



**MEMORANDUM**

Rent Stabilization Program, Community Development Department

**DATE:** January 25, 2021

**TO:** Rental Housing Committee

**FROM:** Patricia Black, Analyst II  
Karen M. Tiedemann, Special Counsel  
Anky van Deursen, Rent Stabilization Program Manager

**SUBJECT:** Capital Improvement Petition Process Study Session

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**RECOMMENDATION**

Receive background information and consider potential policy options related to a Capital Improvement petition process for temporary upward adjustment of rent.

**BACKGROUND**

**RHC Authority**

In November 2016, voters approved the Community Stabilization and Fair Rent Act (CSFRA), which amended the City Charter. The CSFRA regulates the rents of rental properties with certain exemptions, such as single-family homes and duplexes. The CSFRA is a tenant-protection law that has three primary goals:

1. Stabilize rents;
2. Provide eviction protections; and
3. Ensure a fair and reasonable rate of return on investment.

Section 1700 of the CSFRA stipulates that housing providers are entitled to “a fair and reasonable return on their investment.” The CSFRA provides three methods to ensure a fair return is achieved:

1. General Annual General Adjustment (AGA) of rent of 100 percent Consumer Price Index – Urban (CPI-U) (Bay Area Region);

2. Vacancy decontrol; and
3. Individual petitions for upward adjustment of rent (using a fair return standard).

Two of the methods, vacancy decontrol and petitions for upward adjustment of rent, are applicable to Capital Improvement expenditures.

Sections 1708, 1710, and 1711 of the CSFRA charge the Rental Housing Committee (RHC) with promulgating regulations to implement the petition process and provide landlords with a mechanism for achieving a fair rate of return that addresses individualized circumstances. Section 1708 of the CSFRA empowers the RHC to set rents at fair and equitable levels to achieve the purposes of the CSFRA and establish rules and regulations for the administration and enforcement of the CSFRA. The RHC is empowered to determine how a fair and reasonable rate of return is to be achieved, and the CSFRA does not define what is considered a fair and reasonable rate of return.

Section 1710 of the CSFRA provides for petitions for individual rent adjustments, including upward adjustments. Upward adjustments are to be granted only when a landlord demonstrates that the adjustments are necessary to maintain a fair rate of return. Sections 1710(a)(2) and 1710(a)(3) set out factors to be included in considering upward adjustment petitions, including the costs of Capital Improvements that are necessary to bring the property into compliance or maintain compliance with applicable local codes.

### **Previous Committee Discussion**

The RHC in 2017 adopted regulations, located in Chapter 6 of the CSFRA Regulations, defining a fair rate of return as the maintenance of the landlord's net operating income for the base year as adjusted by the Consumer Price Index (CPI).

The RHC has discussed options for adding an additional standard for upward adjustments to allow landlords to recover the cost of Capital Improvements in order to incentivize landlords to continue to maintain their properties and to comply with changing codes. The RHC has discussed a Capital Improvement petition process that would allow landlords to recover costs of certain Capital Improvements without the necessity of providing detailed property records, thereby allowing for an expedited hearing process. The RHC deferred further discussion on a Capital Improvement petition process while Measure D was pending since Measure D would have mandated an expedited Capital Improvement petition process.

On August 24, 2020, the RHC considered draft regulations for a Specified Capital Improvement petition process. As a result of that meeting, the RHC requested the topic

be brought back to the RHC at a later meeting date as a Study Session that included input from the community to further inform the discussion. The RHC also requested information for consideration on a draft joint petition process between property owner(s) and tenant(s).

### **COUNCIL AND COMMUNITY INPUT**

Over the course of the past four years, staff engaged the community multiple times regarding a draft Capital Improvement petition process. The community engagement highlighted general support for a petition process among both tenant and landlord stakeholders. However, the two groups differed in their support for policy options related to sharing of costs and amortization periods.

### **CSFRA Ad Hoc Subcommittee Meetings/Measure D**

On June 25, 2019, the City Council approved formation of the CSFRA Ad Hoc Subcommittee (Subcommittee) to discuss potential CSFRA amendments for a City-initiated ballot amendment. The Subcommittee reviewed a number of areas they were interested in amending and received input from the RHC, stakeholders, and the public. In late 2019, Council approved Measure D, placing it on the ballot for March 2020. One of the primary proposed amendments in Measure D was a Specified Capital Improvement petition process. The draft language of the proposed Charter Amendment was as follows:

- “(e) Increases for Specified Capital Improvements. A Landlord pursuing an eligible Capital Improvement may seek reimbursement for all or a portion of the approved costs of that eligible Capital Improvement by way of a temporary Rent increase in accordance with this Section 1710(e).*
- *“Capital Improvement” means a substantial addition or modification of a physical feature of a Covered Rental Unit, or of a building or Property containing a Covered Rental Unit that primarily benefits one or more Tenants and qualifies as one of the following for purposes of this Section 1710(e).*
    - *(A) Necessary to bring the Property into compliance or maintain compliance with applicable state and local codes affecting health and safety, but excluding the costs of any additions or modifications that could have been avoided by the exercise of reasonable diligence in maintaining and making timely repairs to the Covered Rental Unit and/or Property; or*

- (B) *Significantly improves the environmental sustainability of the Covered Rental Unit or Property and does not result in a net increase in utility costs to the Tenant(s); or*
- (C) *Significantly extends the useful life of the Covered Rental Unit or Property, but excluding the costs of any additions or modifications that could have been avoided by the exercise of reasonable diligence in maintaining and making timely repairs to the Covered Rental Unit and/or Property.”*

The Charter Amendments proposed in Measure D were not approved by the voters. As a result, staff reintroduced draft regulations related to a Specified Capital Improvement petition process as previously requested by the RHC.

### **Community Meetings for CSFRA-Covered Units**

On December 9, 2020, Rent Stabilization Program staff held two virtual community meetings in order to receive community input and feedback regarding the potential petition process as directed by the RHC in the August 2020 meeting. Staff held one community meeting to receive feedback from CSFRA-covered property owners and one bilingual (in English and Spanish) community meeting to receive feedback from CSFRA-covered tenants. Outreach efforts to inform the community of the meetings were performed as follows:

- One postcard in English and Spanish was mailed to all CSFRA-covered units and landlords;
- Two e-mails were sent to CSFRA-interest lists, including tenant and landlord groups;
- City calendars were updated with the information and registration link; and
- Rent Stabilization Program website homepage slideshow was updated to promote the meetings with registration link and information about the meetings.

Eleven (11) community members attended the property owner-focused virtual meeting, and eight community members attended the tenant-focused virtual meeting.

## **COST-RECOVERY MECHANISMS**

Section 1700 of the CSFRA stipulates that housing providers are entitled to “a fair and reasonable return on their investment.” The CSFRA provides three methods to ensure a fair return is achieved:

1. General AGA of rent of 100 percent CPI-U (Bay Area Region);
2. Vacancy decontrol; and
3. Individual petitions for upward adjustment of rent (using a fair return standard).

Two of the methods, vacancy decontrol and petitions for upward adjustment of rent, are applicable to Capital Improvement expenditures.

### **Vacancy Decontrol**

The Costa-Hawkins Rental Housing Act (Costa-Hawkins) (Civil Code 1954.50 to 1954.535) is a California State law enacted in 1995 that restricts certain aspects of jurisdictional independence over rent control. One aspect of Costa-Hawkins is the requirement that rent control laws allow for vacancy decontrol, which grants housing providers the opportunity to set initial rent for new tenancies at market rate, as is the case under the CSFRA. In general, 20 percent of rental units in Mountain View experience tenant turnover annually. In five years, turnover rates could approach 100 percent. There are exceptions to the turnover rate, with some units and buildings having long-term tenants and minimal, if any, turnover during a five-year time frame.

### **CSFRA Petitions for Upward Adjustment of Rent**

If a landlord does not believe the permitted annual general rent adjustment provides a fair rate of return, they may petition for an upward adjustment of rent. The CSFRA sets forth the factors a hearing officer may consider when deciding whether to grant the petition.

### **Fair Return Standard: Maintenance of Net Operating Income (MNOI) Petition**

Under current CSFRA Regulations, property owners are able to request rent increases above the allowed annual general adjustment through the petition process. The process utilizes a “maintenance of net operating income (MNOI) fair return standard” to ensure property owners are able to achieve a fair and reasonable return on investment as required under the law. This process determines whether current rent levels are able to

maintain the net operating income of the property over time. It compares the net income received from a property in the base year (2015) (adjusted for inflation) with the net income received in the petition year.

The MNOI calculation is used in petitions for upward adjustment of rent to determine whether the AGA of rent allowed under the CSFRA maintains a property's net operating income from year to year, adjusted by an inflation rate percentage. The equation utilizes the CPI to adjust a petition's 2015 base year net operating income by an inflation rate percentage. The petition year's net operating income is then compared with the net operating income of the base year. If the petition year's new operating income is less than the base year net operating income, the property would be eligible for an increase greater than the AGA in order to maintain net operating income and receive a fair rate of return.

#### *Fair Return Standard – MNOI Petition Process*

In order to request an upward adjustment of rent under the current process, property owners must complete a petition form and provide documentation of income and expenses for two time periods: the base year (2015) and the petition year. The current fair return petition process compares income and expenses in a variety of categories and considers Capital Improvements as one factor in determining net operating income. Once complete, property owners then serve the petition on affected tenants and formally file the petition with the City.

Rent Stabilization Program staff then reviews the petition to make sure it is complete and, if information or documentation appears to be missing, staff contacts the petitioner to provide a chance to supplement or revise the petition. Staff then accepts the petition and notifies all parties involved.

#### *Settlement Meeting*

The Mountain View Rental Housing Helpline contacts all parties to discuss the hearing process, including scheduling a settlement meeting, if that option was selected. If all parties agree to participate, the Helpline schedules the meeting. At the meeting, parties have the opportunity to privately discuss issues brought up in the petition with a trained facilitator. If a mutual understanding is reached, the facilitator drafts a binding agreement, and the petition is resolved without going to a hearing. Any settlement agreement is a private record and not subject to public disclosure.

### *Hearing Process*

If a settlement meeting is not requested, or no agreement is reached, the Helpline coordinates a hearing with a hearing officer and the parties. The hearing officer holds a telephone conference to review what happens at the hearing, request additional documentation, and answer any questions. At the hearing, all parties have a chance to share information with the hearing officer, respond to each other's statements and provide clarifying answers as requested. After the hearing is over and the record is closed, the hearing officer issues a written decision determining the outcome of the petition.

### *Appeal Process*

A hearing officer's decision may be appealed to the RHC. The appeal must be filed within 10 days of the mailing date of the decision. If the hearing officer's decision is not appealed, it automatically becomes final, and the petition is closed.

### **Proposed Additional Fair Return Standard: Specified Capital Improvement Petition**

The Specified Capital Improvement petition process would be included in Chapter 6 of the CSFRA Regulations, which addresses upward adjustment petitions. The main features of the proposed petition and process are summarized below. The amendments to Chapter 6 would determine that a fair rate of return can be achieved either by the MNOI or by the recovery of costs of certain Capital Improvements, potentially defined in Chapter 6 as Specified Capital Improvements. The Specified Capital Improvement temporary upward adjustment would not be considered part of rent as defined in the CSFRA and would not be included when calculating future annual general adjustments.

Amendments to Chapter 6 could introduce an expedited petition process for certain Capital Improvements, defined as Specified Capital Improvements. Specified Capital Improvements are generally major Capital Improvements that significantly extend the useful life of the property. Additionally, Capital Improvements that adhere to the above qualifications and also improve the environmental sustainability of the property while reducing costs to tenants may be considered Specified Capital Improvements eligible for the expedited petition process. Specified Capital Improvements must also meet the definition of Capital Improvement, which is already part of Chapter 6. The CSFRA limits the capital improvements that can be considered in upward adjustment petitions to improvements necessary to bring the property into compliance with applicable codes and cannot include costs that could have been avoided by the exercise of reasonable diligence in maintaining the property.

Specified Capital Improvement petitions can support the intentions of the CSFRA to stabilize the community by:

1. Encouraging landlords to proactively maintain property;
2. Promoting safe and healthy housing for tenants;
3. Reducing potential large scale displacement; and
4. Preserving affordable housing stock in the City.

*Fair Return Standard – Specified Capital Improvement Petition Process*

Landlords petitioning for a Specified Capital Improvement temporary upward adjustment would be required to complete a petition that includes documentation on the type and cost of Specified Capital Improvement installed. Landlords would also be required to provide limited information regarding the property, primarily the current rent roll, and the date that each tenant initially occupied the rental unit. This information is required because the CSFRA prohibits the consideration of Capital Improvements that arose prior to the current tenancy (Section 1710(a)(3)(D)). Landlords would be able to petition for approval of Specified Capital Improvements that have not been installed yet, but any upward adjustment awarded would not be effective until the Specified Capital Improvements are installed and proof of installation and final cost is provided to the Hearing Officer. Attachment 1 provides an example of a Capital Improvement petition form from the City of San Jose.

*Expedited Hearing Process*

Once a Specified Capital Improvement petition is deemed complete and, therefore, accepted by the RHC, affected tenants will be provided notice and the opportunity to request a hearing on the petition. Tenants requesting consideration of a hardship must do so when requesting a hearing. If no tenant requests a hearing, a hearing officer will decide on the petition without a hearing. If a tenant requests a hearing, the hearing is to be held within 30 days of the request for a hearing. At the conclusion of the hearing, the hearing officer will issue a decision, which is appealable by either the landlord or the tenant. This process is similar to the current process for Tenant Petition C.



### *Appeal Process*

A hearing officer's decision may be appealed to the RHC. The appeal must be filed within 10 days of the mailing date of the decision. If the hearing officer's decision is not appealed, it automatically becomes final, and the petition is closed.

### **Proposed Components for Specified Capital Improvements**

#### *Qualifications*

Currently, Chapter 6, Section F, of the CSFRA Regulations sets forth the following qualifications (requirements) and exclusions for Capital Improvement for MNOI petition requirements:

1. **"Capital Improvement"** means additions to or modifications of a physical feature of a Covered Rental Unit or of a building or property containing a Covered Rental Unit. To qualify as a Capital Improvement, the addition or modification must:
  - a. Be necessary for bringing the property or Covered Rental Unit into compliance or to maintain compliance with applicable building or housing codes, including, without limitation, additions or modifications made to prevent the occurrence of conditions listed in Mountain View City Code Section 25.58, the International Property Maintenance Code as incorporated by reference into the Mountain View City Code, and/or California Green Building Standards as codified in Chapter 4 (Residential Mandatory Measures) of Part 11 of Title 24 of the California Code of Regulations, as each may be amended or revised; and
  - b. Primarily benefit the Tenant rather than the Landlord; and
  - c. Be permanently fixed in place or relatively immobile (e.g., roofs, foundations, and window replacements may qualify in whole or in part as Capital Improvements).
2. **Exclusions.** The following are not eligible as Capital Improvements:
  - a. Costs of additions or modifications of a physical feature, or portions of additions or modifications, that could have been avoided by the Landlord's exercise of reasonable diligence in maintaining and making timely repairs after the Landlord knew or should reasonably have known of the problem that caused the damage leading to the addition or modification; or

- b. Use or installation of a Landlord's personal appliances, furniture, etc., or those items inherited or borrowed; or
- c. Ordinary or routine repair, replacement, or maintenance to a Covered Rental Unit or property containing a Covered Rental Unit; or
- d. Overimprovements (for example, replacing a standard bathtub with a Jacuzzi bathtub), unless the Tenant approved the improvement in writing, the improvement brought the Covered Rental Unit up to current building or housing codes, the improvement was necessary to meet California Green Building Standards, or the improvement did not cost more than a substantially equivalent replacement.

In addition to these qualifications and requirements already contained within Chapter 6, staff proposes an additional qualification be added to the definition of Capital Improvements that the improvement have a useful life greater than one year and be required to be amortized over the useful life of the improvement. Capital Improvements that adhere to the above qualifications and also improve the environmental sustainability of the property while reducing costs to tenants also may be considered by the hearing officer.

#### *Categories*

As in other jurisdictions, Specified Capital Improvements would be limited to the following categories:

- New roof covering all or substantially all of a building or a structurally independent portion of a building; and/or
- Significant upgrade of the foundation of all or substantially all of a building or a structurally independent portion of a building, including seismic retrofits; and/or
- New or substantially new plumbing, electrical, or heating, ventilation, and air conditioning (HVAC) system for all or substantially all of a building; and/or
- Exterior painting or replacement of siding on all or substantially all of a building; and/or
- Repairs reasonably related to correcting and/or preventing the spread of defects which are noted as findings in a Wood Destroying Pest and Organisms Inspection Report; and/or

- Installation of water conservation devices intended to reduce the use of water or energy-efficient devices, such as solar roof systems; and/or
- Improvements or upgrades to the Rental Unit or the building/complex that meet or exceed disability/accessibility standards as required by law.

### *Authorized Expenses*

Staff proposes the creation of an additional Authorized Expenses and Amortization Schedule. The list restricts improvements allowed in Specified Capital Improvement petitions by the categories and qualifications outlined above.

Staff performed an extensive review of peer jurisdictions and incorporated community feedback from the December 2020 community meetings when refining the proposed authorized expense list. The list provides specific examples and amortization periods for expenses and can act as a comprehensive guide to property owners when considering how to allocate costs associated with a large improvement project. The proposed authorized expenses for Specified Capital Improvement petitions are found in Attachment 2: Draft Authorized Expenses and Amortization Schedules—Schedule B.

### *Share of Costs*

During the August 24, 2020 RHC meeting, staff proposed an allocation of the full cost of the Specified Capital Improvement be applied to all benefitted tenants. It was also recommended that the total amount of the temporary adjustment be limited to 10 percent of rent for any unit subjected to the upward adjustment. Additionally, staff proposed that if a landlord is unable to recover the full cost of the improvement because of the 10 percent limitation, the landlord could request an extended amortization period.

During the December 2020 community meeting, tenants and community members shared their concern with the proposed cost-share allocation. They expressed that property owners experience an increase in property value after Capital Improvements are performed from which tenants do not benefit and, therefore, feel it is inappropriate for tenants to bear the full cost burden. Property owners expressed support for the initial proposal.

The share of costs allowed under Capital Improvement petitions in other rent-controlled jurisdictions is typically split between tenants and landlords because both parties benefit from the improvements. Restrictions vary by jurisdiction and often are also limited by

amortization schedules, percent and dollar amount caps allowed under the rent stabilization laws, sunset provisions, and/or income of tenants.

After receiving community feedback and reviewing peer jurisdictions, staff proposes amending this recommendation for the RHC to consider the following cost-sharing options:

#### Amount of Cost Share

Staff proposes the RHC consider the following cost-sharing options:

1. 50 percent (similar to Hayward);
2. 70 percent (similar to Oakland); and
3. Split depending on size of complex: 100 percent cost-recovery for small landlords with five or fewer units; and 50 percent cost-recovery for larger properties with five or more units.

Staff proposes the RHC consider the following total amounts for associated increases:

1. 10 percent of the rent (inclusive of the AGA and banked increases) capped at a certain dollar amount per year (similar to San Francisco); and
2. 3 percent to 5 percent of rent (not inclusive of the AGA) and not capped at a certain amount per year (similar to Hayward and San Jose).

Based on community feedback and to ensure community stability, staff also recommends that all increases associated with capital improvements be limited to a total of 10 percent of rent at any time per unit.

#### *Amortization and Sunset Periods*

Staff proposes Capital Improvement costs be amortized, or spread out, over a specified time frame and that any Specified Capital Improvement temporary upward adjustment is temporary and will expire either at the end of the amortization period or when the tenant vacates the unit. Vacancy decontrol allows property owners to raise rents upon vacancy to recover the cost of any Capital Improvements. Amortization schedules specify the length of time for each type of allowed cost. Once the amortization period is complete, the increases sunset and can no longer be applied to monthly rent charges. The

proposed amortization schedule can be seen in Attachment 2: Draft Authorized Expenses and Amortization Schedules – Schedule B.

### **JOINT PETITION BETWEEN PROPERTY OWNER(S) AND TENANT(S)**

The RHC also requested information for consideration of a draft joint petition between property owner(s) and tenant(s). Both tenants and landlords express that they often are restricted in being able to address certain situations that would otherwise be easily solved in unregulated markets. CSFRA Regulations could introduce an additional petition process allowing tenants and landlords to file a joint petition for an increase of rent or allow for a one-time payment from tenant to landlord in order to cover, or partially cover, increased costs associated with the following categories:

1. New or additional housing services (housing services not included in lease):
  - a. Improvements or modifications as requested by the tenant, such as new flooring, paint, appliances, etc.; and
  - b. Other housing services as requested by tenant;
2. Additional Occupant defined as neither an eligible family member (under Section D of the CSFRA Regulations, Chapter 9) nor as a roommate who will replace a departing or former roommate in a Covered Rental Unit (as defined under Section E of the CSFRA Regulations, Chapter 9);
3. New or additional pet(s) not included in lease; or
4. Additional parking spaces.

The mediation services offered through the Mountain View Mediation Program provide a vehicle for property owners and tenants to agree to repairs and improvements that may increase rents or result in a pass-through payment by the tenant beyond the CSFRA. While a Capital Improvement and associated cost sharing between property owners and tenants may be voluntarily agreed to, a tenant may later dispute the charge as an unlawful increase in rent on the basis that the CSFRA prohibits waiver of the tenant's rights. The joint petition process would prevent a subsequent waiver argument.

#### *Joint Petition Process*

Through this administrative hearing process, tenants could file a petition with the City, signed and agreed to by their landlord, for an upward adjustment of rent or one-time

payment, in order to receive additional services beyond the scope of their rental agreement. Tenants would be required to complete an abbreviated petition that includes a copy of the tenant's lease as well as the landlord's signature of approval for additional services. Additional documentation may also be required, depending on the category of increase requested. Attachment 3 provides an example of a joint petition form from the City of San Jose for reference.

#### *Administrative Hearing Process*

Once a joint petition is deemed complete and, therefore, accepted by the RHC, both parties will be provided notice and a hearing officer would be assigned to the petition. The hearing officer would then review the petition and associated documentation. Once the review is complete, the hearing officer will issue a decision outlining the allowed increase or one-time payment. The decision would have the same effect as other administrative decisions of the RHC and would establish the rent increase or pass through payment. The decision would only be appealable if the hearing officer's decision deviated from the request in the petition.

#### **Proposed Components for Joint Petitions by Category**

Staff proposes the following policies for each category.

##### *New or Additional Housing Services (Housing Services Not Included in Lease)*

For improvements, modifications, or other housing services as requested by the tenant, staff recommends tenants and landlords have the ability to select their preference of two choices, that are both capped as described below:

- Choice 1: Amortized temporary monthly rent increase with an agreed-upon cost-share between tenant and landlord.
- Choice 2: One-time payment not to exceed 5 percent of rent.

Additional Occupant defined as neither an eligible family member (under Section D of the CSFRA Regulations, Chapter 9) nor as a roommate who will replace a departing or former roommate in a Covered Rental Unit (as defined under Section E of the CSFRA Regulations, Chapter 9).

This type of request would allow for tenants and landlords to agree to an Additional Occupant for an agreed increase in monthly rent. The Additional Occupant would be

then covered by the Regulations as outlined in Chapter 9. For petitions requesting an additional occupant, staff proposes a cap in monthly rent increase of 5 percent.

*New or Additional Pet(s) not included in Lease*

For petitions requesting a new or additional pet, staff recommends restricting the allowed monthly increase to either a cap of \$50 per month or the agreed-upon amount as defined in the lease for other pets, whichever is lower.

*Additional Parking Spaces*

For petitions requesting an additional parking space, staff recommends restricting the allowed monthly increase to either a cap of \$50 per month or the agreed-upon amount as defined in the lease for other parking spaces, whichever is lower.

**JURISDICTIONAL COMPARISON**

**Fair Return Standard – MNOI Petitions**

As in Mountain View, all jurisdictions have a fair-return standard/MNOI petition process to ensure housing providers are able to maintain their net operating income on a year-to-year basis adjusted by a percentage increase of a specified CPI. In this type of petition, Capital Improvements are documented as one of a variety of factors to be included when calculating a fair return. For the most part, although available, MNOI petitions are generally no longer filed in the researched cities due to the age of the rent stabilization ordinances. Essentially, the further away from the implementation date of the rent stabilization ordinance, the less necessary fair return petitions are for maintaining income. This is due to vacancy decontrol. Santa Monica and West Hollywood strictly utilize the fair return standard.

**Fair Return Standard – Capital Improvement Cost Recovery (Expedited Petitions)**

Alameda currently utilizes a Capital Improvement plan application that must be filed with the City of Alameda prior to the repairs being conducted. If approved, the plan allows the Program Administrator to determine the maximum allowed rent increase per unit. If the requested increase is above 5 percent, the applicant may also consider filing an increase petition. Repairs must meet a minimum cost threshold to qualify for the plan as follows:

1 months' rent x number of units improved x 8 (number determined by Council)

Should this threshold be met, an additional calculation is used to determine the allowed maximum increase per unit:

$$[\text{Total cost of repairs + interest}] / \text{amortization period} / \text{number of units improved}$$

Staff notes that the City of Alameda adopted sweeping changes to its rent stabilization ordinance that have yet to be implemented and may impact the current Capital Improvement plan application process.

Berkeley allows for a modified process that takes into account Capital Improvement costs but not all operating expenses. This method bypasses MNOI calculations to determine a fair return. Capital Improvements allowed under this petition are valued at a specific calculation rate. This calculation rate is then used to determine the potential increase per unit via the following equation:

$$[(\text{Out of pocket cost} + \text{self-labor cost}) \times \text{calculation rate}] / \text{number of units}$$

Los Angeles, Oakland, San Jose, and San Francisco have regulations that provide for a truncated petition process to recover costs associated with capital improvements. These expedited petitions grant housing providers an opportunity to request rent adjustments based solely on costs incurred due to certain capital improvements instead of reviewing all income and expenses as required under a fair return standard. The petitions require that documentation related to such capital improvement expenses be provided and go through a petition and hearing process similar to that of the fair-return petition. Increases granted by these expedited petitions are often capped, amortized, and restricted as described below.

	<b>MNOI Fair Return Standard</b>	<b>Capital Improvement Cost-Recovery Standard</b>
Alameda	✓	✓
Berkeley	✓	✓
Hayward	✓	✓
Los Angeles	✓	✓
Oakland	✓	✓
San Francisco	✓	✓
San Jose	✓	✓
Santa Monica	✓	
West Hollywood	✓	

See Attachment 4 for an in-depth review of cost-recovery mechanisms in rent-stabilized jurisdictions.



## **POLICY OPTIONS FOR CONSIDERATION**

*Question No. 1: Does the RHC request staff draft regulations for a Specified Capital Improvement petition process?*

*Question No. 2: Does the RHC have any input or additional parameters/qualifications it would like to add to consider eligibility for those improvements?*

*Question No. 3: Does the RHC have any input regarding the proposed share of costs?*

*Question No. 4: Does the RHC have any input regarding the proposed amortization and sunset periods?*

*Question No. 5: Does the RHC request staff draft regulations for a joint petition between landlords and tenants process?*

## **FISCAL IMPACT**

There are no associated increased costs as a result of this Study Session. The inclusion of the proposed petition processes may increase the number of upward adjustment petitions received by the RHC, resulting in increases in the costs associated with hearing processes.

**PUBLIC NOTICING** – Agenda posting.

PB-KMT-AVD/TG/6/CDD/RHC  
812-01-25-21M-2

- Attachments:
1. City of San Jose Capital Improvement Petition Form
  2. Draft Authorized Expenses and Amortization Schedules
  3. City of San Jose Joint Petition Form
  4. Cost-Recovery Mechanisms in Rent Stabilized Jurisdictions
  5. August 24, 2020 RHC Memo – Draft Regulations Amending Chapter 6: Specified Capital Improvement Upward Adjustments
  6. CSFRA Regulations: Chapter 6
  7. CSFRA Regulations: Chapter 9