The Impact of Market Rate Vacancy Increases – Four-Year Report

January 1, 1999 - December 31, 2002

Santa Monica Rent Control Board
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IMPACT OF MARKET RATE VACANCY INCREASES

SUMMARY

On January 1, 1999 vacancy decontrol-recontrol began and owners were allowed to raise the rents on vacant units to market rate. The law has now been in effect for four years.

During the first year (1999), owners filed 3,796 vacancy market increase forms with the Rent Control Agency. Excluding multiple registrations on the same unit, 3,192 units were impacted. During the second year (2000), 3,684 market increase forms were filed, impacting an additional 2,487 units for the first time. In the third year (2001), 3,669 market increase forms were filed, impacting an additional 1,828 units for the first time. In the fourth year (2002), 3,730 market increase forms were filed, impacting an additional 1,729 units for the first time. Additionally, in 2002 market rate rent levels were registered on approximately 250 unsold TORCA units. Taken together, first time market rate rentals were registered on 1,979 units in 2002.

By the end of the fourth year, 9,486 units had been rented at market rates. This represents 35% of the controlled rental units for which the Agency has registered rents. (Units with exemptions at the unit level and unregistered rents are excluded from the total.) The Agency's records indicate that 17,961 units (65%) have not received market rate increases. For comparison, at the end of 2001, 27% of the units (7,507 units) had been rented at market rate. Therefore, another 8% of the controlled units were rented at market rates during 2002.

The impact of the increases on rents is explored in this report and is summarized below.

- Excluding multiple increases on the same unit, 9,486 units have received market increases. In the first three years, the number of new units affected decreased each year (3,192 in 1999, 2,487 in 2000 and 1,828 in 2001). However, in 2002, the number of units rented at market rate for the first time increased slightly from 2001, with 1,979 units impacted. This number includes approximately 250 unsold TORCA units.[1]
- Upon re-rental, median MARs have increased from $612 to $896 (46%) for 0-bedroom units, from $695 to $1,195 (72%) for 1-bedrooms, from $889 to $1,606 (81%) for 2-bedrooms and from $1,131 to $2,074 (83%) for 3+ bedroom units.

[1] Pursuant to a change in state law, owners were required to register rents on unsold condominium units. These units reflect market rate rentals established since January 1, 1996.

- Depending on the number of bedrooms in a unit, the household income needed to "afford" the median market rent at 30% of gross income is from $51,200 to $76,461. This is $16,200 - $34,700 higher than the income needed to afford the median rent of the same size unit if it had not been rented at market rate.
- Vacancy increases on 9,486 units have resulted in the loss of 6,506 units that had rent levels formerly affordable to low-income households (80% of median income) including 3,950 units with rent levels formerly affordable to very low-income households (50 and 60% of median income).[2]
- Before the increases, 79% (7,528 units) of the 9,486 units that have been rented at market rate were affordable to low-income households. After the increases, just 11% (1,022 units) remained affordable at the low-income level.
- Before the increases, 20.6% of these 9,486 units were only affordable to households with a moderate income or above (100% of median and above). After the increases, 89.2% of the units were only affordable to households at the moderate-income level or above.
- Market rate vacancies continue to be distributed throughout the city, roughly paralleling the distribution of all controlled rental units.
- Market rate rentals have been distributed between 0, 1, 2 and 3 or more bedroom units in approximately the same proportion as their occurrence in the City as a whole.
- Once a unit is rented at market rate, the tenant has less incentive to stay in place and therefore the unit may receive subsequent increases in a relatively short period of time. At the end of the fourth year, 2,377 units had two reported increases, 733 units had three reported increases, 220 units had four reported increases and 76 units had five or more reported increases.
- Vacancy-related increase forms were filed at approximately the same rate in each of the four years. In all years, the heaviest filing period was July – September.

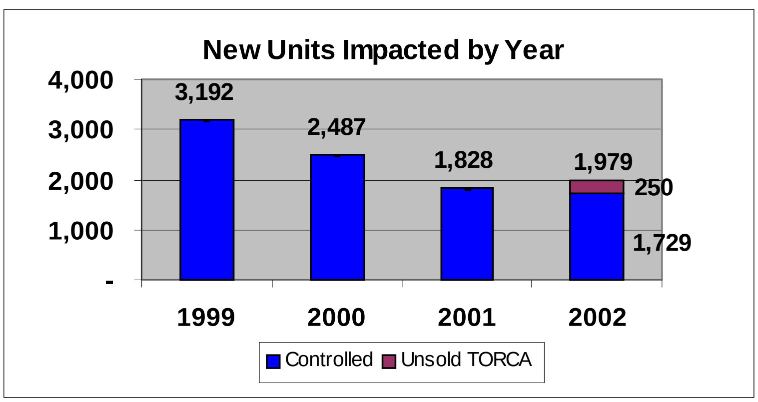
[2] See page 10 Affordability Standards, for the maximum income at each level.

This report analyzes the 9,486 units that received market increases in the first four years of vacancy decontrol. It compares units that have received vacancy increases to units of the city as a whole and details the impact of increases on rent levels and affordability.

Rates of Filing – Units Impacted

In the first four years of vacancy decontrol, 9,486 units experienced at least one market-rate increase. In the first three years, the number of new units impacted declined each year. During calendar year 1999, 3,192 units were impacted by market rate increases. In 2000, 2,487 units received market increases for the first time. In 2001, 1,828 units received their first market rate increase. In 2002, the number of units impacted for the first time increased slightly above 2001 with 1,979 units impacted.

One explanation for the increase in units impacted in 2002 was a change in state and local law that required owners of unsold TORCA units to register established market rate rents for these units. Of the 1,979 units impacted in 2002, approximately 250 were unsold TORCA units. Taking these units out of the total, 1,729 new units were impacted for the first time and the declining trend of new units impacted each year continued in 2002. The table below shows the number of new units impacted in each year of vacancy decontrol.



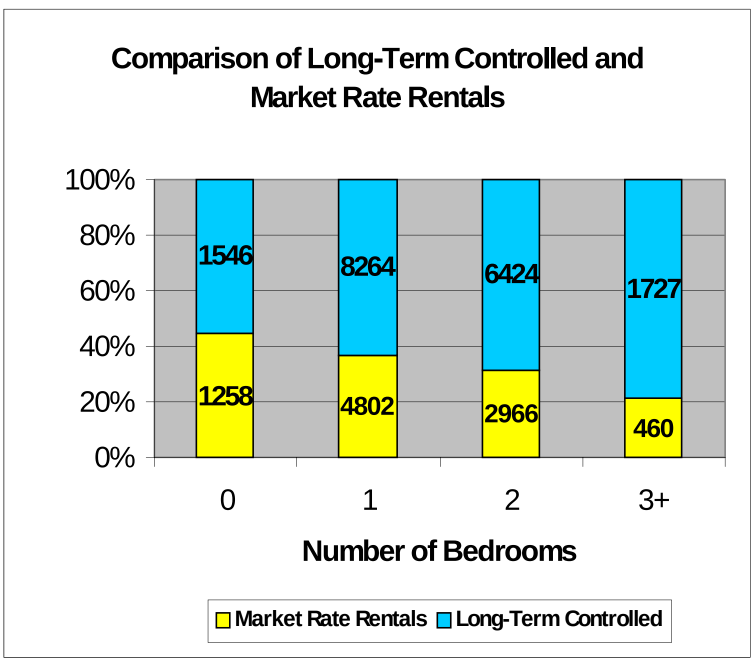
Vacancy Increase Registration Forms have been filed at approximately the same rate each year: 3,796 in 1999; 3,684 in 2000; 3,669 in 2001 and 3,730 in 2002. During the first six months of 2002, approximately 287 forms were filed per month. Following the Agency's annual June mailing in which owners received reports of current rent levels on file with the Agency, an average of 444 forms were filed per month during the third quarter (July – September 2002). During the final quarter, filings dropped to an average of 226 per month. The same approximate pattern of filings was observed in previous years with the largest number of forms filed in July and August every year.

Market Rate Rentals by Unit Size

This year the market rate rentals were evaluated to determine if certain size units (i.e. number of bedrooms) were being impacted disproportionately by vacancy increases. As the table below shows, almost half the controlled units are one-bedroom units. Slightly more than half of all the market rate rentals have been in one-bedroom units. The next largest group of units is 2-bedrooms (34% of total) and 31% of the market rate rentals have been in 2-bedroom units. While 0-bedroom units (singles) make up just 10% of the controlled housing stock, 13% of the market rate rentals have been in these units. Finally, just 8% of the housing stock is made up of units with 3 or more bedrooms, and only 5% of the market rate rentals have been on these units. Given the desirability of larger units and the tenants' incentive to remain in those units, it is not surprising that just 5% of the market rate rentals have been on the largest units.

Number of Bedrooms	0	1	2	3+
Percentage of Units Overall	10	48	34	8
Percentage of Market Rentals	13	51	31	5

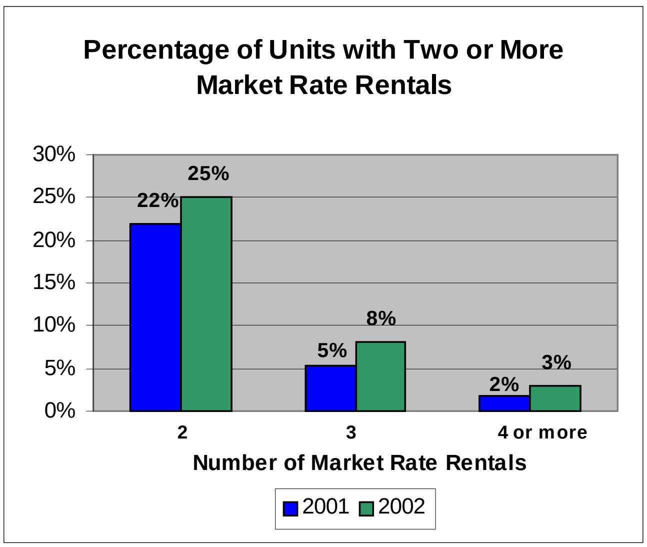
The graph below shows for each unit size (number of bedrooms) the number of units that have been rented at market rate (yellow) and the number of long-term controlled units (blue). Of the 2,804 total 0-bedroom units, 45% (1,258) have been rented at market rate. Of the 13,066 total one-bedroom units, 37% (4,802) have had vacancy rent increases. Of the 9,390 total 2-bedroom units, 32% (2,966) have been rented at market rate. And, not surprisingly, just 460 (21%) of the total 2,187 three or more-bedroom units have been rented at market rate.



Multiple Increases per Unit

In addition to the 1,979 units that were impacted by market rate vacancy increases for the first time in 2002, there are now 3,406 units that have been rented at market rate two or more times: 2,377 units with 2 market rentals; 733 units with 3; 220 units with 4; and 76 units that have been rented at market rate 5 or more times. Overall, 64% of the affected units (6,080) had a single vacancy increase. Thirty-six percent of the units had two or more increases: 25% had 2; 8% had 3; and 3% had 4 or more increases.

The graph below shows the breakdown for the units with two or more market rate increases at the end of 2001 and 2002. At the end of 2001, 29% of the market rate units had been rented two or more times. By the end of 2002, 36% had two or more increases. The increase in units with more than one market rate increase shows that once a unit is rented at market rate, it is likely to receive subsequent increases in a relatively short period of time.



Units with multiple turnovers (4 or more) are primarily in buildings that are dissimilar from the rental housing stock as a whole. For the most part, they have occurred in large buildings (more than 50 units), buildings near the beach, and buildings that advertise as "corporate housing". Although the larger buildings may have had several units turn over multiple times, in most smaller buildings just one unit has been rented at market rate multiple times.

As is noted in the section on "Loss of Affordable Units by Income Level", affordability to low-income people is generally lost with the first market rate increase (affordability is lost in 70% of the cases). Therefore, the filing of a subsequent market rate increase on the same unit usually does not result in the additional loss of an affordable unit.

Impact on Median MARs[3]

The chart below summarizes median rent information for the 9,486 units that received market rate increases between January 1, 1999 and December 31, 2002.

Vacancy Increases 1/1/99 – 12/31/02 (9,486 units)

Number of Bedrooms	**Adjusted 1998[4]** Median MARs	**Post-Increase** Median MARs	Dollar Amount Change	% Change
0	$612	$896	$284	46%
1	695	1,195	500	72
2	889	1,606	717	81
3 or +	1,131	2,074	943	83

Since January 1, 2002, 1,979 units have been impacted by market rate increases for the first time. This is in addition to 7,507 units that received market rate increases between January 1, 1999 and December 31, 2001. The post-increase medians above reflect the cumulative effect of four years of rentals at market rate.

The chart details rents based on the number of bedrooms in the units. The second column is the median rent in effect as of December 1998 (before any market rate increases were implemented) with the 1999 – 2002 general adjustments added. Adding the general adjustments allows a comparison of what the medians of these 9,486 units would be as of December 2002 if they had not received vacancy increases. The next three columns reflect the median rent after the market rate increases, the dollar amount of the change from the pre-increase adjusted rent and the percentage change.

0-Bedroom Units:

Twelve hundred and fifty eight (1,258) 0-bedroom units have received market rate increases since January 1, 1999: 490 in 1999; 301 in 2000; 221 in 2001 and 246 in 2002. Without market rate increases, these 1,258 units would have a 2002 median rent of $612. With the market increases, the median rent is $896, an increase of $284 or 46%.

1-Bedroom Units:

Four thousand eight hundred and two (4,802) one-bedroom units have received market rate increases in the last four years: 1,684 in 1999; 1,265 in 2000; 922 in 2001 and 931 in 2002. Without market rate increases, these 4,802 units would have a 2002 median rent of $695. With the market increases, the median rent is $1,195, an increase of $500 or 72%.

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[3] Median rent levels (the point at which half the rentals were higher and the other half were lower) are used throughout this report because they are considered more statistically accurate than average rents. Medians filter out the effect of rents at the extreme high and low ends.

[4] December 1998 median MARs with 1999-2002 general adjustments added.

2-Bedroom Units:

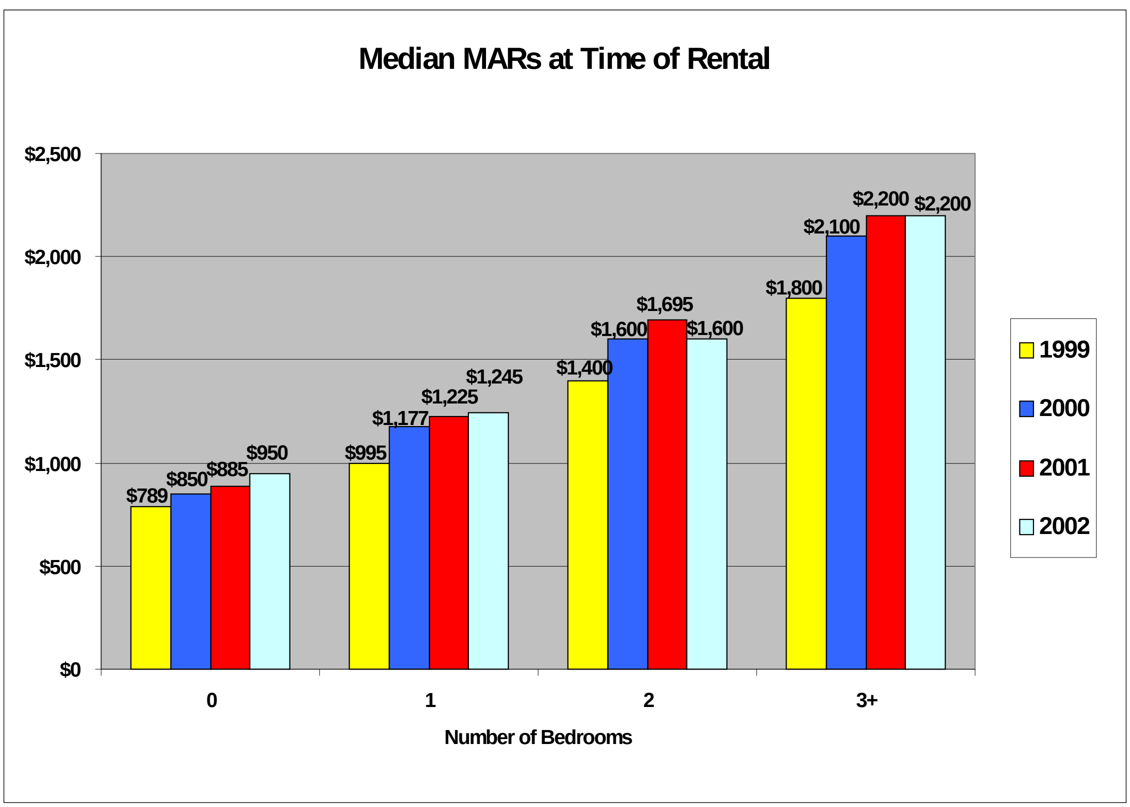
During the last four years 2,966 two-bedroom units have received market increases: 891 in 1999; 797 in 2000; 596 in 2001 and 682 in 2002. Without market rate increases, these 2,966 units would have a 2002 median rent of $889. With the market increases, the median rent is $1,606, an increase of $717 or 81%.

3 or More- Bedroom Units:

There are 460 three or more-bedroom units that have received market rate increases since 1999: 127 in 1999; 124 in 2000; 89 in 2001 and 120 in 2002. The current median rent of all three plus-bedroom units that have received market increases is $2,074. This is an increase of $943 over the adjusted pre-increase median rent of $1,131, an increase of 83%.

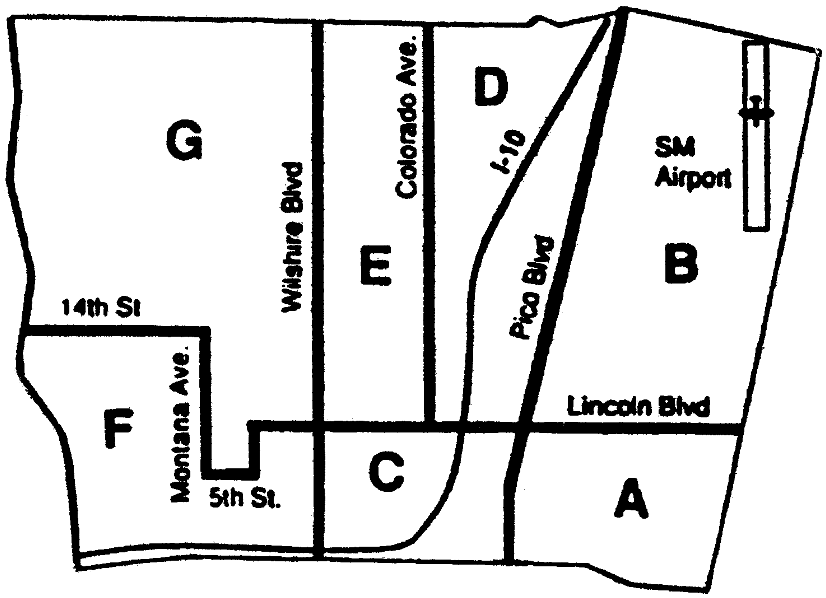
Median MARs at Time of Rental

While the median rents at time of rental for 0 and 1-bedroom units have increased each year since vacancy decontrol started, this year the median rent at time of rental for 2 bedroom units decreased from $1,695 to $1,600 and the median rent for 3-bedroom units remained steady at $2,200. The graph below shows the median rent levels by bedroom at the time they were established each year for both initial market rate rentals and re-rentals. These rents do not include general adjustments that would have been allowed for units rented in 1999, 2000 and before September 2001.



Median MARs by City Area

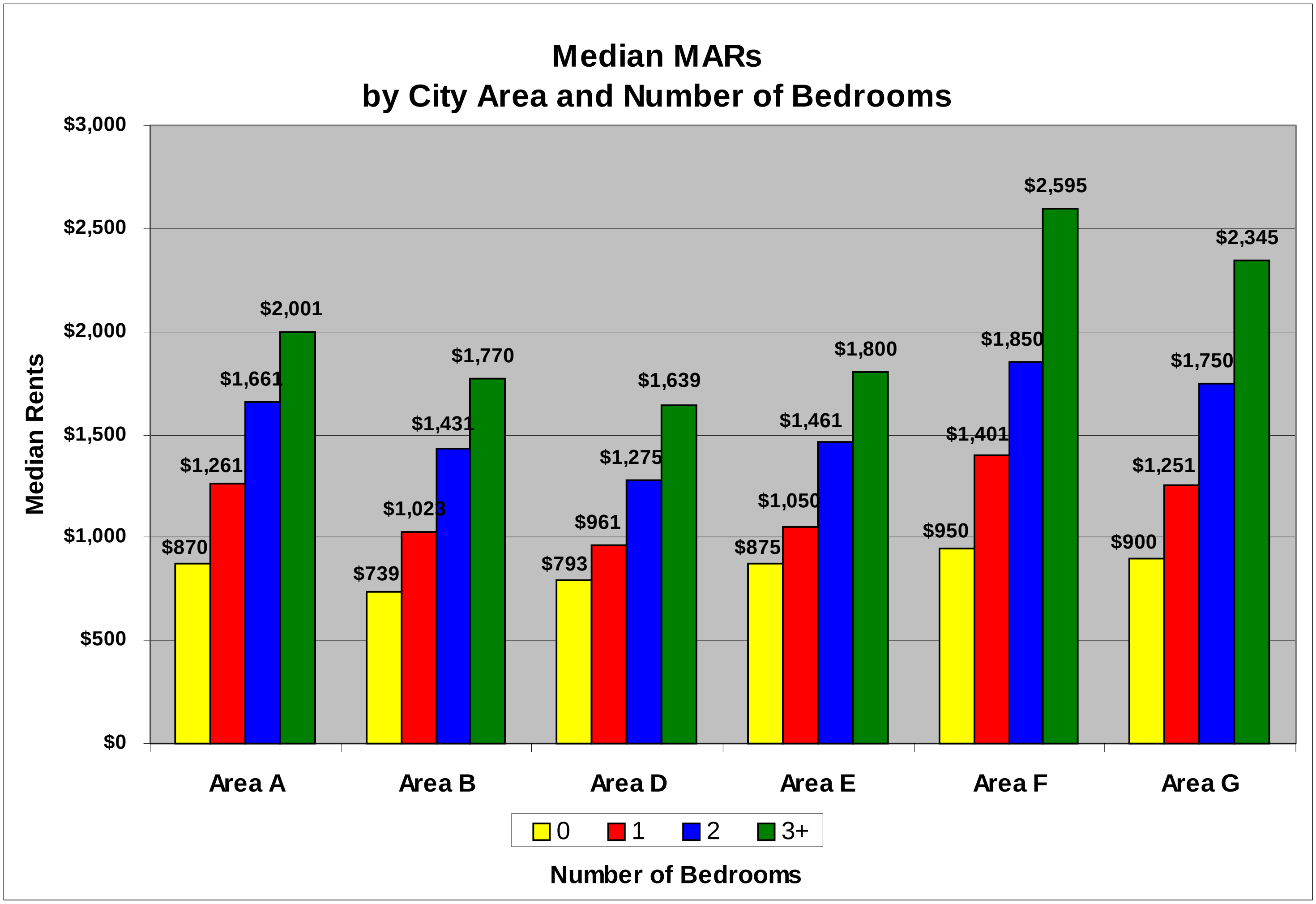
To track changes in the housing stock in different areas of the city, the Rent Board divided the city into seven areas which parallel neighborhoods and census tracts. The map below shows the city areas identified as A-G.



As the table below shows, the distribution of units rented at market rate over the four years of vacancy decontrol closely parallels the distribution of rental units throughout the city overall.

City Area	A	B	C	D	E	F	G
Percentage of Units	17	12	4	10	19	16	22
Percentage of Market Rentals	17	12	5	8	20	16	22

The graph on the following page details the market rate median rents by number of bedrooms for areas A, B, D, E, F and G. Area C is omitted because the majority of market rate rentals in this area have been in two very large buildings (120 units and 288 units) located on Ocean Avenue. Area C has such a small number of controlled rental units (just over 900) that these two buildings account for more than one-third of all controlled units in this area. Because of the small size of this area and the distorting impact of these two buildings, rents for this area are not included. These buildings, both in their size and character, are not representative of most buildings throughout the city and the market rent levels registered have been significantly different from those in the other areas.



Affordability Standards

HUD affordability standards assume 30% of a household's gross income may be used for rent before the household becomes "rent burdened". For the year 2002, the HUD median income for a "Four-Person Household" in Los Angeles County is $55,100 (up from $54,500 in 2001). The maximum income levels for a four-person household at 50%, 60%, 80%, 100% and 120% of median income are shown on the table below:

Very Low 50%	Very Low 60%	Low 80%	Moderate 100%	Moderate 120%
$27,550	$33,060	$44,100	$55,100	$66,100

Translating Affordability into Income

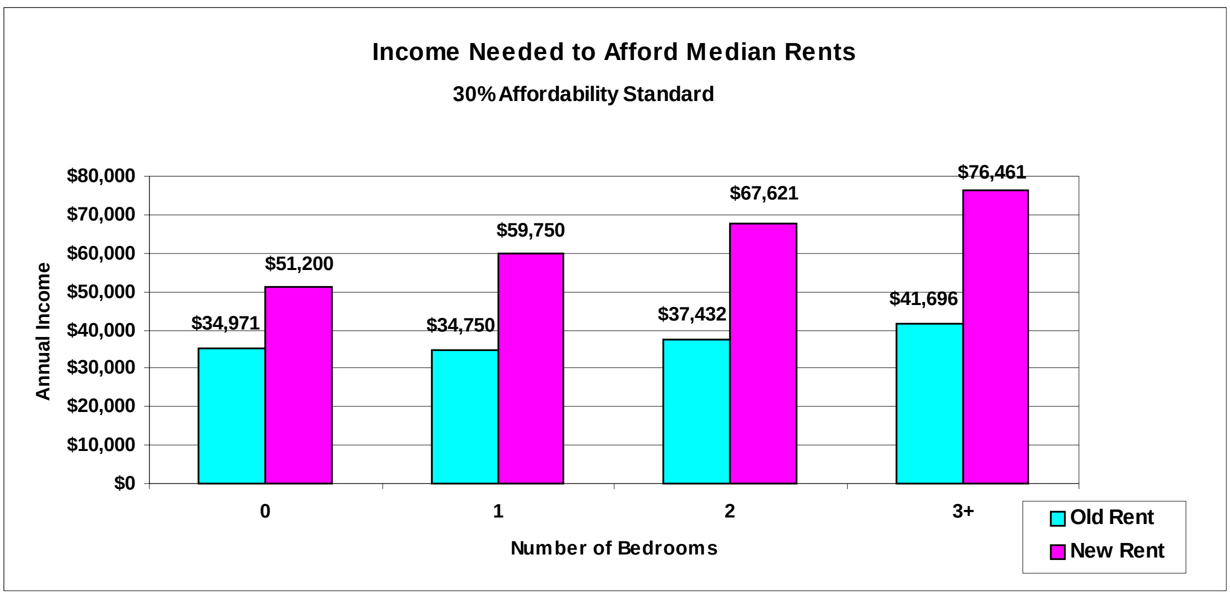
Using HUD affordability calculations that include adjustments for number of bedrooms[5], staff calculated the minimum income required to afford the median rents.

The chart below shows the *minimum* total household income needed to pay for the median rents without being rent burdened. The light blue numbers show the median income needed today to afford the various units if they had not been rented at market rate. The pink numbers show the median income necessary to afford the market rate rent levels.

Income Needed to Afford MARs (30% Affordability Standard)
Units with Vacancy Increases 1/1/99 – 12/31/02 (9,486 units)

No. of Bedrooms	Adjusted 1998[6] Median MARs	Income needed to Afford MAR	Post-Increase Median MARs	Income Needed to Afford MAR	Income Difference
0	$612	$34,971	$896	$51,200	$16,229
1	695	34,750	1,195	59,750	25,000
2	889	37,432	1,606	67,621	30,189
3 or more	1,131	41,696	2,074	76,461	34,765

As the chart above shows, depending on size of a unit, the household income needed to “afford” the median market rent is $16,200 - $34,700 higher than the income needed to afford the median rent of that same size unit if it had received a market rate increase.



[5] A HUD-determined Household Adjustment Factor is used to calculate the income needed to afford the MAR and results in the unexpected difference for the 0 and 1-bedroom units.
Income Calculation = annual rent/household adjustment factor/affordability standard

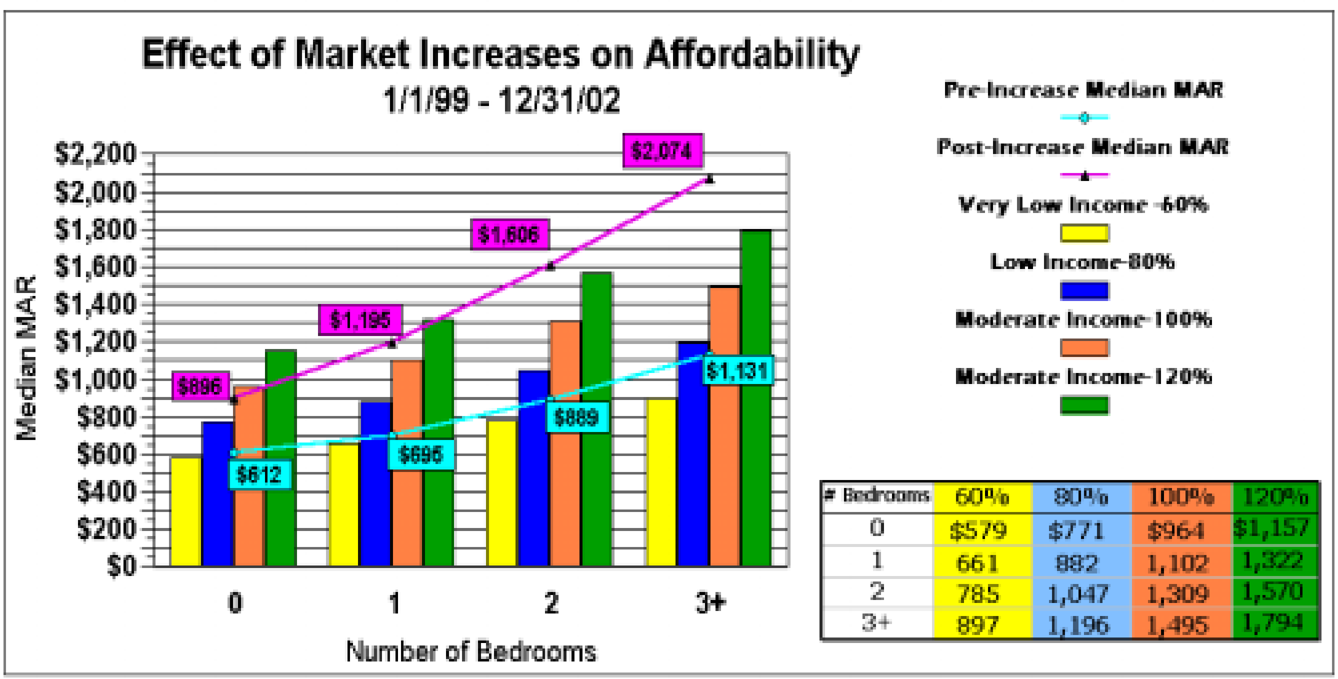
[6] December 1998 median MARs with 1999-2002 general adjustments added.

Loss of Affordability – 1/1/99 - 12/31/02

Affordable units have been lost at every affordability level and every bedroom size as a result of market rent increases since January 1, 1999. For the 9,486 units that have received market increases, their pre-increase median MARs at all bedroom sizes (with 1999-2002 general adjustments added) would be affordable to a household whose income is 80% of the adjusted County median. *None* of the post-increase medians are affordable to a family making 80% of median income.

After the increase, the median MARs of 0-bedroom units are affordable only at 100% of median and above. Even more significantly, the median rents for 1, 2 and 3 bedroom units are no longer affordable even at 100% of median income. (The median MAR for a 3-bedroom unit is $579 above the amount affordable at 100% of median income.) In addition, the median MARs of 2 and 3-bedroom units are no longer affordable even to households at 120% of the median income. (The median MAR for a 3-bedroom unit is $280 above the amount affordable at 120% of median income.)

This information is shown in graph form below. The bars represent the rents affordable to households with incomes at 60%, 80%, 100% and 120% of the adjusted county median. The chart shows the corresponding rents affordable for each of the four household sizes. The light blue line shows the pre-increase median MARs (with 1999-2002 GAs) and the purple line shows the post-increase median MARs for the various bedroom sizes. In order for a unit to be affordable, the top of the bar representing that income category must be above the line representing the median MARs. The table shows that the post increase median rents are higher than the affordable rents for almost every income category and bedroom size.



# Bedrooms	60%	80%	100%	120%
0	$579	$771	$964	$1,157
1	661	882	1,102	1,322
2	785	1,047	1,309	1,570
3+	897	1,196	1,495	1,794

<u>Loss of Affordable Units by Income Level</u>

The 9,486 units impacted by market rate increases had a mixture of rents affordable to families at all income levels before the increases were implemented. Forty-four percent (44%) of these units, or 4,152 of the units, were affordable to families with very low incomes, i.e., families with incomes at 60% of median or less. Seventy-nine percent (79%) of the units, or 7,528 of the 9,486 units, were affordable to low-income people, i.e., households with incomes at 80% of the median income or less.

After the market rate increases, the 44% of the units with rents affordable to households with 50% and 60% of median income had shrunk to 2%, or 202 units. This represents a loss of 3,950 units that had been affordable to very low-income households that are no longer affordable to those households.

Following the market rate increases, of the 79% of the units that had been affordable to low-income families (i.e. 80% of median income), just 11% remained affordable at this income level. This represents a reduction from 7,528 affordable units to just 1,022, <u>a net loss of 6,506 units affordable to low-income households</u>.

Before the market rate increases, 92% of the units (8,755) were affordable to households at moderate (100% of median) income levels. After the increases, only 34% of the units remained affordable at the 100% income level. This represents a decrease from 8,755 units affordable at this level to 3,255 units now affordable to families with moderate-income levels (a loss of 5,500 units).

Before the market rate increases, just 8% of the units (731) had rents affordable only to families with incomes at 120% or more of median income. After the market rate increases, 66% of the units (6,231) are now in this category and are only affordable to families at 120% of median income or greater. This represents an increase of 5,500 units in this category.

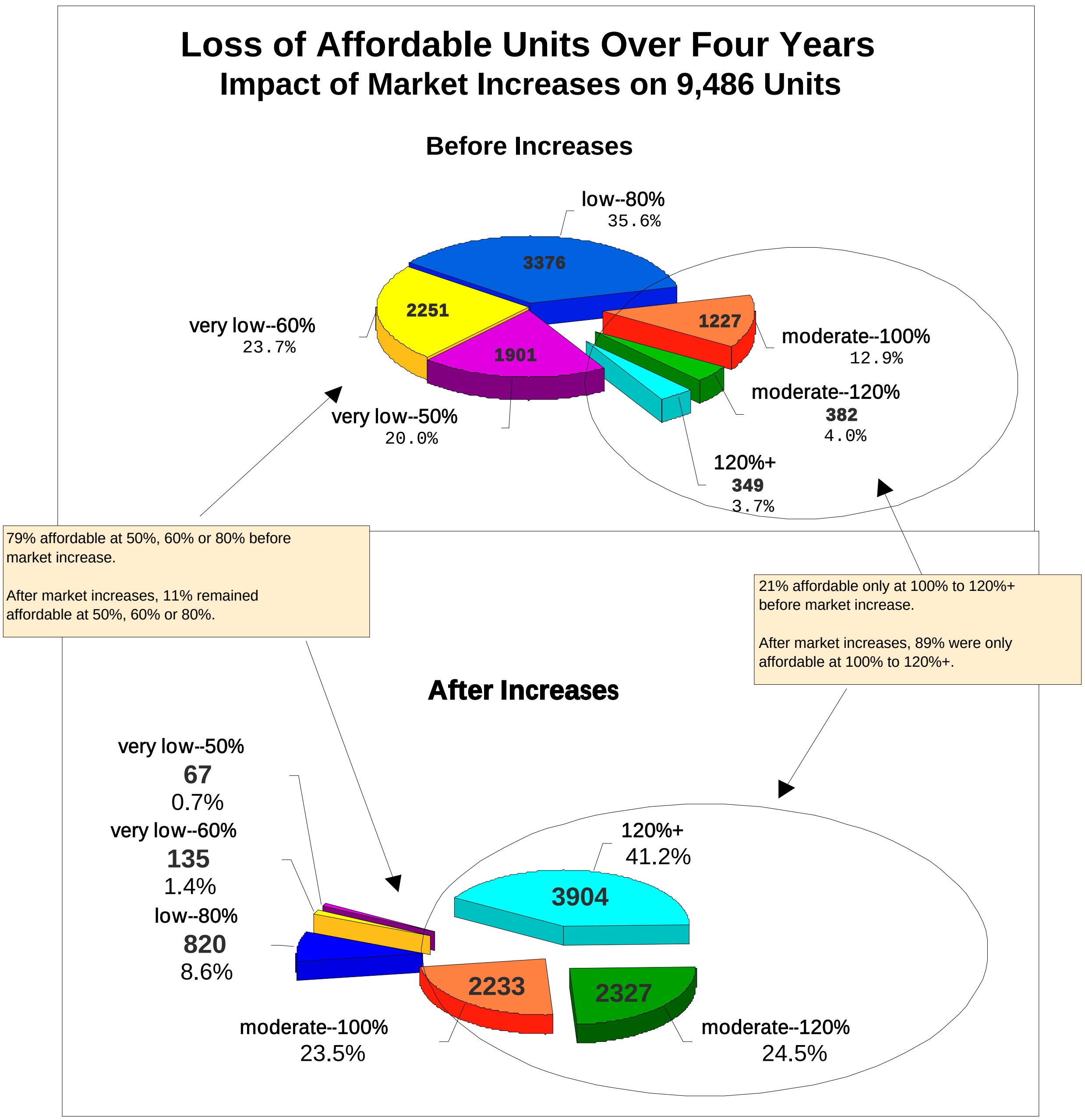
In summary:

- Before the increases, 44% of the units had median rent levels affordable to **very-low income** households. After the increases, only 2% of the units remained affordable to these households. This represents a loss of affordability of 3,950 units.
- Before the increases, 79% of the units had median rent levels affordable to **low-income** households. After the increases, only 11% of the units remained affordable at this income level.
- Before the increases, households with **moderate-income** levels could afford 92% of the units. After the increases, only 34% remained affordable to these households.
- Before the increases, 8% of the units were affordable only to families with **incomes at 120% of median or more**. After the increases, 66% of the units are affordable only to people making 120% or more of median income.

The following charts detail the dramatic shift in affordability levels for the units that have received market rate rent increases.

Distribution of 9,486 Units Before and After Increases

Affordability Category	Number of Units Before Increases	Number of Units After Increases	Difference
Very Low – 50%	1,901	67	-1,834
Very Low – 60%	2,251	135	-2,116
Low – 80%	3,376	820	-2,556
Moderate – 100%	1,227	2,233	+1,006
Moderate – 120%	382	2,327	+1,945
120% +	349	3,904	+3,555



CONCLUSION

After four full years of vacancy decontrol/recontrol, 6,506 units that had been affordable to low income households (80% of median income), are no longer affordable to them. Included in this number are 3,950 units no longer affordable to very low-income households (50% and 60% of median income).

As a result of vacancy decontrol, a dramatic shift has occurred in the affordability levels of the 9,486 units that received vacancy increases. Before the increases, 79% of the units had rent levels affordable to low-income households. After the increases, just 11% remain affordable at the low-income level. Additionally, before the increases, just 21% of the units were only affordable to households with moderate-income levels or higher. Today, 89% of the units with market-rate increases are **only** affordable to these households.

The following points show the effect of vacancy-related increases on all controlled units in the city.[7] During the seven years that vacancy increases have been in effect (including the three year phase-in period where rents were eligible to be increased 15% two times upon voluntary vacancy):

- Units with rents affordable to very low-income households (50% of median income) decreased from 11,093 to 5,474, a decrease of 51% (5,619 units).
- Units with rents affordable to very low-income households (60% of median income) decreased from 19,247 to 11,245, a decrease of 42% (8,002 units). This includes 5,619 units formerly affordable at 50% of median.
- Units with rents affordable to low-income households (80% of median income) decreased from 25,676 to 19,006, a decrease of 26% (6,670 units).
- Registration fee waivers held by very low-income seniors decreased from 895 to 521, a loss of more than 41%, between January 1995 and December 2002. This represents a total loss of 374 units since 1995 with 198 of those units lost since 1999 when full vacancy decontrol went into effect.

Despite the significant loss of affordability in those units that have had a vacancy increase, there remain a substantial number of units (approximately 18,000) that have not received vacancy increases and that continue to provide affordable housing.

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[7] In evaluating the loss of units at various affordability levels, the numbers fluctuate from year to year as HUD adjusts the median income level for a “Four-Person Household”. As the median income level goes up, the rent levels affordable at various income levels also go up. The numbers in the first three points compare units affordable in 1995 based on a median income of $51,300 with units affordable in 2002 based on a median income of $55,100.