LINDSAY PROPERTIES, LLC

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August 22, 2018

City of Mountain View
Rental Housing Committee
PO Box 500
Mountain View, CA 94039

Dear Members of the Rental Housing Committee:

Subject: Appeal No. 17180002 – Tentative Appeal Decision - Lindsay Properties, LLC
Submission of Supplemental Materials in Response

Lindsay Properties, LLC ("Lindsay Properties"), respectfully submits the following response to the above-referenced Tentative Appeal Decision (the "Tentative Decision"). For ease of reference, our response tracks the issues in the same order as addressed in the Tentative Decision. Lindsay Properties objects to the following aspects of the Tentative Decision and requests that the Committee modify it accordingly. We also intend to address the Tentative Decision at the upcoming Committee hearing.

I. SUMMARY OF PROCEEDINGS.

Lindsay Properties accepts the Tentative Decision's summary of proceedings, with this additional background information that is not included in the Tentative Decision summary: Del Medio Manor has 104 rental units, and Lindsay Properties' petition covers 56 rental units. 20 of the tenants, members of the Del Medio Manor Tenants Association formed for the purpose of opposing the petition, are represented by the Community Legal Services of East Palo Alto in this proceeding. 36 of the Del Medio Manor tenants, whose units are the subject of the Lindsay Properties' petition, have not joined Respondent's opposition.

II. LINDSAY PROPERTIES' SUPPLEMENTAL MATERIALS AND DISCUSSION IN RESPONSE TO TENTATIVE DECISION

Lindsay Properties requests that the Committee modify the substance of the Tentative Decision as follows. We will be prepared to discuss these concerns as well as other aspects of our appeal at the upcoming hearing:

A. **Vega Adjustment, Including Hearing Officer's Reclassification of Junior One-Bedroom Apartments as Studio Apartments (Tentative Decision Section IV.A.)**

Lindsay Properties asserts that the Tentative Decision is incorrect on the Vega Adjustment issues and, for the following reasons, requests that the Committee reverse the Tentative Decision.

1. The Hearing Officer's Reclassification of Del Medio Junior One-Bedroom Apartments as Studios is improper and should be reversed.

The Tentative Decision's proposal to affirm the Hearing Officer's reclassification of Del Medio's Junior One-Bedroom Apartments as studios and deny a Vega adjustment would deprive Lindsay Properties of the proper upward adjustment and fair rate of return. Each of the factors described in the Petition, as well as the HUD information regarding Mountain View apartment sizes, supports maintaining the classification as Lindsay Properties has kept for decades. According to the HUD statistics for May 2018, the Del Medio Junior One-Bedrooms are 106 square feet larger than the average studio apartment in Mountain View; this is 91 sq. ft. larger than the Del Medio studios.

As reflected in Lindsay Properties' Documentation of Maintenance and Turnover Expenses submitted May 8, 2018, it costs more money to maintain the Junior One-Bedroom apartments based solely on the larger size. In all cases where carpeting or flooring is replaced, or the unit is repainted, the cost is significantly higher for a Junior One-Bedroom than a Studio. For example, flooring replacement costs $980 more. Repainting costs $75 more.

Finally, notwithstanding the efforts of the 20 tenants who formed the Del Medio Manor Tenant Association to discount the larger size and additional amenities provided by the Junior One-Bedroom apartments, all 28 tenants subject to the Petition who are living in the Junior One-Bedroom apartments, including 11 Del Medio Manor Association tenants, willingly chose to rent them—as well as stay in them when opportunities have arisen to move—over the studios, recognizing and accepting the higher rental rates that have always been charged for these units. Under these circumstances, it would be improper and unfair to deny a Vega adjustment for these units. For all these reasons, Lindsay Properties contests the Tentative Decision's proposal to affirm the Hearing Officer's unfounded reclassification. However, in the spirit of compromise and in recognition of the fact that even greater amenities are provided for a full one-bedroom apartment, Lindsay Properties would accept a Vega adjustment that is proportional to the difference in size among the studio, Junior One-Bedroom and the full One-bedroom apartments. Del Medio Manor Studios are 520 sq.ft., Junior One Bedrooms are 611 sq.ft. and One Bedrooms are 734 sq. ft. Based on the proportional difference in square footage, we propose that the Vega Adjustment for Del Medio Manor Junior One-Bedrooms be set at 143 percent of what it would be for Del Medio Manor Studios.

2. Resolving the discrepancy between Units subject to Rent Increase and Units Subject to Vega Adjustment

The Tentative Decision asserts that "the request for Vega Adjustments does not align with the units for which a rent increase is sought." To clarify our request, Lindsay Properties is seeking a Vega Adjustment only for those units that are covered by the Petition for upward adjustment of rents. All units in Del Medio Manor were included in "Worksheet 2.1: Vega Adjustment" per the instructions mandated in the petition. Header information for Worksheet 2.1 states, "Instructions: Complete columns b through h *for each unit in the property....*" (emphasis added). Again, there was no attempt to calculate a possible Vega adjustment for all units--only those units being considered for upward adjustment. Nevertheless, consistent with the instructions, we understood that ALL units were required to be listed as part of the analysis—whether they qualified for a Vega adjustment or not—in order to determine Total Gross Income for the Base Year (2015). We inferred that the City agreed with the approach reflected in the instructions because, having reviewed our petition, the City did not respond with direction to modify our interpretation of Worksheet 2.1 or its impact on Adjusted Gross Income for the Base Year in Worksheet 2

We note that, Lindsay Properties did not seek an increase for any unit that qualified for a Vega Adjustment but was less than $500 below market rates. It was not our intention to request increases for all units under market, only to focus on those units significantly below market i.e., more than $500 below market.

Please note that, for the reasons discussed above, a Vega adjustment should be granted for the 11 Junior One-Bedroom Apartments. With the Junior One Bedrooms added back in, the total number that should be granted a Vega Adjustment should be 33. We object to the Tentative Decision's statement that "the Petition *must be interpreted* to request a Vega Adjustment for 22 of the 56 Subject Units." Our Petition should be interpreted as written--requesting a Vega adjustment for all eligible units that are the subject of the Petition for Upward Adjustment.

3. The Factors the Decision Cites as a Basis for Rejecting the Vega Adjustment are Unsubstantiated and Improper, given that Lindsay Properties Refuted Each Unsubstantiated Allegation Made With Actual Evidence

As prescribed in the City's Vega Adjustment regulations (see page 4 of Petition and Attachment Example 2.1), granting of a Vega Adjustment necessarily addresses the physical and market conditions of the property. Market conditions overwhelmingly support this adjustment (Response to Respondents Supplemental Responses, Exhibit C- submitted 5/17/18).

The physical condition of the building also supports our requested adjustment as it has been maintained with pride of ownership for 45 years. The tenant statements of 20 of the 56 tenants on the petition make unproven and misleading allegations which Lindsay Properties refuted in detail in its document submitted on July 20, 2018. Contradictory and undocumented statements were made by tenants who failed to substantiate their allegations.

Inexplicably, the hearing officer failed to validate any of the claims made by tenants; further, the Hearing Officer failed to give consideration to Lindsay Properties' May 18 response, which

addressed each allegation in detail. (Response to Respondent Del Medio Manor Tenants Association Response Brief submitted 5/8/18).

Lindsay Properties' appeal document submitted July 20, 2018 contains nuerous examples of claims made without proof and substantiation. Lindsay Properties' written log of work orders for the past two years, which was submitted as evidence. (May 8, 2018-Work order history). This shows no requests for wall heater repairs, balcony repairs, noise issues, or broken towel bars. These issues only became complaints and appeared in Respondent tenants' statements when they were made aware that an upward adjustment had been requested. Ironically, aside from the 20 members of the Tenants Assocation opposing our Petition, Lindsay Properties has received no other complaints opposing our proposed rent increases based upon concerns about building conditions or maintenance.

There was never any evidence of structural deficiencies as was alleged by one of the 56 tenants. In fact, Lindsay Properties produced evidence showing that the building had a voluntary structural earthquake retrofit 14 years ago at a cost of over $150,000. The structural fortifications were far in excess of what was recommended by the structural engineer and architect. There was never any actual indication or proof of dangerous conditions.

The age of the building should have no bearing on the eligibility for a Vega adjustment as the building continues to be maintained and upgraded on a regular basis. Within the past three years the complex has installed a state-of-the-art exercise room, new furnishings in the recreation room, a permanent commercial bike rack which accommodates 28 bikes, and a new 60-inch television in the recreation room. The building has also received a new roof, solar panels for the pool, and a cutting-edge video surveillance system that provides greater security for our tenants.

To summarize, Respondent tenants' portrayal of Del Medio Manor Apartments as an old, neglected, and run-down building plays into the narrative the Tenant Respondents have advanced throughout this petition process, but it is grossly inaccurate and misleading. These unsubstantiated claims are not the proper basis for denying a Vega adjustment, particularly when the record reflects that all were addressed in Lindsay Properties' responses. We request that the Committee reconsider and change this determination.

For all these reasons, the Committee should reverse the Hearing Officer's Decision on the Vega Adjustment issue.

B. Calculation of Adjusted Gross Income (Tentative Decision Section IV.B-C)

Lindsay Properties continues to object to the Decision regarding the Calculation of Adjusted Gross Income in the Base Year and requests that Committee further review our submission and, if necessary, remand this calculation for further consideration.

Regarding the Calculation of Adjusted Gross Income in the Petition Year, in recognition of the Tentative Decision's proposal to remand for further consideration, we will be prepared to address on remand. However, for clarity, we point out that the entry in Worksheet 2: Adjusted Gross

Income line 1.a.1. is not germane to the determination of Total Gross Income for the Base Year. Worksheet 2 line 1.a.2. was used to calculate Total Gross Income as allowed in instructions for Worksheet 2. The entry in Worksheet 2 line 1.a.2. includes all vacancies as calculated in Worksheet 2.1., therefore, Worksheet 2 line 3.a. should be left blank per the instructions. Worksheet 2 line 3.b. Uncollected Rents was left blank because there was no uncollected rent in the Base Year.

Finally, we request that the Committee reject altogether Respondent Tenants' argument regarding "unimplemented annual general adjustments." Respondent appeals the Hearing Officer's decision not to impute to Lindsay Properties "unimplemented annual general adjustments" in the amount of $7,126.14 –an annual increase that Lindsay Properties did not and could not impose without losing its right to pursue the petition that is currently before the Committee. The CSFRA prohibits the imposition of more than one rent increase every 12 months. (CSFRA Section 1707b(3)). CSFRA Program Director Anky van Duersen advised Lindsay Properties that the "one increase every 12 months rule" applies to increases allowed by a decision on a petition as well as annual adjustments. Therefore, had Lindsay Properties imposed the annual increase that Respondent seeks to charge to Adjusted Gross Income in the Petition Year, Lindsay Properties would have been precluded from pursuing this petition. Based on that limitation, Lindsay Properties determined to wait to impose the annual increase until after this petition and appeal is resolved. Therefore, there is no basis for the Respondent's argument that Lindsay Properties should be treated as having received an additional $7,126.14 of income in the petition year. Rather than remanding this issue, the Committee should simply reject this aspect of Respondent Tenants' appeal.

C. Evaluation of Specified Expenses (Tentative Decision (Section IV.D-G)

Regarding Section IV.E and F of the Tentative Decision (Calculation of Base Year Management Expense and Exclusion of Petition Year Management Expenses), we request that the Committee reverse and remand, rather than affirm, the Hearing Officer's decision regarding Base Year Management Expenses. Subsections E and F of the Tentative Decision should be considered together on remand.

There appears to be confusion surrounding Worksheet 3.1: Reasonable Management Expenses.

The CSFRA limits the recognition of Management Expenses to 6 percent of Gross Income in the Base and Petition years. The amount claimed by Lindsay Properties in the base year was only 4.1 percent of Gross Income, much less than the 6 percent allowed but accurately reported and verified on certified tax returns.

To clarify, the actual amount incurred in the Petition Year was $26,981.49 greater than the 6 percent allowed. Therefore, Lindsay Properties complied with the CSFRA in the Petition Year by capping its claim for Management Expenses to six percent of Gross Income, approximately $111,000. We will address this issue further on remand as necessary.

Regarding the Tentative Decision Section IV.G, based on the hearing officer's decision there appears to be some confusion as to the structure and relationship between maintenance and

management expenses. Because of this, the Hearing Officer has disallowed eligible salaries relating specifically to the Del Medio Manor complex. We support the proposal to remand these issues and call attention to the following.

While casting aspersions on the amount and applicability of expenses is certainly a tactic to reduce eligibility for upward adjustment, the appropriateness of all payroll and maintenance expenses was established by the data Lindsay Properties submitted on 5/8/18. Every employee paycheck and the property their hours were attributed to was included. There is a clear distinction between work done at Del Medio Manor Apartments and other properties owned by the same company.

Based on fully accepted accounting and industry practices, all expenses incurred on the property for physical upkeep and onsite management are deemed property expenses. In contrast, management expenses are separate and are incurred by employees of the management company generally; each property pays at least 6 percent of its annual gross income in the form of management fees to the management company to cover these general expenses. However, the amount claimed was accurately capped at 6 percent as required by the petition. Our approach, reflected in our prior submissions, is fully supported by our certified tax returns, payroll checks, and employee descriptions requested by the Hearing Officer.

The following summary of our submissions and testimony demonstrates the distinction between property expenses and management expenses that Lindsay Properties has claimed.

Elizabeth Lindsay is the property manager for Calson Properties, and expenses attributable to her work are included in the general management expenses recovered under the six percent management fee. In contrast, Stephanie Valle is the Del Medio Manor onsite manager and all compensation to her is charged as an operating expense of Del Medio Manor Apartments.

Expenses associated with the Calson Properties Maintenance Staff are allocated across three properties, including Del Medio, and the hours they worked at Del Medio Manor were the only expenses applied to Del Medio Manor operating expenses in the petition.

For example, Jose Topete and Francisco Duenas work under the direction of the on-site manager, Stephanie Valle and complete outstanding work orders two days per week. Two days are spent at Meadowood Apartments in Mt. View and one day per week is spent at Castlemont Arms in Sunnyvale. Their compensation is allocated to these three properties accordingly.

George Gomez and Wilson Walch also work under the direction of Stephanie Valle but are focused on asset improvements such as fence repair, exercise room remodel, and other property improvements. These activities are all completed to code where appropriate and are inspected by Building Inspectors from the City of Mt. View.

The expenses arising from these activities have nothing to do with management expenses and resulting management Fees. They are focused on the day-to-day operation of Del Medio Manor Apartments and are appropriately charged as ordinary repair, replacement, and maintenance

expenses of Del Medio Manor. These expenses were explained, fully delineated, and indexed in the financial documentation we provided to the Hearing Officer.

D. Allocation of Upward Adjustment of Rents (Tentative Decision Section IV.J)

Lindsay Properties objects to the Tentative Decision's proposal to affirm the Hearing Officer's denial of Lindsay Properties' request that the requested upward adjustment be applied only to those rental units and tenants who are the subject of the petition and appeal. The Hearing Officer determined that the upward adjustment must be applied evenly to all rental units, despite the authority granted in Section 6J of the City's Fair Return Standard Regulations. This regulation provides that exceptions to the general rule are authorized and, as is the present case, are necessary in certain cases:

> "in the interests of justice, a Hearing Officer and/or the Rental Housing Committee may allocate Rent increases in another manner necessary to ensure fairness and further the purposes of the Act.

As explained in detail, Lindsay Properties' June 4, 2018 response to the Hearing Officer's request for authority to grant our request, allocating the rent increases to the 56 tenants who are the subject of the petition, and who benefitted from the 2015 rollback of rents, is necessary to ensure fairness and further the purposes of the Act. The Hearing Officer's Decision and the Tentative Decision rely solely on the fact that Lindsay Properties "does not charge expenses to any specific unit but charges expenses across all of them." Unfortunately, this narrow focus excludes consideration of the specific circumstances involved here (the very purpose of Section 6J) and misses the point of the authority granted in Section 6J and principles outlined in the court decisions summarized in our June 4 submission. This is not solely an evidentiary issue but also an issue of the proper exercise of the authority and discretion granted the Hearing Officer and the Committee. Both the CSFRA and constitutional principles of due process necessitate the result that Lindsay Properties has requested.

The allocation of the upward adjustment to the 56 tenants as requested is necessary to ensure fairness and to ensure that Lindsay Properties in fact achieves the fair rate of return mandated by the CSFRA and the legal precedent. In fact, it is the only way to ensure that we obtain the full amount of the upward adjustment to which Lindsay Properties is entitled. Requiring that the upward adjust be applied evenly to all 104 units would willingly ensure the opposite result—that the full amount of any authorized upward adjustment cannot and will not be obtained. Such a result would violate Section 6J's requirement to ensure justice and fairness and further the purposes of the act—including meeting the fair return standard mandated by the CSFRA. Further, such a result would violate the constitutional principles enunciated by the California Supreme Court. *Kavanau v. Santa Monica Rent Control Bd.*, 16 Cal. 4th 761 (Cal. Supreme Court 1997). Please see our June 4 submission on this issue, the substance of which was not addressed in the Hearing Officer's Decision or the Tentative Decision.

Application of the allowable rent increase to all 104 rental units, including those who are not subject to CSFRA, would ensure that this mandate of the Ordinance—to ensure a fair rate of return—would be frustrated. Put another way, the amount of any upward adjustment granted

equals the shortfall in current rents that should be recovered in order to meet the fair return standard. The increase makes up the difference between what is currently being paid overall and what needs to be paid overall in order to meet the fair return standard. As explained previously, tenants who have rented units since the CSFRA was implemented are already paying market rates—well above those rates being paid by the 56 tenants subject to our petition; these post CSFRA tenants cannot reasonably be expected to accept a further increase above market rates; to require it would drive them away.

Further, the financial contribution from those rental units not subject to the CSFRA are already accounted for in the calculation of the increase that is required to make up the difference and achieve a fair rate of return. To rule that the shortfall in rental income must be recovered from those tenants whose market rate contribution to the total rents is already accounted for in the upward adjustment is to effectively accept and even mandate a lower upward adjustment and thereby deny Lindsay Properties the fair rate of return that the ordinance and established case law require. The objectionable allocation mandated by the Hearing Officer would preclude Lindsay Properties from charging the approved upward adjustment to 48 of Del Medio Manor's 104 units. Accordingly, affirming the Hearing Officer's decision on this point would effectively disallow a full 46 percent of the fair rate of return that any approved upward adjustment otherwise would allow

It is the 56 tenants who are the subject of the petition, who are still at 2015-2016 rental rates and whose significantly lower rental rates are the cause of the shortfall represented by the upward adjustment, whose rates should be adjusted to make up the difference. These 56 tenants on the petition are the only ones who can reasonably be expected to make up the shortfall represented by the approved upward adjustment. In order for Lindsay Properties to obtain the full amount of any approved upward adjustment, it is critically necessary for the Committee to allocate the upward adjustment as Lindsay Properties requests.

E. Lindsay Properties' Response to Respondent's Appeal

Lindsay Properties contests all the contentions made by Respondent Tenants Association and will address them as needed in the upcoming Committee hearing and the remand to the Hearing Officer.

III. SUMMARY AND CONCLUSION.

In conclusion, Lindsay Properties reminds the Committee that this process is taking significantly longer than anticipated in the procedures the Ordinance and City have established. These delays alone are contributing to the failure of the City to ensure that Lindsay Properties and other Mountain View landlords achieve a fair rate of return. The Tentative Decision acknowledged this concern but did not address it in its decision.

Further, as the Committee considers this appeal, we remind you of the California Supreme Court's direction relating to rent control ordinances:

> Though due process protections generally focus on method, not result, in the context of price regulation, "it is the result reached not the method employed which is controlling. [Citations.] It is not theory but the impact of the [price regulation] which counts." (*Id.* at p. 602 [64 S.Ct. at pp. 287-288].) In sum, when considering whether a price regulation violates due process, a "court must determine whether the [regulation] may reasonably be expected to maintain financial integrity, attract necessary capital, and fairly compensate investors for the risks they have assumed, and yet provide appropriate protection for the relevant public interests, both existing and foreseeable." (*Permian Basin, supra,* 390 U.S. at p. 792 [88 S.Ct. at p. 1373].). Kavanau at p. 772. See also *Birkenfeld v. City of Berkeley*, 17 Cal. 3d 129, 169, 550 P.2d 1001, 1029□30 (1976), which,

If the Committee does not change the objectionable provisions of the Decision as discussed above and give clear direction to the Hearing Officer for consideration on remand, the result will clearly violate these same principles just as the Hearing Officer's Decision did. Contrary to the demands of the Tenants Association, it is not permissible to ignore these principles and the specific requirements reflected in the fair rate of return standard. Rather, maintaining financial integrity, attracting necessary, capital and fairly compensating investors for the risks they have assumed must be reflected in the Committee's decision and the Hearing Officer's decision upon remand, in order to achieve the fair rate of return mandated by the CSFRA and to withstand scrutiny from reviewing courts that must follow these legal precedents.

Lindsay Properties appreciates the Committee's efforts to resolve these issues. We look forward to addressing these issues at the Hearing, as well as resolving the issues that will be remanded to the Hearing Officer for further consideration based on the Committee's final decision and instructions.

Sincerely,

Elizabeth Lindsay