

Rent Stabilization and the Berkeley Rental Housing Market

- 1. Berkeley in the San Francisco Bay Area Rental Housing Market (slides 2-8)**
- 2. The Effects of Vacancy Decontrol on Berkeley Rental Housing (slides 9-15)**
- 3. Rent Stabilization and the Policy Challenge for Berkeley (slides 16-19)**

Part I: A High-Rent Regional Market

Figure 1: 2010 Median Rents

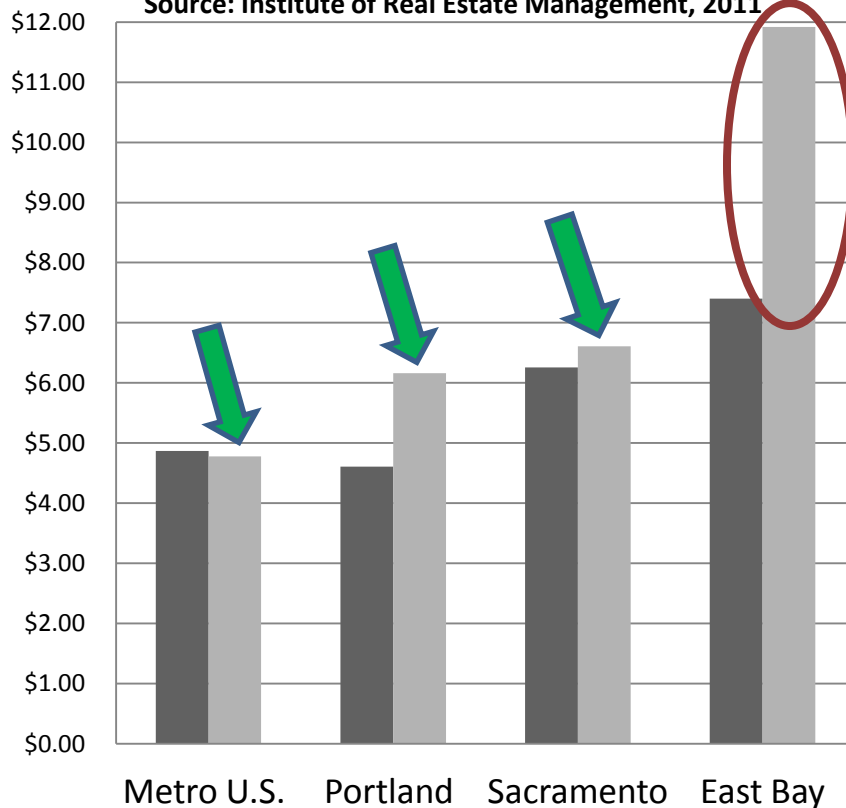
Source: Bureau of the Census



The Bay Area's High Rents are Neither Normal Nor Necessary

Operating Expenses and NOI for Apartment Buildings in 2010

Source: Institute of Real Estate Management, 2011



- Operating Expenses per square foot
- Net Operating Income (NOI) per square foot

- East Bay rents are far above
 - rents in reasonably competitive markets such as Portland & Sacramento
 - what is really necessary to profitably operate and maintain rental housing

Why Rents Are So High

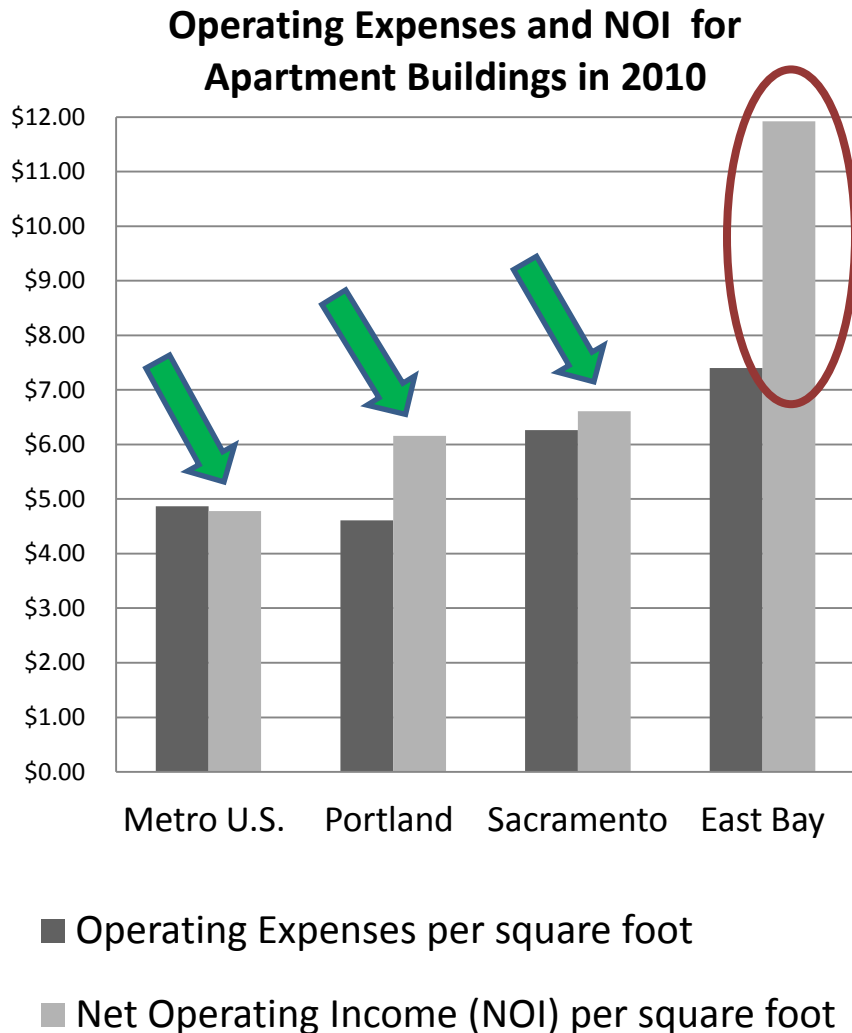
High demand

- Beauty of the natural setting
- Diverse and creative culture
- Strong regional economy
 - anchored in Berkeley by University of California
- Quality public services
 - City, BUSD, County, BART, EB Regional Parks, etc.

Constraints on supply

- Bay, ocean & hills limit land to build on
- Land use regulations often favor single-family homes over apartment buildings
- High cost to redevelop urbanized land at higher densities

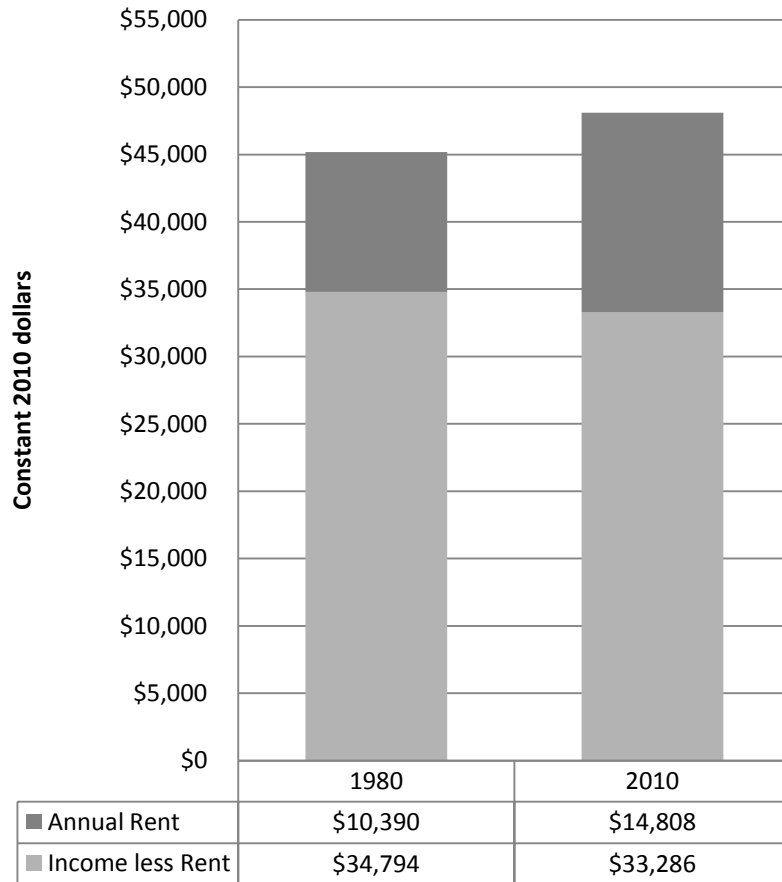
Market Failure Leads to High Rents



- Bay Area, L.A., San Diego are islands of high rent
- After 30+ years we find this normal and people tend to believe the normal is necessary
- Portland is a great city, with reasonable rents, not a devastated ruin
- Homeowners contributions raise their property values, renters contributions raise their rents.

Income left after paying rent is down

Fig. 2: Income Remaining to Median Income Bay Area Tenant After Paying Median Rent, 1980 & 2010



- 1980 and 2010

Median real income up 6% for tenant households

Median real rent up 43%

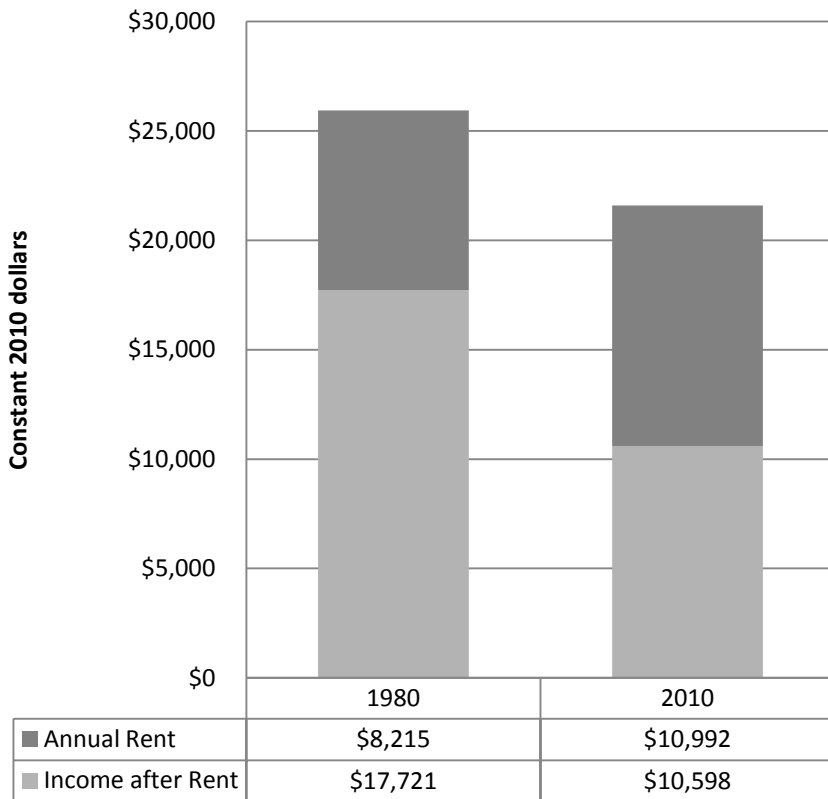
Income remaining after paying rent is down 4%

- “Real” rent & income = inflation-adjusted constant 2010 dollars

Very Low-Income Tenants Hit Hard

Fig. 3: Income Remaining to Very Low-Income Bay Area Tenants After Paying Low-End Rent : 1980, 2010

(25th percentile tenant income and rent)



- 1980 and 2010
(constant 2010 dollars)

Very low-income tenant has 17% less real income

Low-end real rent up 34%, takes more than half of income

Income remaining after paying rent is down 40%

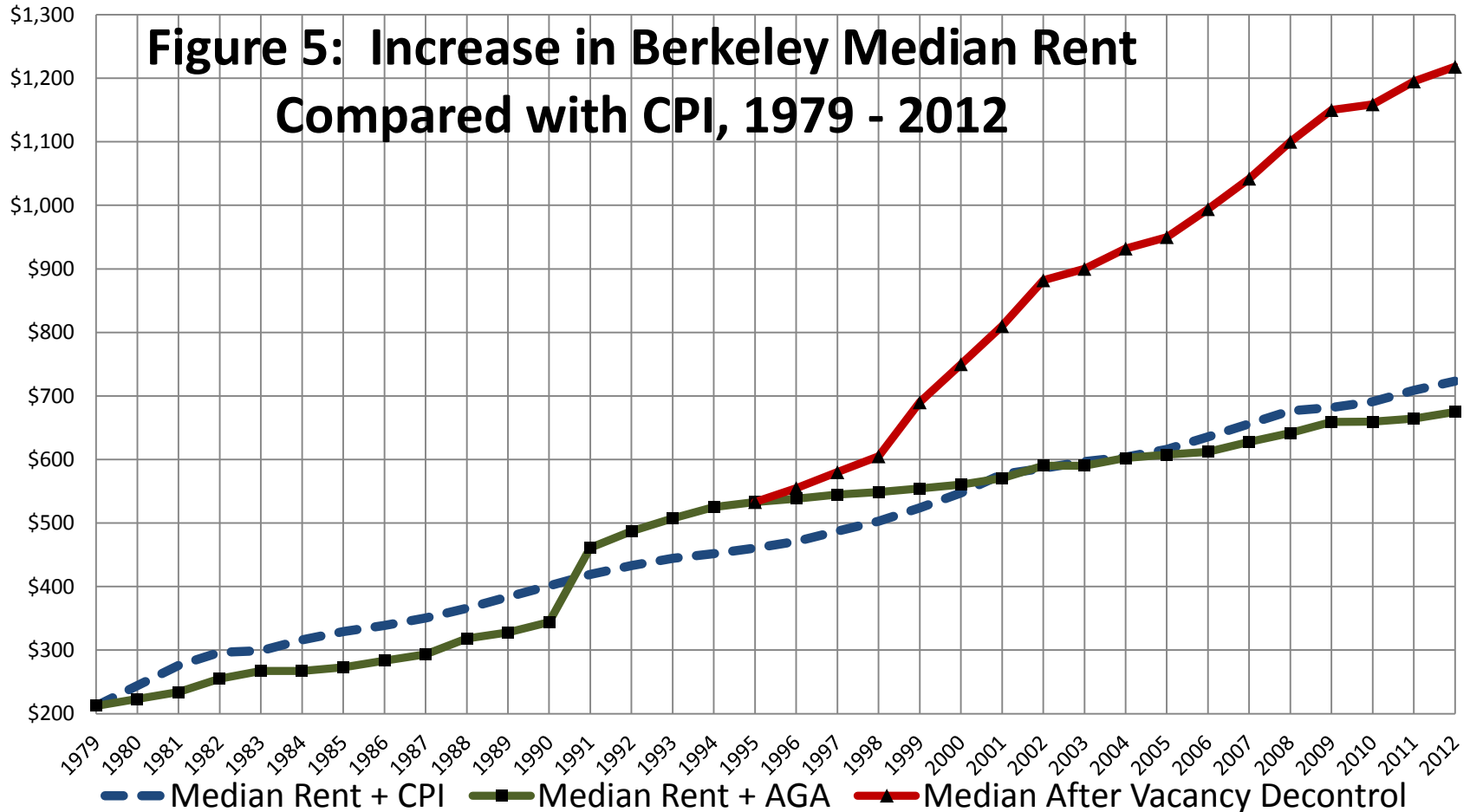
The Original Purposes of Rent Control

- The 1980 Ordinance proposed to “protect tenants from unwarranted rent increases and arbitrary, discriminatory or retaliatory evictions”
- “unwarranted rent increases” are rent increases
 - Beyond what is actually necessary to profitably operate and maintain rental apartments
 - Beyond what rents would be if a competitive market had stabilized rents in 1980 so that after 1980 rents went up at a rate related to inflation.
 - “old rent control” = market rents in Portland

Part II: The Effects of Vacancy Decontrol on Rental Housing in Berkeley

- Proponents of vacancy decontrol argued that it would result in
 - An increased supply of rental housing available to low-income, elderly and minority tenants
 - greatly improved buildings
 - a fair return on investment for landlords
 - higher tax receipts
 - City could use additional tax revenue to assist truly needy low-income tenants

Rent Stabilization and Inflation Before and After Vacancy Decontrol in 1999



Real Rent Increased 50% Under Vacancy Decontrol

- Since 1999, rents for 16,000 of 19,000 rent stabilized apartments increased by about \$100 million annually
 - This is over and above the inflation adjustment necessary to provide owners with a fair return on their investment
 - Total rent is now approximately \$300 million annually in rent stabilized apartments
 - Average vacancy rent - \$1,436 monthly

Vacancy Decontrol & Building Renovation

Rate of renovation is low

- 44% increase in permit values since vacancy decontrol
- If assume renovations at 300% of permit valuations
- = 6% of the increased rent
- \$6 million annually is now invested in building renovations
- = 2% of total rent

Need for renovation is high

- 2,000 “soft story” apartments remain at-risk of collapse in the event of a major earthquake
- In 2009 Tenant Survey one quarter reported unresolved maintenance problems (projects out to 4,500 apartments with problems).

Property values and reinvestment

Minimal reinvestment

- Increased taxes are under 4% of increased rent
 - 70% have old assessed values, resulting in a tax saving of \$9 million - \$10 million a year
- Total reinvestment in the community through renovations and increased tax payments is less than 10% of the increase in rent.

Major increase in property values

- Increase in total annual cash flow = \$90 million
- The total value of these rental properties increased by \$1.2 - \$1.5 billion
 - (cap rate of 7.5% to 6% applied to \$90M cash flow)
- Total rental property values nearly double after vacancy decontrol
 - Capital gains tax rate on sale

How Some Landlords Lose Money on Profitable Rental Property

- Investment in rental property is usually a partnership between a lender and a landlord
 - Lender: limited profit, priority on NOI, lower risk
 - Landlord: pays operating expenses, pays “investment expenses” (mortgage and any building renovations) and gets remaining NOI (cash flow) and capital gains
- *No matter how high the rent and NOI, some landlords will pay too much for a property and/or take loans that result in losing money*
 - Lender and/or former owner takes the profit

How Tenants Cope with Higher Rents

- 16,000 apartments occupied by tenants who moved in after 1998, subject to vacancy decontrol.
- 1/3 rented to students, 2/3 non-student households
- Students double up, two or more to a bedroom.
- Non-student tenants have 11% higher average real incomes in 2009 than in 1998.
- Non-student tenants pay more of their income for rent.
 - 53% pay more than 30% of their income for rent, up from 41% in 1998.
 - 28% pay more than half of their income for rent, up from 20% in 1998.

Part III: Rent Stabilization and the Policy Challenge for Berkeley

- The Rent Stabilization Ordinance remains essential for community stability
- Rent Stabilization continues to provide 21,000 tenants with predictable rents after they move in
- Eviction for Good Cause continues to provide 26,000 tenants with stability in their homes
- The Rent Stabilization Program ensures most tenants and owners are educated about their rights and responsibilities
 - “Berkeley can be very proud it certainly has the most educated tenants in the United States.” President, Berkeley Property Owners Association, 2003

“Old Rent Control” still a major City affordable housing program

- Low-income “old rent control” tenancies 2,200 households
 - Half disabled or elderly
- Subsidized housing developments 2,000 apartments
- Inclusionary or density bonus 200 apartments
- Monthly rental assistance 2,000 households
 - Housing Vouchers and Shelter + Care
 - Overlap with subsidized development (300)
- ***Total assisted low-income households – 6,100 households***

Cost of replacing “old rent control” with subsidies for low-income tenants

- Rent Program current operating budget is \$4.05 million.
- Estimated cost of subsidizing 2,200 low-income “old rent control” tenants without rent stabilization.
 - Through vouchers \$20 million annually
 - Vouchers over 20 years \$400 million
 - Through Housing Trust Fund \$220 million
 - HTF one-time capital subsidy with Federal or State matching subsidies
- Cost of subsidizing all very low-income tenants is at least double these amounts.

Policy Challenges for the City of Berkeley

- Rent Stabilization and Eviction for Good Cause continues to provide tenants with essential services but under vacancy decontrol cannot keep housing affordable when tenants move.
- Despite high rents City does not ensure that all rental housing is safe and well-maintained.
- *Can we find measures that will*
 - *Benefit low-income tenants harmed by rent increases?*
 - *Generate greater reinvestment in rental housing?*
 - *Generate reinvestment in the community?*

Summary

- 1. Regional Market Overview (slides 3 – 9)**
 - a. Berkeley is part of larger, dysfunctional regional housing market that generates unnecessarily high rents**
 - b. Benefit investors and harm low-income tenants**

- 2. The Effects of Vacancy Decontrol on Berkeley Rental Housing (slides 10 – 16)**
 - a. Decontrol -- major increases in rents & property values**
 - b. Limited and insufficient reinvestment**

- 3. Rent Stabilization and the Policy Challenge for Berkeley (slides 17 – 20)**
 - a. Rent stabilization still important but limited**
 - b. How to protect and assist low-income tenants and promote reinvestment in buildings & community**