The Impact of
Market Rate Vacancy Increases
Five-Year Report

January 1, 1999 - December 31, 2003

Santa Monica Rent Control Board
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TABLE OF CONTENTS

Summary	**1**
Units Rented at Market Rates	
Rates of Filing -- Units Impacted	**3**
Rates of Turnover -- Multiple Increases per Unit	**4**
Market Rate Rentals by Unit Size	**4**
Long Term Controlled Units Compared to Market Rentals	**5**
Effects on Rent Levels	
Impact on Median Maximum Allowable Rents (MARs)	**6**
Median MARs at Time of Rental	**6**
Median MARs by City Area	**8**
Effects on Affordability	
Affordability Standards	**11**
Translating Affordability into Income	**11**
Loss of Affordability – 1/1/99 – 12/31/03	**12**
Loss of Affordable Units by Income Level	**13**
Conclusion	**15**

IMPACT OF MARKET RATE VACANCY INCREASES

SUMMARY

The state-initiated vacancy decontrol-recontrol law has now been in effect for five years. Since January 1, 1999, owners have been allowed to raise the rents on most vacant units to market rate.

By the end of the fifth year, 10,929 units had been rented at market rates. This represents 40% of the controlled rental units for which the Agency has registered rents. For comparison, at the end of 2002, 35% of the units (9,486 units) had been rented at market rate. Another 5% of the controlled units were rented at market rates during 2003. The Agency's records indicate that 60% of the rental housing (16,525 units) has not received market rate increases.

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

- The number of new units rented at market rate has decreased each year since 1999 when vacancy decontrol began. The exception to this trend was 2002 when approximately 250 unsold TORCA units were registered due to a change in state law.[1] In 2003, 1,443 new units were rented at market rate for the first time, the lowest number yet for a one-year period.
- 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 fifth year, 42% of the units rented at market rate had turned over at least once since the first market rate rental.
- Upon re-rental, median MARs have increased from \$626 to \$924 (48%) for 0-bedroom units, from \$708 to \$1,231 (74%) for 1-bedrooms, from \$909 to \$1,641 (81%) for 2-bedrooms and from \$1,157 to \$2,109 (82%) for 3 or more bedroom units.
- Depending on the number of bedrooms in a unit, the household income needed to "afford" the median market rent at 30% of gross income ranges from \$52,800 to \$77,751. This is \$17,000 - \$35,000 higher than the income needed to afford the median rent of the same size unit not rented at market rate.

[1] Pursuant to a change in state law, unsold condominium units converted from apartments were again subject to rent level controls after a period of decontrol. These units reflect market rate rentals established since January 1, 1996.

- Vacancy increases on 10,929 units have resulted in the loss of 7,735 units that had rent levels formerly affordable to low-income households (80% of median income) including 4,547 units with rent levels formerly affordable to very low-income households (50 and 60% of median income).[2]
- Market rate vacancies continue to be distributed throughout the city, closely 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.

[2] See page 12 Affordability Standards, for the maximum income at each level.

MARKET RENT INCREASES – JANUARY 1 – DECEMBER 31, 2003

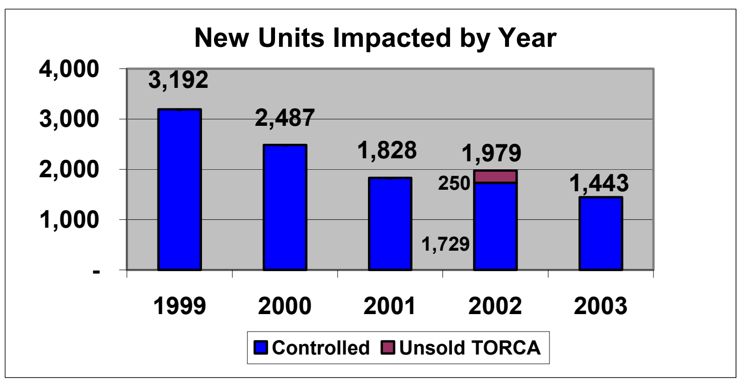
This report analyzes the 10,929 units that received market increases in five years of vacancy decontrol. It compares units that have received vacancy increases to units of the city as a whole and details the impact of increases on rent levels and affordability.

UNITS RENTED AT MARKET RATES

Rates of Filing – Units Impacted

In five years of vacancy decontrol, 10,929 units experienced at least one market-rate increase. As the table below shows, the number of new units impacted each year has declined, with the exception of 2002[3]. In 2003, 1,443 new units were registered as being rented at market rate for the first time. This is fewer than half the units rented at market rate in the first year of vacancy decontrol and the lowest number yet for a 12-month period.

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; 3,730 in 2002; and 3,667 in 2003. As in previous years, the largest number of forms were filed in the third quarter following the Agency's annual June mailing in which owners received reports of current rent levels on file with the Agency. An average of 477 forms were filed per month in July – September 2003.

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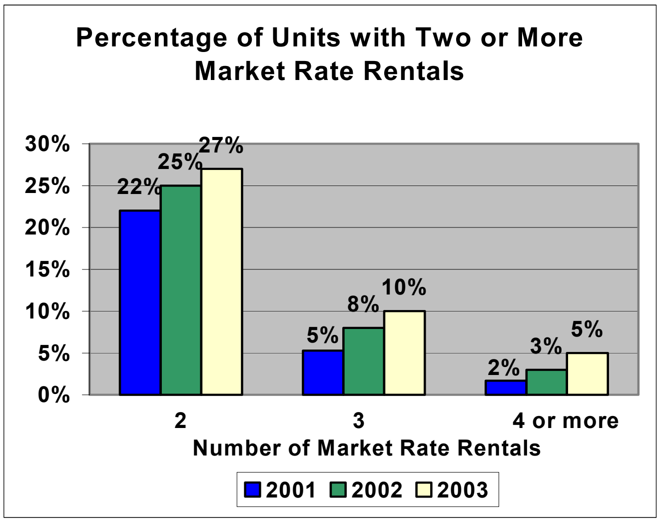
[3] A 2002 change in state and local law required owners of unsold TORCA units to register established market rate rents for these units recontrolled after a period of decontrol. Of the 1,979 units impacted in 2002, approximately 250 were unsold TORCA units. Taking these units out of the total, 1,729 new units were impacted for the first time and the declining trend of new units impacted each year continued in 2002.

Rates of Turnover – Multiple Increases per Unit

The initial expectation that vacancy decontrol would result in a more mobile renter population has proven true once market rents are established. After five years of vacancy decontrol, 42% of the units rented at market rate have turned over at least once since the first market rate rental. Of the 10,929 units rented at market rate, 27% (2,967) have experienced two vacancy increases, 10% (1,096) have had 3, and 5% (750) have 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, 2002 and 2003. The continuing 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.



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. 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.

Market Rate Rentals by Unit Size

Market rate rentals were again evaluated this year to determine if certain size units (i.e. number of bedrooms) were impacted disproportionately by vacancy increases. As the table on the following page 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. 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 3 or more bedroom units.

Although an additional 1,443 units were rented at market rate in 2003, the percentage distributions described here have not changed since the end of 2002.

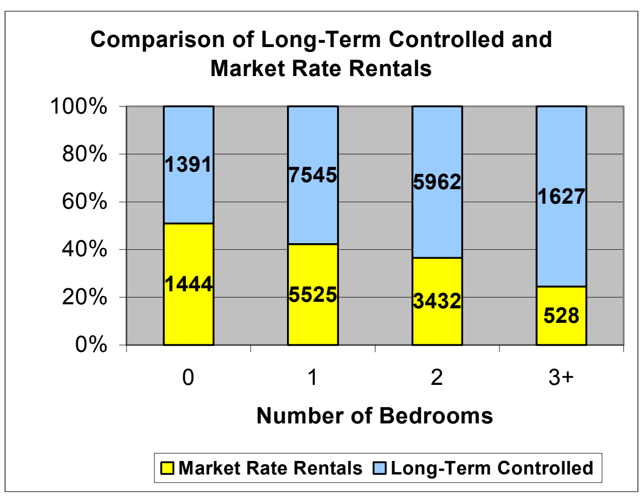
Number of Bedrooms	0	1	2	3+
Percentage of Units Overall	10	48	34	8
Percentage of Market Rentals	13	51	31	5

Long-Term Controlled Units Compared to Market Rate Rentals

Overall, the 10,929 units rented at market rate since 1999 represent 40% of the controlled units for which the Agency has registered rents. For comparison, at the end of 2002, 35% of the units (9,486) had been rented at market rate. Another 5% of the controlled units were rented at market rates during 2003. Agency records indicate that 60% of the units (16,525) have not received market rate increases.[4] The following table shows the percentage of long-term controlled units compared with market rate rentals by unit size and overall.

Number of Bedrooms	0	1	2	3+	OVERALL
Percent Long-Term Controlled Units	49	58	63	75	60
Percent Market Rate Rentals	51	42	37	25	40

The graph below details for each unit size the number of long-term controlled units (blue) and the number of units rented at market rate (yellow). As the table and graph both show, the smaller the unit (number of bedrooms), the more likely it has been rented at market rate. While more than half of the singles have been rented at market rate, just 25% of the three or more bedroom units have experienced market rate rentals.



[4] Excluded from these totals are: units on properties with owner-occupied exemptions (approximately 1,900), units withdrawn under the Ellis Act (approximately 1,500); units that have received removal permits (approximately 1,550); units with various other use exemptions (approximately 2,750); and units that do not have registered base rents because they have been occupied by owners since April 10, 1979 or have received non-rental or commercial exemptions.

Impact on Median Maximum Allowable Rents (MARs)[5]

The chart below summarizes median rent information for the 10,929 units that received market rate increases between January 1, 1999 and December 31, 2003. The post-increase medians reflect the cumulative effect of five years of rentals at market rate.

Vacancy Increases 1/1/99 – 12/31/03 (10,929 units)

Number of Bedrooms	**Adjusted 1998**[6] Median MARs	**Post-Increase** Median MARs	Dollar Amount Change	% Change
0	$626	$924	$298	48%
1	708	1,231	523	74
2	909	1,641	732	81
3 or +	1,157	2,109	952	82

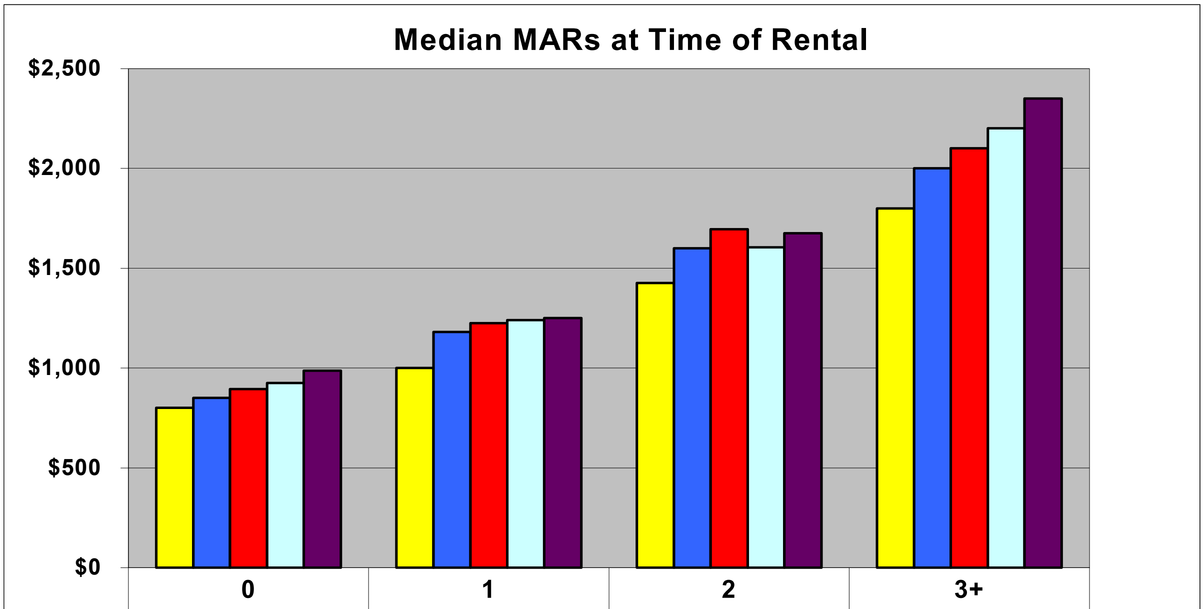
The chart details rents based on the number of bedrooms in the units. The second column is the median rent in effect as of December 1998 (before any market rate increases were implemented) with the 1999 – 2003 general adjustments added. Adding the general adjustments allows a comparison of what the medians of these 10,929 units would be as of December 2003 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.

Median MARs at Time of Rental

The table on the next page shows the medians by year for **all** units in which a market rate rent was established in a given year. If a unit was rented in 1999 and re-rented again in 2003, the first market rent is reflected in the figures for 1999 and the later market rent is reflected in the figures for 2003. These rents do not include general adjustments that would have been allowed for units rented in 1999, 2000, 2001 and before September 2002.

[5] 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.

[6] December 1998 median MARs with 1999-2003 general adjustments added.



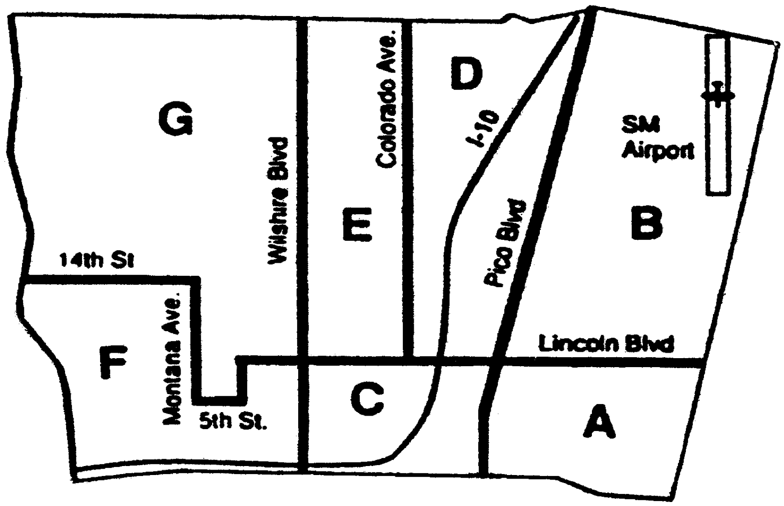
	0	1	2	3+
1999	$800	$1,000	$1,425	$1,800
2000	$850	$1,180	$1,600	$2,000
2001	$895	$1,225	$1,695	$2,100
2002	$925	$1,239	$1,604	$2,200
2003	$987	$1,250	$1,675	$2,350

Number of Bedrooms

In looking at the year-to-year change in median rents, the largest variation occurred between 1999 and 2000. Although the general trend of rents is upward (note the rents shown above do not include general adjustments), the upward movement in one-bedroom rents in the last three years has been relatively small, $25 in three years. The rents for two-bedroom units, the second largest category, decreased from 2001 to 2002 by $90 per month. The median in 2003 regained some of the 2002 decline but is still lower than the two-bedroom median in 2001. The year-to-year variations are minimized if a multi-year period is used for establishing comparable rents.

Median MARs by City Area

To track changes in the housing stock in different areas of the city, in the early 1990s 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.



The table below shows that the distribution of units rented at market rate during five years of vacancy decontrol closely parallels the distribution of rental units throughout the city overall. For example, Area G contains the largest percentage of controlled rental units (22%) and 22% of the market rate rentals have occurred in this area.

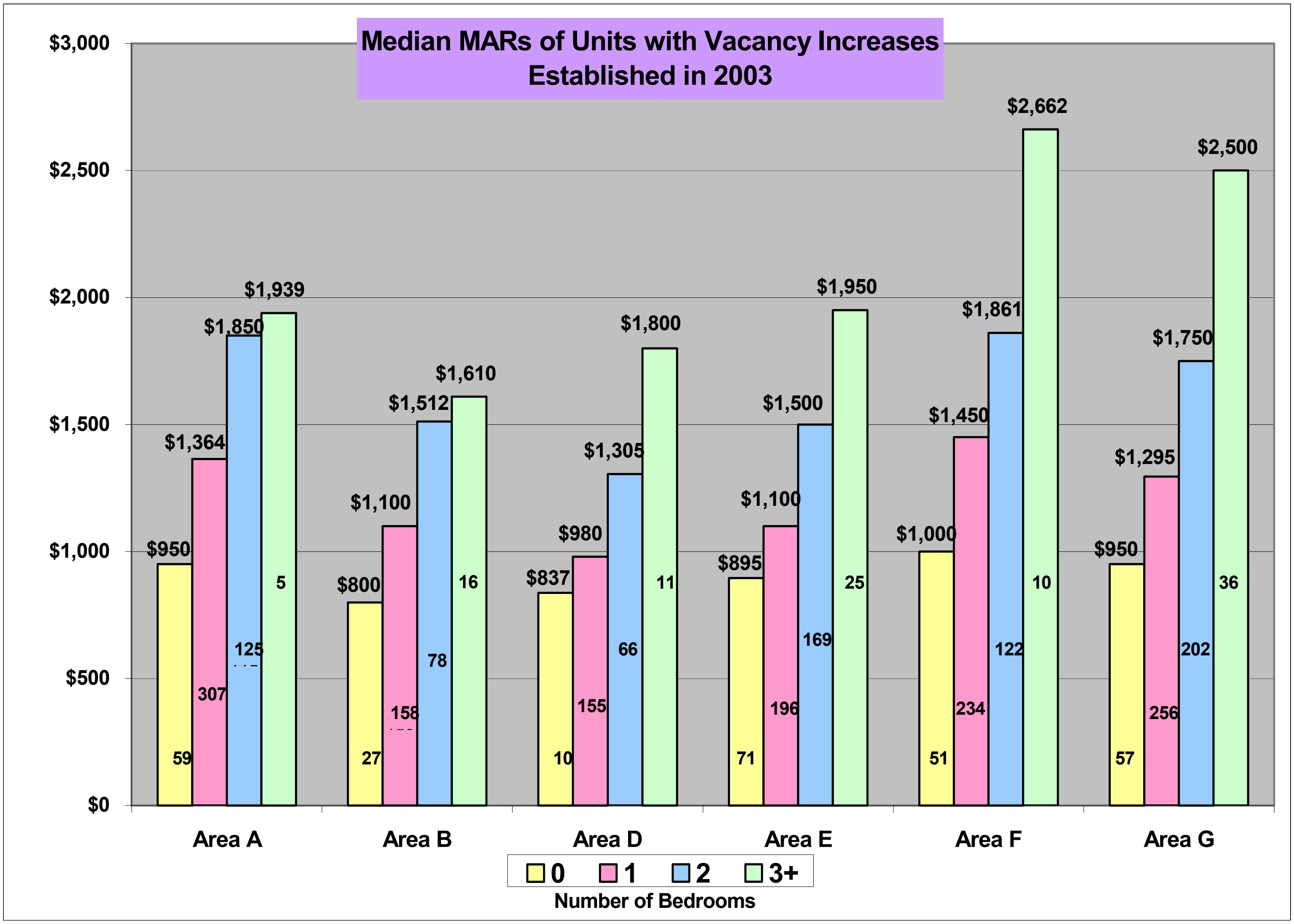
City Area	A	B	C	D	E	F	G
Percentage of Units	17	12	4	10	19	16	22
Percentage of Market Rentals	18	12	5	8	19	16	22

The graphs on the following two pages show the median market rents for 2003 and 2001 – 2003. In both graphs, the dollar amounts at the top of the bars represent the median market rent for each bedroom size in each city area. The numbers within the bars are the number of units in each category rented at market rate during the time period.

In both graphs, 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. Due to a substantial number of units removed from rent control since the area lines were drawn, Area C has a significantly smaller number of controlled rental units than every other area. With just over 900 controlled units in Area C, these two buildings account for more than 40% of all controlled units in the 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.

Median MARs by City Area—2003

This graph details for the various areas of the city by number of bedrooms the current median rents for the 2,702 units in which a vacancy increase was implemented in 2003.

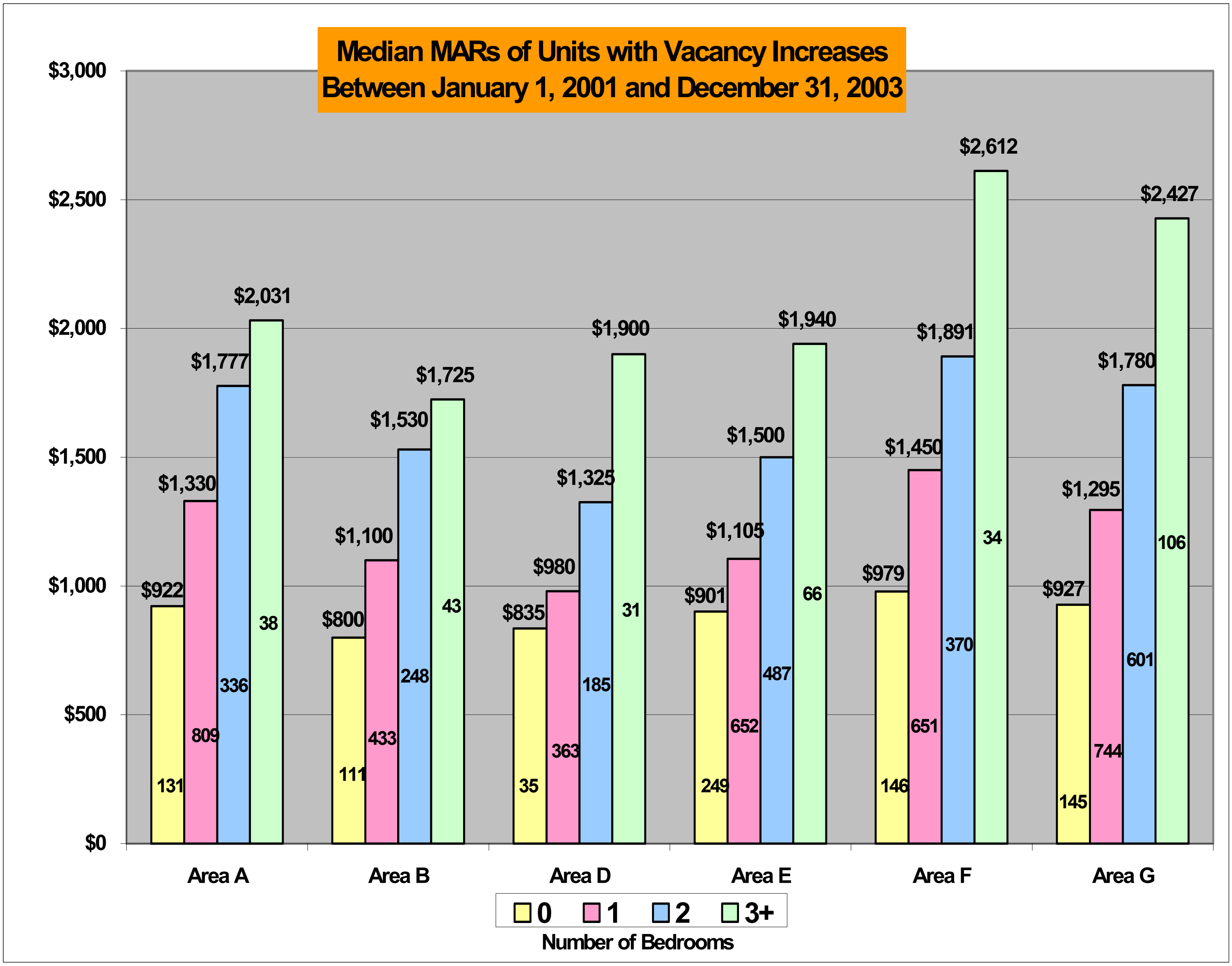


The numbers within the bars are the number of units in each category rented at market rate during the time period. As the numbers inside the pink bars show, in each city area more one-bedroom units were rented at market rate this year than any other size unit. This is consistent with the table on page 6 which shows that the largest percentage of units overall (48%) are one-bedroom units. Conversely, the numbers in the green bars show that very few 3-bedroom units were rented in 2003. Area A had just 5 units of this size rented and Area G had the largest number, but this was just 36 units.

Where the number of units impacted is quite small, the applicability of the median to other units in the area is less accurate. Therefore, looking at just one year of rentals does not always give a true picture of general market conditions. A three-year graph follows.

Median MARs by City Area—2001-2003

This graph shows median MARs by area and number of bedrooms for 7,386 units with vacancy increases established in the most recent three-year period, January 1, 2001 through December 31, 2003. This three-year view of vacancy increases provides a more complete overview of current market rate rentals because it includes significantly more units overall (7,386) as well as many more units of each size than the look at 2003 alone.



The numbers within the bars are the number of units in each category rented at market rate during the time period. The median rents on these units were used to determine the median for each unit size within each area.

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 2003, the HUD median income for a "Four-Person Household" in Los Angeles County is $55,100 (unchanged from 2002). 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	$44,080	$55,100	$66,120

Translating Affordability into Income

Using HUD affordability calculations that include adjustments for number of bedrooms[7], 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 – 12/31/03 (10,929 units)

No. of Bedrooms	Adjusted 1998[8] Median MARs	Income needed to Afford MAR	Post-Increase Median MARs	Income Needed to Afford MAR	Income Difference
0	$626	$35,771	$924	$52,800	$17,029
1	708	35,400	1,231	61,550	26,150
2	909	38,274	1,641	69,095	30,821
3 or more	1,157	42,654	2,109	77,751	35,097

As the chart above shows, depending on size of a unit, the household income needed to "afford" the median market rent is $17,000 - $35,000 higher than the income needed to afford the median rent of that same size unit if it had not received a market rate increase.

[7] 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

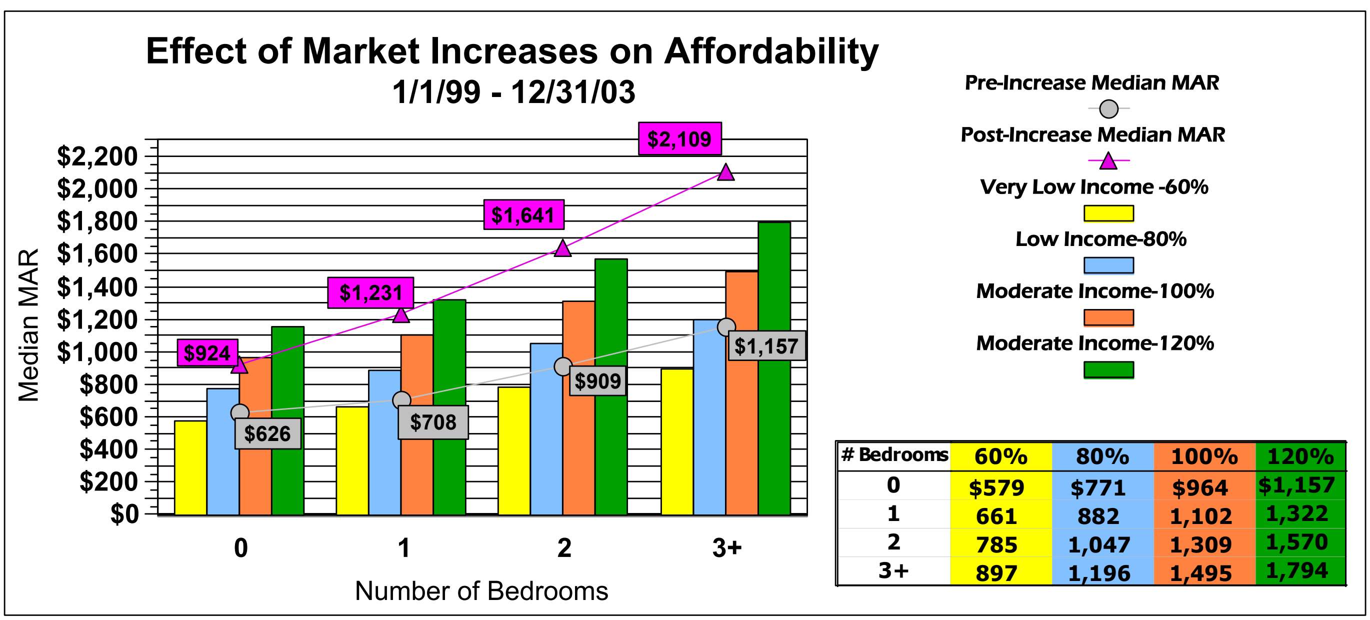
[8] December 1998 median MARs with 1999-2003 general adjustments added.

Loss of Affordability – 1/1/99 - 12/31/03

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 10,929 units that have received market increases, their pre-increase median MARs at all bedroom sizes (with 1999-2003 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 $614 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 $315 above the amount affordable at 120% of median income.)

This information is shown in graph form below. The vertical 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 gray line shows the pre-increase median MARs (with 1999-2003 GAs) and the pink 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

Loss of Affordable Units by Income Level

The 10,929 units impacted by market rate increases had a mixture of rents affordable to families at all income levels before the increases were implemented. The table below and graph on the next page detail the dramatic shift in affordability levels for the units that have received market rate rent increases.

Distribution of 10,929 Units Before and After Increases

Affordability Category	Number of Units Before Increases	Number of Units After Increases	Difference
Very Low – 50%	2,026	66	-1,960
Very Low – 60%	2,708	121	-2,587
Low – 80%	3,944	756	-3,188
Moderate – 100%	1,407	2,316	+909
Moderate – 120%	447	2,740	+2,293
120% +	397	4,930	+4,533

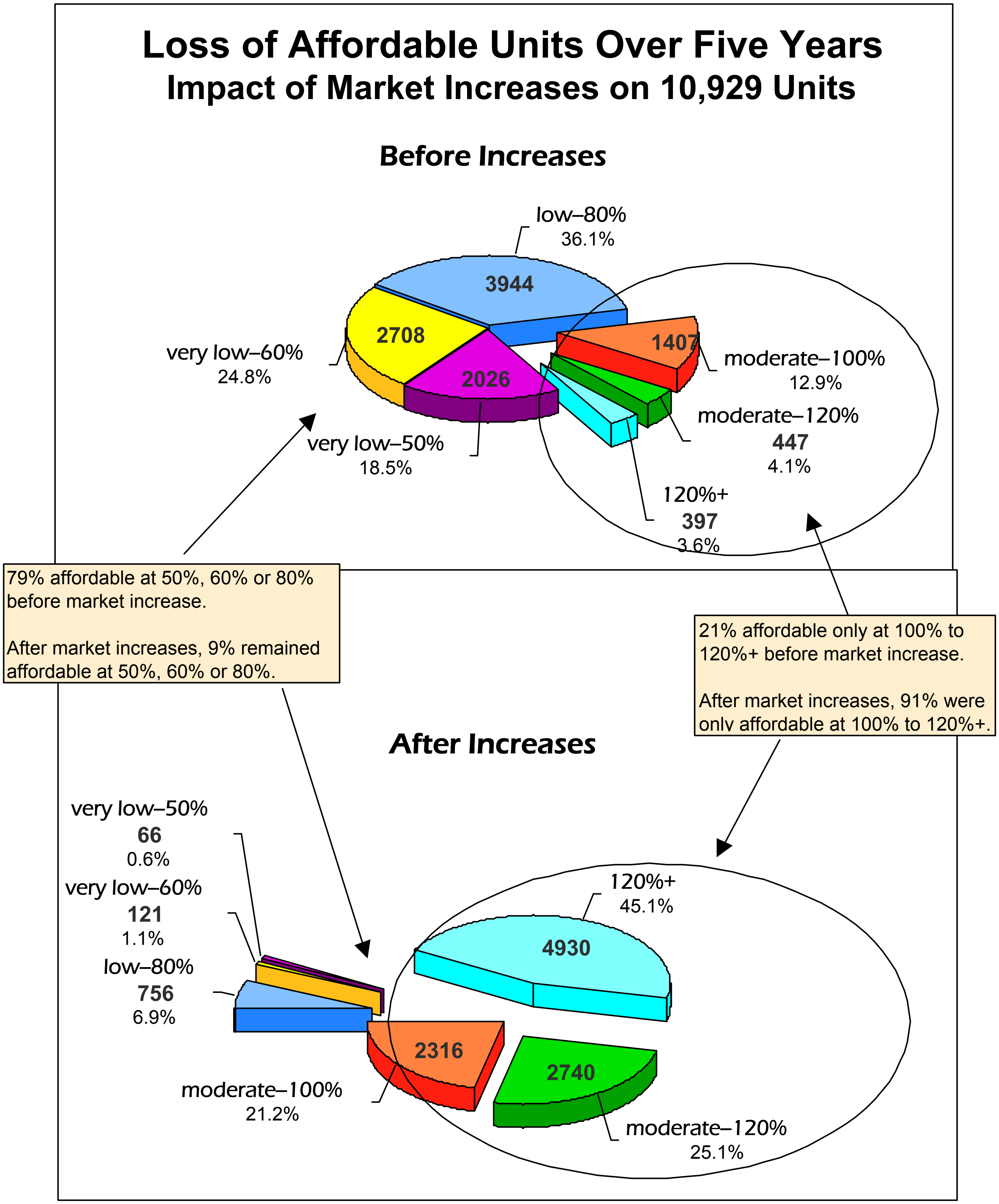
In summary:

- Before the increases, 43% of the units had median rent levels affordable to **very-low income** households. After the increases, less than 2% of the units remained affordable to these households. This represents a loss of affordability of 4,547 units.

- Before the increases, 79% of the units had median rent levels affordable to **low-income** households. After the increases, only 9% of the units remained affordable at this income level.

- Forty-five percent (45%) of market rents are affordable only to people making more than 120% of the median income for a family of four ($66,120).

The pie chart on the next page graphically details the shifts in affordability of the units rented at market rate.



Loss of Affordable Units Over Five Years
Impact of Market Increases on 10,929 Units
Before Increases
low–80%
36.1%
3944
very low–60%
24.8%
2708
2026
very low–50%
18.5%
1407
moderate–100%
12.9%
moderate–120%
447
4.1%
120%+
397
3.6%
79% affordable at 50%, 60% or 80% before market increase.
After market increases, 9% remained affordable at 50%, 60% or 80%.
21% affordable only at 100% to 120%+ before market increase.
After market increases, 91% were only affordable at 100% to 120%+.
After Increases
very low–50%
66
0.6%
very low–60%
121
1.1%
low–80%
756
6.9%
120%+
45.1%
4930
2316
2740
moderate–100%
21.2%
moderate–120%
25.1%

CONCLUSION

Five years into vacancy decontrol, 40% of the rental housing stock has been rented at market rate and 60% remains rented to long-term tenants. The rate at which new units receive market rate increases has slowed each year since 1999, the first year of vacancy decontrol. In that year, more than 3,000 units were first rented at market rate. In 2003, fewer than half that number (1,443 units) received market rate increases for the first time.

Once a unit is rented at market rate and loses its affordability, it is much more likely to turnover again. Forty-two percent (42%) of the market rate rentals have turned over at least once since the first market rental.

As a result of vacancy decontrol, a dramatic shift has occurred in the affordability of the 10,929 units that received vacancy increases. Before the increases, 79% of the units had rent levels affordable to low-income households. After the increases, just 9% remain affordable at the low-income level. Additionally, before the increases, just 21% of the units were affordable only to households with moderate-income levels or higher. Today, 91% of the units with market-rate increases are **only** affordable to these households.

Despite the significant loss of affordability in those units that have had a vacancy increase, a substantial number of units (approximately 16,500) have not received vacancy increases and continue to provide affordable housing.