



17555 PEAK AVENUE MORGAN HILL, CALIFORNIA 95037

City Hall
Council Chambers
17555 Monterey Road
Morgan Hill, California

Chairperson: Swanee Edwards
Vice-Chairperson: Chuck Dillmann
Commissioner: John Liegl
Commissioner: Robert Graham
Commissioner: Elena Ann Miles
Staff: BAHS Margarita Balagso

MOBILE HOME RENT COMMISSION NOTICE

SPECIAL MEETING
Community & Cultural Center
17000 Monterey Road

February 12, 2008

7:00 P.M

Agenda

CALL TO ORDER
Chair Edwards

ROLL CALL

DECLARATION OF POSTING OF AGENDA
In compliance with Government Code 54954.2
Flag Salute

PUBLIC COMMENTS

NOW IS THE TIME FOR COMMENTS FROM THE PUBLIC REGARDING ITEMS NOT ON THIS AGENDA.

The Commission welcomes comments from all individuals on any agenda item being considered by the Committee. Please complete a Speaker Card and present it to the Secretary/Staff Liaison. This will assist the Committee Members in hearing your comments at the appropriate time. In the interest of brevity and timeliness and to ensure the participation of all those desiring an opportunity to speak, comments presented to the Committee are limited to **Three Minutes**. We appreciate your cooperation.

BUSINESS:

- 1. DELIBERATE UPON WINDMILL MOBILE HOME ESTATES OWNER'S PETITION** regarding proposed rent increase

ADJOURNMENT Next Regular Meeting is scheduled for February 25, 2008

NOTICE **AMERICANS WITH DISABILITIES ACT (ADA)**

The City of Morgan Hill complies with the Americans with Disabilities Act (ADA) and will provide reasonable accommodation to individuals with disabilities to ensure equal access to all facilities, programs and services offered by the City. If assistance is needed regarding any item appearing on the Mobile Home Rent Commission agenda, please contact the Office of the City Clerk at 17555 Peak Avenue, or call 779-7259 (or, Hearing Impaired only – TDD 776-7381) to request accommodation.

CITY OF MORGAN HILL

MOBILE HOME RENT COMMISSION

MEETING DATE: February 12, 2008

AGENDA ITEM: 1

TITLE: Commission Hearing Regarding Petition for Rent Increase at
Windmill Mobile Estates

RECOMMENDED ACTION:

It is recommended the Mobile Home Rent Commission:

- 1) Discuss the written materials submitted to date and the comments made at the December 3 Hearing.
- 2) Obtain clarification of any issue from the Owner, Tenants or Staff. If necessary, request revised or additional materials be submitted for the Commission's review and discussion at a subsequent special meeting.
- 3) Once the Commission is satisfied that it has all the documents and explanations it needs to make a decision (the "Final Record"), decide the matter by majority vote. The Commission must make findings to support its decision. The decision and findings must be consistent with the requirements of the Morgan Hill Mobile Home Park Rents Ordinance, Chapter 5.36 of the Morgan Hill Municipal Code (the "Ordinance").
- 4) Direct Staff to prepare a document setting forth the Commission's findings and decision. That draft document will be considered by the Commission for final adoption at a subsequent special meeting. Once finally adopted, the findings and decision shall constitute the final determination of the Commission as provided in Morgan Hill Municipal Code ("MC") Section 5.36.190.

DISCUSSION:

This memorandum provides discussion of five key areas the Commission should consider during the deliberation process: 1) Overview; 2) Threshold Issue: Timing of Owner's Petition; 3) Rent Increases Allowed by Ordinance; 4) Effectiveness of Any Authorized Increase; 5) Adoption of Written Findings and Determination.

In addition to these five key areas, staff provides a separate memorandum (Attachment A) which addresses the decision making process to facilitate determination of the necessary findings.

I. Overview

In accordance with MC Section 5.36.180, the Commission must make a determination whether or not the rent increase proposed by the Owner is reasonable under the circumstances. MC Section 5.36.250 provides guidance as to the meaning of "reasonable":

"The commission shall determine whether rent increases are reasonable under the circumstances taking into consideration that the purpose of this chapter is to permit owners a just and reasonable return on their property while protecting tenants from arbitrary, capricious or unreasonable rent increases. The commission's determination shall be made with reference to the standards set out in this article."

Therefore, the Commission is charged with applying the Ordinance to the facts presented. This means the Commission must (a) ascertain the relevant facts based upon the Final Record, and (b) reasonably interpret the various provisions of the Ordinance. Interpretations should be based upon guidance from relevant California court decisions, if available.

At the outset, one important point should be clarified. Owner alleges that unless it obtains a rent increase of \$192.55 per space, the Ordinance is unconstitutional. That allegation is a legal conclusion. Legal conclusions are rendered by Judges. MC Section 5.36.010 E states that the application of its provisions are intended to meet constitutional requirements. The Commission's job is to reasonably interpret and apply the Ordinance.

II. Threshold Issue: Timing of Owner's Petition.

Tenants have asserted that the Owner's petition should be dismissed because Owner instituted a rent increase in October 2007. MC Section 5.36.060 provides: "The space rent of any mobile home space may not be increased more than once in any twelve-month period." Owner responds that although it has submitted a petition for a rent increase, if the Commission approves any increase, the Commission can require the increase not be effective until October 2008.

Staff can find nothing in the Ordinance which establishes how many months in advance of the effective date of a requested increase that an owner's petition may be filed.

Further, MC Section 5.36.140 provides:

“Providing that a completed petition is timely filed . . . that portion of the requested rent increase (and only that portion) which exceeds the seventy-five percent increase in CPI limitation described in this chapter, shall not take effect unless and until such time as the rent commission allows such increase or portion thereof pursuant to the provisions of this chapter.”

The following options are available:

- 1) Consider the Owner's request and, if an increase is approved, make the increase effective in October 2008; or
- 2) Dismiss the Owner's petition stating why the Commission believes that the only reasonable interpretation of the Ordinance would require the Owner to reapply no earlier than October 2008.

III. Net Increases Allowed by Ordinance.

A. CPI Adjustment.

The Ordinance allows for an annual 75% of CPI increase without any review by the Commission (MC Section 5.36.060). Owner has instituted these annual increases, the last one effective October 2007.

B. Net Operating Income Analysis (MNOI).

The Owner is entitled by MC Section 5.36.080 to petition the Commission for an increase in excess of the 75% of CPI increase (MC Section 5.36.080). This is the matter now before the Commission.

MC Section 5.36.180 provides guidance to the Commission as to how it should evaluate the Owner's petition for reasonableness. That provision breaks down into two elements. The first part of MC Section 5.36.180 provides:

“Based upon the evidence presented at the hearing, the commission shall make a determination whether or not, in light of all the evidence presented, the proposed rent increase is reasonable under the circumstances, in accordance with the standards set forth in Section 5.36.250 and following of this chapter. The burden of proof regarding such reasonableness shall be on the owner unless otherwise indicated. The standards set

forth in Section 5.36.250 and following are expected to provide for a just and reasonable return to owner in all foreseeable cases.”

Therefore, first the Commission must determine what the Owner’s net operating income is. MC Section 5.36.250 and following sets forth guidelines for determining the Owner’s net operating income. The Commission is authorized by MC Section 5.36.310 to approve an increase which would allow the Owner to realize a return of that net operating income at the rate of 40% of the increase in the CPI over the base year (“MNOI”). And, in a case like this one, when less than 50% of the spaces in the park are affected, the MNOI return must be apportioned to only the rent-controlled spaces.

Owner is claiming the applicable MNOI would justify an increase of \$81.86 per space per month. In support, Owner has submitted calculations prepared by an expert, Richard S. Fabrikant MBA, Phd, a business/financial economist.

The Commission is charged with satisfying itself that the Owner’s expert has appropriately applied the Ordinance criteria. To that end, the Commission should review the transcripts and materials submitted to determine the basis to approve or deny a rent increase based on the MNOI analysis. The Owner’s discussion begins on page 7, line 16 of the transcript; and the Tenants’ response begins on page 43, line 7 of the transcript.

Additionally, the Commission is entitled, prior to rendering a decision, to receive clarification from the Owner’s expert, if needed, as to whether the expert properly interpreted and applied the Ordinance formula for calculating MNOI.

The following options are available to the Commission regarding MNOI:

- 1) Determine Owner’s calculations comport with the Ordinance and approve the requested increase;
- 2) Based on responses to questions, allow Owner’s expert the opportunity to revise and resubmit calculations for consideration by the Commission; or
- 3) If Owner is unable to satisfactorily answer relevant questions raised, deny the requested increase.

C. Increase Based Upon Unique or Special Circumstances.

The second part of MC Section 5.36.180 provides that, under certain circumstances, the Owner can petition for an increase in excess of MNOI:

"However, an owner shall be permitted to include within the petition additional facts showing that due to unique or special circumstances, the strict application of the formulas set out in Section 5.36.250 and following prevents a just and reasonable return on the owner's property to owner. If the commission concurs, then it may adopt an effective rent schedule or fix an increase thereto up to that required for just and reasonable return to owner."

In this case, the Owner has made such a request and is seeking a total increase of \$192.55 per space per month. Owner has submitted both legal arguments and a financial analysis prepared by its expert, Dr. Fabrikant, in support of the increase. Tenants have objected claiming Owner has failed to provide evidence of any unique or special circumstances which would authorize an increase above the MNOI calculation. Tenants have submitted legal arguments in support of that objection.

Again, the Commission should review the transcripts and submitted materials to decide if the Owner has demonstrated the existence of unique or special circumstances. While the Ordinance remains silent on the definition of unique or special circumstances, both parties have stated their position regarding such circumstances.

The Owner argues he has unique or special circumstances based on expert testimony that he is not receiving a fair and reasonable return on his investment. California courts have given deference to the evidence submitted by experts

In *H.N. & Frances C. Berger Foundation v. City of Escondido*, 127 Cal. App. 4th 1(2005), the California court said:

"Weighing the competing interests of owners and tenants and satisfying constitutional criteria is not a task within common experience. To the contrary, courts 'consider it a matter of expert opinion what rate of return on a mobilehome park is fair.'

"In *Whispering Pines*, the court held a rent commission erred by rejecting expert testimony on the fair rate of return issue and relying instead on 'factors of common knowledge and experience' such as the state of the economy and high interest rates. The court concluded that 'since there is no proper evidentiary basis for the

Commission's conclusions on a fair rate of return, there is no basis for the trial court's conclusion the Commission's findings were supported by the evidence. Similarly, in *Concord Communities* the court held the rent control board's finding that base rents were not significantly below market value lacked evidentiary support. The board rejected expert testimony and premised its finding on 'personal experience and knowledge of real estate.'"

The Tenants argue that the Owner did not prove such circumstances exist. Further Tenants submitted copies of California court cases defining "unique or extraordinary circumstances" which Tenants argue should be used as guidance to the Commission in making its determination.

Staff can find nothing in the Ordinance itself which provides guidelines to the Commission as to what constitutes "unique or special circumstances." Therefore, the Commission must exercise its reasonable judgment. In *MHC Operating Limited Partnership v. City of San Jose*, 106 Ca.App.4th 204 (2003), the Court said: "In the particular context of rent control ordinances, the [Commission's] interpretation of an ordinance's implementation guidelines is given considerable deference and must be upheld absent evidence the interpretation lacks a reasonable foundation. The burden is on the [party challenging the commission's decision] to prove the decision is neither reasonable nor lawful."

The following options are available to the Commission regarding the existence of a unique or special circumstance:

- 1) Determine a unique or special circumstance exists and if so, approve the requested increase ;
- 2) Determine no unique or special circumstance exists and deny any further increase; or
- 3) Based on questions to Owner, allow Owner the opportunity to provide any or all of the following for the Commission's consideration:
 - a. Additional evidence of a unique or special circumstance;
 - b. Legal authority as to how Owner's submittals would justify a finding of a unique or special circumstance; and/or
 - c. Resubmit calculations as revised by Owner's expert based upon a re-evaluation of the circumstances that rise to a level of unique or special.

IV. Effectiveness of Any Authorized Increase.

If the Commission decides any increase is allowed, it must also decide how any such increase would be implemented based upon the limitations of MC Section 5.36.320 which provides:

“Notwithstanding any other provision of this chapter, no upward rent adjustment may be authorized for any given year in an amount in excess of twice the San Francisco/Oakland Bay Area Consumer Price Index (CPI) or fifteen percent, whichever is less. The applicable figure for the CPI shall be the figure for the twelve month period ending sixty days before the notice of rent space was given. If the amount of any individual adjustment otherwise justified under this article is greater than such limit, the full justified amount shall be granted over a period of years such that the rent does not increase by greater than the limit in any given year.”

The CPI for August 2007 (60 days prior to notice of space rent was given) was 216.40. The change in the CPI from August 2006 was 2.63%. Therefore, based on this section, if the average monthly space rent is \$373 then a 5.4% (twice the CPI) increase would equal \$20.14. Any increase above \$20.14 would have to be passed on to Tenants over subsequent years. Each year this limit will change based on the CPI and the base rent rate it is applied to. The implementation period could take upwards of nine years to phase-in rents (e.g., if \$190/mo increase approved) depending on the CPI rate and approved increase.

The following options are available to the Commission regarding implementation of a phased increase:

1. Ask the parties to submit possible methodologies for implementation of a phased increase. The submittals should be supported by either (a) legal authority or (b) an agreement between the parties as to the suggested process.
2. Request Staff to prepare a proposed schedule of rent increases to comport with the Commission's authorized increase and submit that schedule for Commission's consideration.

III. Adoption of Written Findings and Determination

Finally, the Commission is charged with adopting findings supporting its decision. These findings and decision must be in writing. MC Section 5.36.190 provides:

“Within thirty working days following the conclusion of the hearing, the commission shall make a determination in writing that the proposed space rent increase is reasonable under the

circumstances or not, and shall make written findings of fact upon which such determination is based."

At the December 3 hearing, the Commission scheduled its oral deliberations for January 15. However, due to schedule conflicts, the Commission (with the concurrence of the parties) rescheduled the deliberations for February 12. It is possible based upon the deliberations that additional information will be required and the hearing continued.

Upon completion of the Commission's deliberations on a Final Record, Staff will prepare written findings and determination reflecting the Commission's oral actions. Those written findings and determination must then be submitted to the Commission for its final approval. A special meeting will be scheduled for the final adoption of written findings and determination as quickly as possible but within 30 working days of the Commission's conclusion of its deliberations.

Memo

To: Mobile Home Rent Commission
From: Business Assistance and Housing Services
Date: January 17, 2008
Re: **PROCESS FOR COMMISSION HEARING**

Staff has prepared this memo to assist the Commission with its decision making process. This memo is to be used in conjunction with the more detailed staff report. Because the issues are very complex, we have prepared the following "roadmap" of the process. By following this process, the Commission will be able to make the findings necessary to support its decision.

DECISION TREE

Below is a "decision tree" laying out the process the Commission should follow based on specific decisions. For example, a "No" decision in some instances would eliminate the need to further discuss some issues. Similarly, a "Yes," decision would lead the Commission down a different path. The following issues are presented in the order they should be considered. Each issue identifies the possible decisions available to Commission.

1. ISSUE – Can Owner submit a petition to the Commission for a rent increase within 12 months of Owner's last automatic cost of living increase? Owner has stated that if the Commission grants an increase it would be implemented no earlier than October 2008 which is 12 months after the last increase was implemented.

If NO – The Owner's petition is denied and no further decisions are required.

If YES –The Commission should proceed to Issue 2.

2. ISSUE – Owner is requesting a rent increase of \$81.86 per space per month based on the Ordinance formula for maintaining Net Operating Income ("MNOI"). The Commission is charged with determining whether the Owner has correctly applied the Ordinance formula.

The Commission is entitled to request further clarification, if necessary, before deciding. This may require a subsequent special meeting to consider the requested information. The Commission may also request the Owner or staff to recalculate amounts, if needed.

If NO – The Owner's rent increase request of \$81.86 is denied and no further decisions are required. The Commission will need to make findings for why the rent is denied.

If YES – The Owner's rent increase request of \$81.86 or a lesser amount as determined by a recalculation of the financial data is approved. However, a further decision will be needed on timing of implementation – see Issue 4. The Commission should proceed to Issue 3.

3. ISSUE -- Owner is requesting a total rent increase of \$192.55 per space per month based on an Ordinance provision allowing an Owner to prove that "unique or special circumstances" entitle an increase in excess of that authorized by the MNOI formula. There is no clear guidance in the Ordinance as to what the Owner must prove. Therefore, the Commission must exercise its reasonable judgment as to whether Owner has made this case. The staff report provides some for guidance on this matter.

Again, the Commission is entitled to request further clarification, if necessary, before deciding. This may require a subsequent special meeting to consider the requested information. The Commission may also request the Owner or staff to recalculate amounts, if needed.

If NO – The Owner's rent increase request of \$192.55 is denied.

If YES – The Owner's rent increase request of \$192.55 or a lesser amount as determined by a recalculation of the financial data is approved. (Please note: This amount would include the \$81.86 or a lesser amount if already approved by the Commission.) But, a further decision will be needed on timing of implementation – see Issue 4.

4. ISSUE – Any increase authorized by the Commission must be spread out over a reasonable timeframe so as not to increase a Tenant's rent by more than twice the annual CPI for any given year. For 2007, twice the CPI is about 5.4% which equates to a limit of \$20.14 per space per month on an annual basis (\$373 @ 5.4%). Each year this limit will change based on the CPI and the base rent rate it is applied to. The implementation period could take upwards of nine years to phase-in rents depending on the CPI rate and approved increase.

The Commission could request: a) staff to prepare a schedule of the proposed increases or b) the Owner to submit an implementation plan.

WRITTEN FINDINGS

After the Commission has made its decision regarding the four above issues, the Commission should direct Staff to prepare a document setting forth the Commission's findings and final decision. That draft document will be presented to the Commission for its consideration and final adoption at a subsequently scheduled meeting. Upon adoption, the Commission will have completed its task.