rent Adjustment required (d)
Property Taxes	0.0839	\$66.09	11.61%	0.9739%	\$73.76	\$7.67
Refuse	0.0231	18.18	2.0%	0.0462%	18.54	0.36
Fire & Life Safety Inspection Fee	0.0011	0.89	2.2%	0.0025%	0.91	0.02
Water & Sewer	0.0342	26.94	14.48%	0.4951%	30.84	3.90
Gas	0.0303	23.88	-17.77%	-0.5386%	19.64	-4.24
Electricity	0.0161	12.71	1.16%	0.0187%	12.86	0.15
Maintenance	0.1422	112.07	1.284%	0.1828%	113.51	1.44
Insurance	0.0405	31.94	10.52%	0.4265%	35.30	3.36
Self Labor	0.0720	56.76	0.88%	0.0634%	57.26	0.50
Debt Service	0.1580	124.51	0.0%	0.0000%	124.51	0.00
Cash Flow	0.3484	274.50	0.88%	0.3066%	276.47*	1.97*
Management	0.0500	<u>39.39</u>	0.88%	0.0435%	<u>40.18*</u>	<u>0.79*</u>
Totals		\$787.86		2.02%	\$803.78	\$15.92

Recommended GA rounded to 2.0% \$787.86 * 2.0% = \$803.62 \$15.76

* Management costs are fixed at 5% of gross rent pursuant to Rent Board Regulation 4101(c)(1). Adjusting management to equal 5% of the new gross rent of \$803.62 sets the cost for management to \$40.18 rather than 39.74. Cash Flow has been adjusted from \$276.92 to \$276.47 to reflect the increase in the management cost.

2010 Rent Dollar Components



APPENDIX 1 Methodology

In 1983, at the direction of the Board, Dr. Kenneth Baar developed a methodology for calculating the annual General Adjustment. Some modifications were made to the methodology in subsequent years.

In 2002, Dr. Baar was asked again to prepare the general adjustment report for the Board and to analyze various approaches to calculating the general adjustment. While the Board decided not to alter the methodology previously developed by Dr. Baar, they did incorporate some of his recommended modifications to several of the components. These modifications were incorporated in the GA reports beginning in 2003.

In 2008, staff proposed studying whether an alternate methodology based entirely on the CPI index should be considered. However, the Board felt the existing methodology was most responsive to changes in costs for Santa Monica properties and did not change the methodology.

The 2009 General Adjustment Report was prepared using the methodology and survey data previously developed by Dr. Kenneth Baar with modifications to accommodate the negative CPI indexes used in the analysis. For 2010, staff has followed the Board's long-standing methodology with the features shown below. 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 and Solid Waste Department). In addition, staff engaged Seifel Consulting Inc. to compile and analyze data related to the property tax and insurance components.

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 Table A, page 13.
3. Survey of utility companies, government agencies and tax assessor records to determine actual increases (or decreases) in property owners' costs in the last year.

This methodology is consistent with the Rent Control Law as stated in the Board's Charter Amendment, Section 1805(b).

ANNUAL GENERAL ADJUSTMENT: Each year the Board shall generally adjust rents as follows:

- (1) Adjust rents upward by granting landlords a utility and tax increase adjustment for actual increases in the City of Santa Monica for taxes and utilities.
- (2) Adjust rents upward by granting landlords a maintenance increase adjustment for actual increases in the City of Santa Monica for maintenance expenses.
- (3) Adjust rents downward by requiring landlords to decrease rents for any actual decreases in the City of Santa Monica for taxes.

In adjusting rents under this subsection, the Board shall adopt a formula of general application.

APPENDIX 2

Property Tax and Insurance

Santa Monica Rent Control Board 2010 Property Tax Adjustment Summary of Findings

A. Purpose and Organization

- Rent Control Law Section 1805(b) requires the Santa Monica Rent Control Board (Board) to generally adjust rents each year and adopt a formula for making general adjustments (GA). The adjustment must take increases in utility, tax and maintenance expenses into account.
- The Board requested Seifel Consulting Inc. (Seifel) to inform the 2010 GA through a review of property tax information. This summary presents findings to the Board and staff.
- This status update is organized as follows:
 - A. Purpose and Organization
 - B. Key Findings
 - C. Recommendation

B. Key Findings

- Proposition 13 (1979) limited property tax increases to a 2 percent increase per year, except upon a transfer (sale), when properties are reassessed to market value. The Board has generally used the 2 percent limit to calculate the property tax component of the GA. In depth analyses were done in 1989, 1992, and 2002 to account for the increases that occur upon sale.
- The 2009 property tax component of the GA was \$66.09. The potential 2010 property tax component would be \$67.41, applying the 2 percent limit.
- Seifel Consulting used County Assessor and Rent Control Board data to analyze property tax.¹ Findings are presented by timeframe of prior purchase in Tables 1A and 1B.
 - The sample is based on properties subject to rent control, excluding those where 50 percent or more of the units have no registered rents as of April 2010. This includes 26,478 housing units in 3,158 buildings.
 - Properties were analyzed by timeframe of prior purchase as property taxes and the related expense ratio vary significantly based on when they were last transferred. Over 50 percent of the units were last purchased prior to 1990. Roughly 20 percent were last purchased in the 1990s and 28 percent since 2000.
 - Both median and mean (average) monthly property taxes paid per apartment were calculated to understand typical property tax levels.
 - The median monthly property tax paid per apartment unit is \$74, roughly 109 percent of the 2010 property tax component calculated using the 2 percent limit. By timeframe, this ranges from a low of \$24 for properties without a prior purchase date listed to a high of \$221 for properties that last turned over between 2005 and the present.

¹ Data collected as of April 2010. Property tax data is as of 2008, the most recent available from the Los Angeles County Assessor.

Table 1A
Apartment Property Taxes by Timeframe of Prior Purchase
Santa Monica Rent Control Board

Purchase Year	Total Buildings	Total Units	Percent of All Units Sold	Median Tax Per Unit Per Month	Average Tax Per Unit Per Month	Average Monthly Rent/Unit	Average Ratio of Tax to Rental Income
No sale date	233	1,763	6.7%	\$24.15	\$31.39	\$1,142	2.9%
1969 and prior	164	1,323	5.0%	\$25.06	\$27.56	\$1,149	2.6%
1970-1979	550	4,689	17.7%	\$32.84	\$39.80	\$1,289	3.3%
1980-1989	681	5,763	21.8%	\$65.80	\$71.63	\$1,308	6.0%
1990-1994	213	1,743	6.6%	\$82.68	\$89.61	\$1,349	7.3%
1995-1999	407	3,712	14.0%	\$86.14	\$95.14	\$1,420	7.4%
2000-2004	523	4,418	16.7%	\$142.39	\$162.68	\$1,496	11.8%
2005-2009	387	3,067	11.6%	\$221.00	\$238.93	\$1,502	17.4%
Total	3,158	26,478	100.0%	\$73.76	\$100.65	\$1,356	7.7%

Table 1B
Cumulative Analysis of Apartment Property Taxes by Timeframe of Prior Purchase
Santa Monica Rent Control Board

Purchase Year	Total Buildings	Total Units	Percent of All Units Sold	Median Tax Per Unit Per Month	Average Tax Per Unit Per Month	Average Monthly Rent/Unit	Average Ratio of Tax to Rental Income
No sale date							
1969 and prior ^a	397	3,086	11.7%	\$24.69	\$29.75	\$1,145	2.8%
1979 and prior	947	7,775	29.4%	\$28.11	\$35.81	\$1,232	3.1%
1989 and prior	1,628	13,538	51.1%	\$40.43	\$51.06	\$1,264	4.3%
1994 and prior	1,841	15,281	57.7%	\$44.63	\$55.46	\$1,274	4.6%
1999 and prior	2,248	18,993	71.7%	\$53.66	\$63.21	\$1,303	5.2%
2004 and prior	2,771	23,411	88.4%	\$65.20	\$81.98	\$1,339	6.4%
2009 and prior	3,158	26,478	100.0%	\$73.76	\$100.16	\$1,358	7.7%

Note: Because of averaging over timeframes and rounding, calculations may not precisely add/subtract.
a. Includes properties without a sale date available.

Source: Los Angeles County Assessor, Santa Monica Rent Control Board, 2010 (property tax as of 2008). Based on properties subject to rent control, excluding those where 50 percent or more than the units have no registered rents.

- The mean or average monthly property tax paid per apartment unit is \$101, roughly 150 percent of the 2010 property tax component calculated using the 2 percent limit. As shown in Table 1A, average monthly taxes are lower than this in most timeframes. Seventy-two percent of units were last purchased before 2000, timeframes within which the average is less than \$101, and generally much less. In other words, sales within the last decade amount to less than 30 percent of units, but skew property tax amounts up significantly.
- Average monthly rent is just over \$1,350, including both long term (restricted) and market rate rent. Average rent levels vary slightly by timeframe, with the lowest rents found in buildings that have not been sold since before 1970 or have no sale date (roughly \$1,150) and the highest in those that have turned over since 2000 (roughly \$1,500).
- The average ratio of property taxes paid to rental income per apartment is 7.7 percent. While average rents increase over time, they do not increase as much as property taxes. As a result, the ratio of tax to rental income is significantly higher for properties that have turned over since 2000 than for other properties.
- Higher purchase prices (and therefore property tax amounts) may in part reflect higher expectations of rental revenue, particularly for properties sold since 1995 when vacancy decontrols were instituted. However, as discussed above, actual rental income is not high enough to offset higher property taxes on more recently purchased properties.

C. Recommendation

- Based on the data and findings above, Seifel recommends increasing the property tax component of the GA from 66.09 to \$73.76, the median tax currently paid per unit per month. This amounts to an increase of roughly 11 percent. We suggest using the median rather than the mean or average to account for the fact that recently sold properties skew the average data such that it is not representative of the property tax paid on most units.
- Given the impact of resale or turnover on property taxes for local apartment buildings, the Board and staff should consider replicating this analysis every 3 to 5 years to ensure that the GA keeps pace with property tax expenses.

Santa Monica Rent Control Board

2010 Insurance Adjustment Summary of Findings

A. Purpose and Organization

- Rent Control Law Section 1805(b) requires the Santa Monica Rent Control Board (Board) to generally adjust rents each year and adopt a formula for making general adjustments (GA). The adjustment must take increases in utility, tax and maintenance expenses into account.
- The Board requested that Seifel Consulting Inc. (Seifel) inform the 2010 GA through a review of insurance information. This summary presents findings to the Board and staff.
- This status update is organized as follows:
 - A. Purpose and Organization
 - B. Key Findings
 - C. Recommendation

B. Key Findings

- Insurance costs vary widely based on location, the amount and type of coverage provided, and the size, value and other specific characteristics of the property being insured. Costs for individual properties can also fluctuate significantly from year to year based on insurance claims, changes in coverage and/or insurance agents and adjustments to the property.
- An in depth analysis of the insurance component of the GA was conducted in 1997 and 1998. Since that time the Board has increased the insurance component by the change in the Consumer Price Index (CPI), less shelter, with the exception of 2009 when the CPI less shelter was negative and the Board held the insurance component steady.
- Seifel analyzed insurance costs for smaller, low-rise apartment buildings in the Los Angeles Area based on an index published annually by the Institute of Real Estate Management (IREM). As shown in Table 1, monthly insurance costs per unit held relatively steady between 1994 and 2002, generally fluctuating between \$13 and \$18. Since 2002, insurance costs as reported by IREM have more than doubled to \$44 in 2008. As a result, average costs published by IREM currently exceed the insurance component by roughly \$12 or 35 percent. However, average expense levels reported for Los Angeles may not reflect averages or trends in Santa Monica apartment insurance costs, due to differences in the age and/or type of buildings. Moreover, the sample size for IREM data for apartment buildings with 12 to 24 units in the Los Angeles area is quite small and the data is therefore an imperfect indicator of insurance costs.
- Two local property owners/managers, Sullivan-Dituri Co. and Community Corporation of Santa Monica (CCSM), provided data regarding insurance costs for Santa Monica apartment buildings in 2008 and 2009. This data includes information on 441 apartment units within 26 buildings in 2009 and 417 units in 23 buildings in 2008. An analysis of this data by size of building and type of insurance policy is shown in Tables 2A and 2B and summarized below:
 - Average insurance costs in 2009 were roughly \$31 per unit per month.
 - Smaller buildings have significantly higher insurance costs on a per unit basis than larger properties – roughly \$37 per unit per month in buildings with between 4 and 11 units as compared to only \$23 in buildings with 25 or more units. This is particularly notable as

apartment buildings under rent control in Santa Monica are, on average, smaller than those in the sample.

- Of Santa Monica properties with 4 or more units, 84 percent contain 4 to 11 units, 12 percent contain 12 to 24 units, and only 4 percent contain 25 units or more. (Based on 2,770 buildings with 4 or more units subject to rent control in Santa Monica.)
- Santa Monica properties have an average or mean of 8 units per building and median of 6 units per building. In contrast, the average building size in the data provided by CCSM and Sullivan-Dituri Co. is 17 units. (Based on 3,158 buildings subject to rent control in Santa Monica.)
- Insurance costs also vary by the type of policy available. Some properties held by CCSM are eligible to be included within a Master Policy that covers multiple properties and has favorable rates compared to other types due to bulk rate savings. As shown in Table 2B, these savings are significant; with insurance costs roughly \$17 to \$18 less for units under the Master Policy than for those that are not covered by it.
- Changes in the amount and types of coverage provided by insurance agents also impact the cost to insure properties and to rehabilitate them after uncovered losses. Representatives from local property management firms and individual apartment owners stressed that, while insurance costs have increased moderately, the bigger difference has been in coverage. For example, mold, earthquakes, and pollution have been excluded from coverage since the imposition of rent control. Property owners must purchase this coverage separately, if they can obtain it, or cover the loss from related damage independently.

C. Recommendation

- Based on the data and findings above, Seifel recommends increasing the insurance component of the GA from \$31.94 to \$35.30, an increase of roughly 10.5 percent. This recommendation is based on a weighted average to adjust the sample of local units described above to reflect the actual composition of the Santa Monica building stock subject to rent control (84 percent containing 4 to 11 units, 12 percent containing 12 to 24 units, and 4 percent containing 25 units or more). IREM data and other information described above were also taken into account, but the Santa Monica-specific data, adjusted to be representative of the typical size of local buildings, was determined to be the best indicator of actual insurance costs.

Table 1
Comparison of Monthly Insurance Costs per Unit: IREM and SMRCB GA Component
Santa Monica Rent Control Board

Year	IREM Low Rise ^a				GA Component			Difference (GA less IREM)
	Amount	% Change		Size (Units)	Amount	% Change		
		Annual	Average Annual ^b			Annual	Average Annual ^b	
1994	\$ 16.08		N/A	1,234	\$ 17.15	2.4%	N/A	\$ 1.07
1995	\$ 17.83	10.9%	10.9%	1,148	\$ 17.49	2.0%	2.0%	\$ (0.34)
1996	\$ 9.92	-44.4%	-21.5%	1,087	\$ 18.75	7.2%	4.6%	\$ 8.83
1997	\$ 17.25	73.9%	2.4%	402	\$ 23.96	27.8%	11.8%	\$ 6.71
1998	\$ 16.83	-2.4%	1.1%	448	\$ 24.98	4.3%	9.9%	\$ 8.15
1999	\$ 13.58	-19.3%	-3.3%	468	\$ 25.38	1.6%	8.2%	\$ 11.80
2000	\$ 13.58	0.0%	-2.8%	300	\$ 26.22	3.3%	7.3%	\$ 12.64
2001	\$ 15.67	15.3%	-0.4%	273	\$ 27.01	3.0%	6.7%	\$ 11.34
2002	\$ 17.67	12.8%	1.2%	259	\$ 27.31	1.1%	6.0%	\$ 9.64
2003	\$ 25.67	45.3%	5.3%	211	\$ 28.29	3.6%	5.7%	\$ 2.62
2004	\$ 30.42	18.5%	6.6%	133	\$ 28.35	0.2%	5.2%	\$ (2.07)
2005	\$ 45.25	48.8%	9.9%	132	\$ 29.12	2.7%	4.9%	\$ (16.13)
2006	\$ 45.50	0.6%	9.1%	187	\$ 30.31	4.1%	4.9%	\$ (15.19)
2007	\$ 34.75	-23.6%	6.1%	220	\$ 30.98	2.2%	4.7%	\$ (3.77)
2008	\$ 43.58	25.4%	7.4%	199	\$ 31.94	3.1%	4.5%	\$ (11.64)

a. Low-rise apartments with 12-24 units in the Los Angeles area, according to the Institute of Real Estate Management (IREM). Data are shown for the year in which collected, as published the following year in the IREM Metropolitan Area Report.

b. The difference between the monthly insurance cost in each given year and the cost in 1994, expressed as the average annual increase in every year from 1994 to that year.

Sources: IREM, Santa Monica Rent Control Board.

Table 2A
Monthly Insurance Costs per Unit by Building Size, 2008-2009
Santa Monica Rent Control Board

	Sample Size (# Units)	Average Monthly Insurance Cost Per Unit				Weighted Average ^a
		4-11 unit buildings	12-24 unit buildings	25+ unit buildings	All buildings	
2008	417	\$37.30	\$25.16	\$21.57	\$28.60	\$35.22
2009	441	\$36.68	\$29.53	\$23.40	\$31.10	\$35.30
Buildings by Size ^b		84%	12%	4%	100%	

a. Adjusted to reflect the size of buildings subject to rent control in Santa Monica.

b. Share of buildings with 4 or more units subject to rent control in Santa Monica (2,770 buildings).

Source: Sullivan-Dituri Co. and Community Corporation of Santa Monica (April 2010).

Table 2B
Monthly Insurance Costs per Unit by Insurance Policy Type, 2008-2009
Santa Monica Rent Control Board

	Sample Size (# Units)	Insurance Policy Type		
		Master Policies	Other Policies	All Policies
2008	417	\$16.73	\$34.94	\$28.60
2009	441	\$20.85	\$37.51	\$31.10

Source: Sullivan-Dituri Co. and Community Corporation of Santa Monica (April 2010).

Note: Master Policies are policies used by the Community Corporation of Santa Monica to cover multiple properties at a bulk discount.

APPENDIX 3 Component Details

Refuse Collection

Refuse collection charges consist of a fixed charge per apartment and collection fees based on the type of refuse container used and the frequency of collection.

There are several types of containers and various options as to the frequency of collection. Over the years, the 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. Since July 2005, the fixed charge rates and the collection rates have increased effective July 1 of each year. Effective July 1, 2009, the monthly fixed charge rate was increased by 2% resulting in a monthly fee per apartment of \$3.86. Collection rates were also increased by 2% effective July 1, 2009⁷. The table shows the impact of the rate increases on the 2010 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	17.53
April 2009	3.79	14.39	18.18
April 2010	3.86	14.68 ⁷	18.54

The difference between the 2009 total bill calculated as \$18.18 and the projected cost of \$18.54 for 2010 reflects a 2.0% increase (\$0.36).

Fire and Life Safety Inspection Fee

This component was introduced 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.⁸ The average number of units per building used for most components in the Board’s general adjustment calculations is six units per building.

⁷ The rate for the class MSQ - one 2-yard bin picked up once weekly was increased from \$143.87 to \$146.75 per two month period. The analyses developed by staff assume two bins for such a ten-unit building, resulting in a cost of \$146.75 per month or \$14.68 per unit/per month.

⁸ City Council resolution 9858 adopted on June 17, 2003 established the fees.

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.

As of July 2008 the inspection fee was set at \$64.34.⁹ Last year’s estimated cost for this component was set at \$0.89. In July 2009 the inspection fee was increased to \$65.62. Based on that increase the monthly per unit cost for 2010 is projected to be \$0.91 (\$65.62 divided by 6 units divided by 12 months). This represents a 2.2% increase in the cost for this component.

Water and Sewer

On July 8, 2008, the City Council adopted a five-year rate schedule for water and sewer (wastewater). The new schedule reflects a change in the rate schedule to a commodity-only structure. The fixed bi-monthly service charge was eliminated and a four tier commodity schedule (based on water usage) was established. (Previously a three tier schedule was in use.) This change was made to promote water efficiency and conservation.

Pursuant to City Council Resolutions (CCS) 10322 and 10372, the first rate increase under the new schedule was implemented as of August 1, 2008. The Resolutions set forth the maximum increases that would be allowed for 2009 through 2012. In July 2009, the Water Department implemented the second of the five increases and water rates were increased by 10.5% and the sewer (wastewater) rates were increased by 18%. This year’s general adjustment reflects the total increase of 10.5% on water rates and 18% on sewer rates. The net effect of the combined increases is \$3.90 or a 14.48% increase. The amount projected for 2010 is \$30.84. (See page 9 for calculation.)

Average Costs

Water and sewer charges are considered together as the costs for both are made up of fees related to water consumption. Two factors influence the average water/sewer costs used in the general adjustment calculation: actual water and sewer (wastewater) rates and water consumption.

Prior to 2008, changes to the water and sewer rates were usually equal and increases or decreases were projected on the combined water and sewer expenses to determine the total cost for the water and sewer component. In 2009, the rate increases for water and sewer were not equal and it was necessary to separate the water and sewer components to calculate the respective increases.¹⁰

⁹ As of July 2007, the fee increased for \$60 to \$62.04. The general adjustment report for 2008 did not reflect that increase as staff was misinformed about July 2007 increase. In July 2008 the fee was again increased to \$64.34. In the Boards’ 2009 report, staff considered both increases in its projection for the 2009 cost.

¹⁰ In the 2006 general adjustment report the water and sewer expenses were separated due to different rate increases at that time. The amount of \$21.66 projected for 2006 included both the rate changes and an increase in the rate of consumption. Using that figure as a starting point, the proportion of the water expense to the total water/sewer expense was determined to be 48.615% and the sewer expense was 51.385%. Applying these ratios to the 2008 water/sewer component (\$23.51), resulted in the following 2008 costs for each item: \$11.43 for water and \$12.08 for sewer. The August 2008 rate increases of 11% and 18% were applied to the water and sewer costs of \$11.43 and \$12.08 which resulted in the 2009 costs of \$12.69 and \$14.25. The combined per unit cost for 2009 was \$26.94.

Consumption

The new rate structure established by the City Council in 2008 is wholly dependent on the amount of water used. Therefore, consumption levels play an even more significant role than in past years in determining the average costs for water and sewer. To evaluate changes in the cost of the water/sewer component, staff has been monitoring water consumption for many years. Since 1997, water consumption rates and water/sewer and refuse costs on two sets of randomly selected properties have been tracked. (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 GA report modified the average consumption rate to 4.6 HCF which reflected a reduction in consumption and was until 2006. In the 2006 GA report, staff found an upward adjustment to the average consumption rate was warranted and increased the rate to 4.85 HCF.

The 2009 and 2010 costs reflect an average consumption factor of 4.85 HCF per unit per month. The Water Department estimates that water consumption is currently 6% less than last year. Staff's analysis of consumption for the two sets of properties tracked since 1997 also reflects a decrease in water consumption. This downward trend is shown in the Water Consumption Table below. The table also shows that consumption has been decreasing since 2007. At this time, staff does not recommend making a downward adjustment to the consumption rate. Staff will continue to monitor water consumption for these properties and if over the course of the next year the consumption rates continue to decrease, staff will consider adjusting the average consumption factor in next year's GA report. Any changes to the consumption factor will also require an adjustment to the average per unit cost.

Staff usually reviews consumption and costs for the six billing periods (twelve months) immediately preceding the issuance of the GA report and compares those averages to the consumption and costs for the prior year. Last year, to more accurately reflect the effect of the new rate structure that was implemented in the first billing cycle that ended after August 1, 2008, staff reviewed consumption and costs for three billing cycles (six months) which incorporated the new rate structure and compared it to the same three billing cycles from the prior year.

Water Consumption Table

Year*	Average HCF used in GA	Avg. HCF 1 st Group	Avg. HCF 2 nd Group
1997	5.0	4.83	4.56
1998	5.0	4.65	4.54
1999	5.0	4.66	4.51
2000	4.6	4.65	4.34
2001	4.6	4.77	4.42
2004	4.6	5.30	4.61
2005	4.6	5.04	4.52
2006	4.85	4.96	4.68
2007	4.85	5.00	4.71
2008	4.85	4.81	4.64
2009	4.85	(old rate) (new rates) 4.62 4.79	(old rate) (new rates) 4.43 4.45
2010	4.85	4.81	4.10

*The study was not performed in 2002 and 2003.

For 2009 the average HCF for both groups before and after the rate changes authorized by the new rate structure indicates consumption has continued to drop. (Once the new rates were implemented, consumption levels did increase somewhat for both groups, but still reflected a decrease from the 2008 consumption levels.). In 2010 the consumption average for Group 1 increased slightly over last year (4.81 HCF) but is still less than the average HCF of 4.85, while consumption for Group 2 decreased significantly (4.10 HCF). The overall average for both groups is 4.41 HCF.

The two sets of properties staff reviews to evaluate consumption rates and water/sewer costs include 128 properties with 1,181 units. Staff believes these properties provide a good representation of water consumption in controlled rental units. The table below shows the number of properties, the number of units and what percentage of each group's units is within the seven city areas defined by the Rent Control Board for various analyses. In most instances, the groups' percentages are similar to the overall distribution of controlled units within the city areas.

City Area	1 st Group 55 properties/578 units			2 nd Group 73 properties/603 units			
	% of all units by area	Number of properties	Number of units	% units in area	Number of properties	Number of units	% units in area
A	17%	11	92	15.92%	8	65	10.78%
B	12%	8	43	7.44%	5	24	3.98%
C	4%	1	42	7.27%	1	10	1.66%
D	10%	6	51	8.82%	9	58	9.62%
E	19%	14	128	22.15%	18	138	22.89%
F	16%	5	116	20.07%	8	117	19.40%
G	22%	10	109	18.34%	24	191	31.67%

Gas – Common Areas Only

Average Costs

The average gas expense includes the actual cost of gas which is made up of a procurement cost (cost of the gas itself which changes monthly) and a transmission charge (cost for delivering gas to homes), and several incidental charges which include a daily charge, a surcharge for Low Income Discount Rate Surcharge (Public Purpose Programs) and a surcharge for the State Regulatory Fee (Public Utilities Commission Reimbursement Fee), and a 10% Santa Monica Utility Tax.

Cost of Gas

The average of gas costs in a twelve month period is used to calculate the overall effect of 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.

Procurement Cost: The average procurement cost for the most recent twelve months (April 2010 back through May of 2009) is .421881. The average for the prior twelve month period was 0.690945. Overall, for the most recent twelve month period the average monthly procurement cost is 38.39% less than the average cost for the prior twelve month period.

The chart shows the monthly procurement rates for the most recent twelve months and for the twelve month period considered in last year's report. The table shows that beginning in January 2010, the monthly procurement costs were higher than the prior year's. However, more significant is the difference in the procurement costs from May 2009 through December 2009. For

that eight month period, the costs for 2009 were lower than the costs for the same time period the prior year, particularly for the months of May through July (i.e. May 2009 cost was \$0.26 cents per therm while the May 2008 cost was \$1.08, a decrease of 75%.

Monthly Procurement Costs

Time Period	Core Procurement Gas Price (Cents Per Therm)	
	2009/2010	2008/2009
April	.44552	.31010
March	.42429	.36491
February	.59331	.40063
January	.57867	.55448
December	.49786	.55352
November	.47143	.45595
October	.39651	.67960
September	.29807	.68874
August	.39354	.87751
July	.35516	1.22663
June	.33896	1.09483
May	.26925	1.08444
Average	0.421881	0.690945

Transmission Charge: The annual transmission charge for this period is .310400 which is 0.1984 more than last year's charge for of 0.290560.

The total cost for gas per therm (procurement cost + transmission charge).732281 (.421881 + .310400). This is the amount used to calculate the estimated cost for gas for 2010 and is .182769 less than the prior twelve month period.

	2009/2010	2008/2009
Average procurement cost	0.421881	0.690945
Transmission Charge	<u>0.310400</u>	<u>0.290560</u>
Per Therm cost	0.732281	0.981505

To calculate the average monthly cost of gas per unit, a consumption level of 16.036 therms per unit/per month is used. This consumption level was established in the 2003 general adjustment report and was related to a modification of the gas component per Dr. Baar's recommendation in 2002.¹¹

¹¹ In the 2002 GA report, Dr. Baar recommended modification of the average gas component to equal \$9.62. 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. A random sampling of 258 buildings with 3369 apartment units indicated the average monthly gas cost was \$9.62 per apartment unit. In the 2003 GA report staff incorporated Dr. Baar's recommendation and modified the total 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). The \$9.62 gas cost reflects a consumption level of 16.036 therms per month per apartment.

The projected cost for gas for 2010 without incidental charges is \$12.92 (2010 per therm cost of \$0.732281 x 16.036 therms = \$11.74 plus 10% tax = \$12.92). This is \$4.39 less than last year's gas-only cost. In order to calculate the total cost for gas, the incidental charges must be added to the gas-only cost. The incidental charges are discussed below.

Incidental Charges

Only one of the items included in the incidental charges realized a rate change since last year. Effective January 1, 2010, the Public Purpose Program surcharge was increased by \$0.00885 cents (from .06384 cents per therm to .07269 cents per therm). This change resulted in an overall increase of \$0.16 to the incidental charges. The projected cost for incidental charges for 2010 is \$6.72.

Total Monthly Gas Cost

The gas cost and incidental charges for 2009 and 2010 are shown below. The 2010 estimated cost is **17.77%** less (-\$4.24) than 2009.

	2009	2010
Gas	\$17.31	\$12.92
Incidentals	<u>6.56</u>	<u>6.72</u>
	\$23.88¹²	\$19.64¹³

Electricity – Common Areas Only

Average Costs

Through 2008, the common area electricity cost used in the general adjustment report has been based on figures provided in Southern California Edison's rate sheet known as Schedule D.¹⁴ Last year, according to an SCE representative, customers with house meters who were previously on Schedule D were in the process of being switched to Schedule GS-1. Currently an SCE representative reported that most of the qualifying properties were likely to have been converted to the new schedule sometime at the end of 2009.

¹² April 2009 Cost \$17.31 (16.036 therms x .981505 baseline rate = \$15.74 + \$1.57 [10% tax]) + incidentals \$6.56 (daily service rate [30 days x .16438] + State Regulatory Fee [16.036 therms x .00068] + Low Income Discount Rate Surcharge [16.036 therms x .06384] = \$5.97 + \$0.59 [10% tax]) = **Total cost \$23.88.**

¹³ April 2010 Cost \$12.92 (16.036 therms x .732281 baseline rate = \$11.74 + \$1.17 [10% tax]) + incidentals \$6.72 (daily service rate [30 days x .16438] + State Regulatory Fee [16.036 therms x .00068] + Low Income Discount Rate Surcharge [16.036 therms x .07269] = \$6.11 + \$0.61 [10% tax]) = **Total cost \$19.64.**

¹⁴ In 2002, the average monthly cost per unit for common area electricity was set at \$10.68. The general adjustment reports for 2003 and 2004 did not project any additional changes to this component. In 2005, per Assembly Bill (AB)1X, Southern California Edison issued Regulatory Advice letter #1886-E, which resulted in a roll-back of rates to the February 2001 rates for Tier 1 (baseline) and Tier 2 (non-baseline level 1). As a result of the roll-back, the Board adjusted the cost for electricity to \$10.46. This is the amount used until 2009 as the rates for Tiers 1 and 2 of Schedule D were been limited to the 2001 levels until March 1, 2010 when Senate Bill (SB) 695, provided for increases of 3% for Tiers 1 and 2 of Schedule D.

Last year staff increased the average cost for this component based the conversion of properties with “house meters” to the GS-1 schedule. The result was an increase of 21.49% to the 2008 cost which led to the estimated cost for 2009 of \$12.71.

For 2010, staff applied the difference between, the current composite cost for the GS-1 schedule (17.5 cents per kWh) and last year’s cost (17.3 cents per kWh). The difference is an increase of 1.16% or \$0.15. When applied to the 2009 cost of \$12.71 the result is \$12.86. This is the amount projected for 2010.

Consumption

This year, staff reviewed documentation related to electricity costs submitted to the Board in recent years by owners filing increase petitions. The documentation suggests that actual average consumption levels and average per unit costs may be somewhat less than the amount projected for this component. Because the sample documentation is limited it is not sufficient to consider adjusting the estimated cost for this component. In an effort to obtain more information, staff again requested consumption information from SCE.

SCE reported that for 1,973 properties on the GS-1 schedule, the average monthly consumption was 388 kWh and the average cost was \$82 per month. The consumption average is approximately the same as the amount reflected in the increase petition documentation, while the cost is somewhat higher. SCE is unable to provide additional information about the number of units on each of the 1,973 properties included in their data and therefore this information is limited in its usefulness.