City of
Mountain View

MEMORANDUM

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Stakeholder meetings, Base Rent and Concessions

April 28, 2022

Background

Stakeholder meetings were held on April 28, 2022, to request input about the definition of Base Rent and whether provided concessions should or should not be included when calculating Base Rent.

The definition in the CSFRA of Base Rent for tenancies starting after October 19, 2015, is: "The initial rent charged upon initial occupancy, provided that amount is not a violation of the CSFRA or any provision of state laws". The RHC requested specific input with regard to the term **"initial rent"**, defined in the CSFRA as **"initial rent means only the amount of Rent actually paid by the tenant for the initial term of the tenancy."** This definition cannot be changed by the Rental Housing Committee; however, it can be further clarified through regulations.

Both landlords and tenants reached out to the Rent Stabilization Program with questions about whether concessions (reduced, discounted or free rent) provided by a landlord to a tenant upon a move in, should be taken into account when determining the Base Rent, from which next year's allowed Annual General Adjustment (AGA) is calculated.

For example, if a tenant signs a 12-month lease for a monthly rent of $3,000, and receives a concession of 2 months free rent, should the Base Rent be calculated using the $3,000, not taking into account any concessions, or should the concession be taken into account when calculating the average monthly rent, *since this is the amount of rent actually paid by the tenant,* resulting in a Base Rent of $2,500 (10x$3,000 divided by 12=$2,500).

The issue is further complicated when landlords give concessions in the form of reduced rent for the entire term of the initial tenancy. For example, if a tenant signs a lease for a monthly rent of $3,000 and receives a concession of $500 per month in reduced rent, should the Base Rent be calculated not taking the concessions into account, resulting in a Base Rent of $3,000 or should the concession be considered when calculating the Base Rent for the next term of tenancy resulting in a Base Rent of $2,500 plus the applicable AGA.

In order to receive feedback on this issue, the following questions were posed to stakeholders who attended the meetings:

- What is considered the Base Rent from which the following year's allowed rent increase can be calculated?
- Should concessions be included or excluded from calculating Base Rent?

Summary of Landlord Input

About 35 landlord/property managers attended the Landlord focused stakeholder meeting. Landlords are against including concessions in the calculation of Base Rent for the following reasons:

According to landlords concessions would no longer be used if they were to be included in the calculation of Base Rent. Concessions are:

1. Important to help make housing more affordable, keep tenants housed in case of hardships
2. Temporary and are not indicative of future discounts.
3. A marketing tool/expense to mitigate vacancy, help keep down vacancy rate/persuade tenants to move in/reduces barriers to moving in
4. Used to avoid tenants having to pay double rent
5. Must be seen as "deferred rent"
6. Comparable to providing e.g. a 10% discount in other businesses

Comments by Topic

1. Concessions have a positive impact on tenants with hardships

"I think we should acknowledge that a lot of these concessions were in response to COVID-19, and landlords made accommodations to benefit tenants. Tenants without work had to move. Now landlords are in effect being punished for this. New jobs are back, with higher salaries than ever, but the true base rent is down 34% since before COVID (Rumper). Adding another reduction would make this 50% lower."

"Discouraging concessions by including these in the calculation of Base Rent will have a negative impact on tenants and discourages landlords to work with tenants during hardships. By redefining Base Rent the City is taking away the ability to provide temporary relief in times of future mass crises or individual need such as relocation, unexpected lay off, or other life crisis. Concessions give the flexibility to help tenant stay in their homes. If you'd like to make base rent an average of the 12 months, I don't think the COVID years should be included because they were by no means normal rent collection years."

2. Concessions are temporary and not indicative of future discounts.

"Tenants understand that concessions are a one-time temporary waiver of rent to help with a one-time expense such as moving costs, or one-time tenant relief in case of a job loss. Concessions are not indicative of future discounts. Our tenant agreements containing concessions clearly state that concessions are a one-time waiver of rent, and a simple Google search will also reveal the temporary nature of concessions. To convert these temporary reductions into long term permanent base rent reductions is not in line with the definition or spirit of this type of mutual agreement between the landlord and tenant."

3. <u>Concessions are a marketing expense/tool:</u>

"I would like the panel to consider that a concession be viewed as a marketing expense (more of a managed burden) that the landlord carries to mitigate uncertainty of actual loss due to vacancy. Potential vacancy losses are potentially significant without having that practical business tool that other industries have at their disposal to mitigate potential losses through common and reasonable marketing practices."

4. <u>Concessions increase affordability and help tenants with moving costs</u>

"Concessions alleviate the burden of moving for the tenant and avoid tenants having to pay double rent for any overlapping month. It is a temporary relief separate from rent."

"Concessions increase the affordability which is one of the key purposes of the CSFRA."

"The proposed amendment penalizes housing providers who offer these one-time bonuses to promote housing stability and security."

5. <u>Concessions must be seen as Deferred Rent</u>

"Landlords provide concessions only after the initial rental term ends. The discount is only provided when the tenant completes the initial term and should not be calculated in the Base Rent."

6. <u>Concessions are comparable to providing e.g., a 10% discount in other businesses</u>

"Any business uses discount tools in their business. Concessions are the rental market of providing the same type of discounts."

Other Comments

a. <u>Base Rent should be the agreed upon rent in the rental agreement between tenant and landlord</u>

"Rent should be defined as the rate agreed upon by both the tenant and the housing provider in the rental agreement."

"By removing move-in concessions or renewal concessions (which is the likely outcome should this new/expanded definition be implemented), CSFRA is creating a barrier to new housing. COVID conditions aside, moving is costly and housing providers try to ease that burden by providing concessions, but cannot do so at a long-term penalty against a fair rate of return."

"The upshot of including concessions into calculation of Base Rent is that this would effectively end concessions, which is a crucial tool in our industry that benefits stakeholders and tenants alike. It's important to note that this ending of concessions would occur not simply because of the chilling effect that would likely follow, but because concessions, as we currently understand them, would no longer exist. They would essentially be rent changes."

b. <u>The proposed Regulation Is inconsistent with the plain language of the CSFRA.</u>

"Currently "base rent" for tenancies commencing after October 19, 2015, is defined by Section 702(b)(2)1 as "the initial rental rate charged upon initial occupancy, provided that amount is not a violation of this Article or any provision of state law. The term 'initial rental rate' means only the amount of Rent actually paid by the Tenant for the initial term of the tenancy."

"The "initial rental rate" is the monthly gross rent - it does not include concessions because those concessions are a credit or rebate on the initial rental rate. Had CSFRA intended "Base Rent" to include reductions to rental amount set forth in the lease to account for concessions, this would have been written into CSFRA, but it was not and the RHC's attempt to do so now exceeds RHC's authority."

"The CSFRA's current definition of base rent does not require that rent concessions, rebates, or discounts offered to a tenant be included in its calculation. Rent concessions, discounts or rebates are nowhere mentioned in the definition of base rent (or anywhere within the CSFRA), nor is there any reference to the monthly averaging calculation as is cited in the proposed regulation. The definition of "rent" informs what base rent is to include in two important ways. Base rent includes "all nonmonetary consideration." A concession like free rent is a non-monetary consideration received by a landlord in exchange for the value of a tenant moving into the unit or remaining in the unit."

c. <u>Retroactive Application of the Amendment Violates Housing Providers' Right to Due Process.</u>

"Any effort to apply it retroactively, when landlords were not reasonably on notice of this unprecedented interpretation, would work a fundamental unfairness in violation of due process."

"Landlords would be put in this fundamentally unfair position through no wrongdoing of their own but because the proposed regulation altered the definition of base rent in a way they could not have reasonably foreseen, and in violation of their constitutionally protected contract and due process rights."

d. <u>Comparison with other Jurisdictions is incorrect</u>

"Other jurisdictions who include concessions in the calculation of Base Rent are City approved regulations/ordinances. In this case the RHC would make a "material" change to the definition of Base Rent, which it is NOT allowed to do. It also is not in sync with State Law 1482 which stipulates that concessions are not factored in Base Rent."

"It should be noted that the City of Berkeley enacted an exception to its rent control ordinance that allows COVID-related rent concessions to be excluded from the calculation of future rent increases."

"The California Legislature excludes discounts, incentives, concessions and credits in determining the gross rental amount in the state-wide rent control law (AB 1482). Los Angeles likewise excludes concessions."

Questions Raised

"What is rationale for RHC's ignoring the definition of rent in CSFRA which includes "all periodic payments and all nonmonetary consideration"?"

"What are the benefits or drawbacks from including or excluding concessions from calculating Base Rent?"

"Maybe the revised definition could include language something like "If Resident and Landlord have agreed on the amount the rent will be at the termination of the bonus period, that agreement will be binding.""

"Could you please include in the staff report on this item the data on the number of calls, inquiries on this item so it's part of the public record. Please make the statistics on inquiries on this topic (Tenant#, Landlord#) part of your report to the RHC prior to the May meeting."

"Could you please put the draft regulation out for comment before the staff report is published and then includes those comments in the analysis to the RHC?"

"Does the vacancy rate published by the RHC reflect just registered CSFRA housing or the overall MV market? Please specify both in your reporting."

Summary of Tenant Input

About 51 tenants attended the tenant focused stakeholder meeting. Tenants are in favor of including concessions in the calculation of Base Rent for the following reasons:

1. The definition of Base Rent specifically states "the initial amount actually paid for the initial term".
2. The real rent received as an average over the initial term (e.g., 12 months) makes sense.
3. Defining Base Rent as stipulated in the lease, instead of rent actually paid, makes rentals less affordable.
4. Defining Base Rent as stipulated in the lease does not reflect actual market rate.
5. If concessions are meant to entice tenants to move in, just lower the rent.
6. Concessions are used as a loophole to circumvent the CSFRA and makes the rent stabilization program less effective.

Comments by Topic

1. <u>The definition of Base Rent Specifically states "the initial amount paid for the initial term".</u>

   "The current definition states Base Rent is the initial amount paid for the initial term whether it included concessions or not. This should not be the amount listed on the lease without any concessions included. Base rent should be average of total amount paid by Tenant during Initial term of tenancy. for instance, if monthly rent is 3000 USD with 2 free months, then for 12 months lease total amount paid will be 30,000 USD and base rent should be 30,000/12 = 2,500 USD. Another example, if you sign a 13 month lease, and you get one month free, the base rent is RENT PAID * 12 months paid divided by 13 months".

2. <u>The real rent received as an average over the initial term (e.g., 12 months) makes sense.</u>

    "Base Rent should be calculated based on rent actually paid and received. The real rent received as an average over 12 months makes sense. The best way to define base rent is to use the average rent over the initial rental period. This covers all tenants who have concessions during any time in their initial period instead of just the people who had concessions at the beginning of their period."

3. <u>Defining Base Rent as stipulated in the lease, instead of rent actually paid, makes rentals less affordable.</u>

    "By allowing the base rent to be defined by the lease, tenants and renters lose more of their ability to live in this high cost of living state."

4. <u>Defining Base Rent as stipulated in the lease does not reflect actual market rate.</u>

    "Base Rent is not a landlord's perception about what they want rent to be. Base rent is what is actually paid. Landlords are trying to use the written lease amount as the base rent which is a money grab. Landlords have been using dishonest tactics in order to ensure that they fill their vacancies."

5. <u>If concessions are meant to entice tenants to move in, just lower the rent.</u>

    "If landlords want to entice tenants to move in, the best way is to lower the rent."

6. <u>Concessions are used as a loophole to circumvent the CSFRA and makes the rent stabilization program less effective.</u>

    "Concessions are a loophole to circumvent the CSFRA and violates the purpose of the CSFRA."

    "Meetings like this are one of the very few tools tenants have to protect themselves. By allowing the definition of base rent to be the amount written on the lease it essentially is a loss in the effectiveness of the whole rent control program."

Other Comments:

a. <u>Enforcement after one year</u>
    "If landlords are concerned about the concessions provided during COVID, then start enforcing the calculation of Base Rent including Concessions in 2023?"

b. <u>Landlords are less affected by Covid than other businesses</u>
    "Covid affected everyone including landlords. But landlords were not told to shut down their business, like many other businesses. So, landlords are less affected. What was paid and received makes the most sense, as the law states."

Questions Raised

"How does this affect you if your initial term is 6 or 3 months?"

"Is base rent retroactive? I moved in May 1, 2021 and my lease renews on May 1st (next Monday) but my landlord did not incorporate the fact that I received 1 month off as a rent concession."

"Are these questions related to Mobile Home Park lot rents?"

"If rent paid is the base rent, does that mean if I don't pay all my rent then my base rent is lower for calculating rent increase? In first year of my lease, I did not pay rent to my landlord for several months due to COVID and it was protected from eviction. Do the months I didn't pay rent impact the base rent when they calculated my rent increase?"

"You mentioned how some other CA municipalities have ruled on this question. The State of California itself has some state-wide rent control regulations now, how does their law interpret this question? Do they also use "rent actually paid during the initial term"?"