

BOARD of SUPERVISORS



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MEMORANDUM

TO: Robert Collins, Executive Director, Rent Board
Kate Hartley, Director, Mayor's Office of Housing and Community
Development

FROM:  Alisa Somera, Legislative Deputy Director
Rules Committee

DATE: April 10, 2018

SUBJECT: LEGISLATION INTRODUCED

The Board of Supervisors' Rules Committee has received the following proposed legislation, introduced by Supervisor Fewer on April 3, 2018:

File No. 180318

Ordinance amending the Administrative Code to prohibit landlords from seeking rent increases on existing tenants due to increases in debt service and property tax that have resulted from a change in ownership.

If you have comments or reports to be included with the file, please forward them to me at the Board of Supervisors, City Hall, Room 244, 1 Dr. Carlton B. Goodlett Place, San Francisco, CA 94102 or by email at: alisa.somera@sfgov.org.

c: Eugene Flannery, Mayor's Office of Housing and Community Development
Amy Chan, Mayor's Office of Housing and Community Development

1 [Administrative Code - Landlord Operating and Maintenance Expenses]

2
3 **Ordinance amending the Administrative Code to prohibit landlords from seeking rent**
4 **increases on existing tenants due to increases in debt service and property tax that**
5 **have resulted from a change in ownership.**

6 NOTE: **Unchanged Code text and uncodified text** are in plain Arial font.
7 **Additions to Codes** are in *single-underline italics Times New Roman font*.
8 **Deletions to Codes** are in *strikethrough italics Times New Roman font*.
9 **Board amendment additions** are in double-underlined Arial font.
10 **Board amendment deletions** are in ~~strikethrough Arial font~~.
11 **Asterisks (* * * *)** indicate the omission of unchanged Code
12 subsections or parts of tables.

13 Be it ordained by the People of the City and County of San Francisco:

14 Section 1. Purpose and Findings.

15 (a) The Residential Rent Stabilization and Arbitration Ordinance (the “Rent
16 Ordinance”) is intended to protect tenants from excessive rent increases while also assuring
17 that landlords receive fair and adequate rents. Thus, although rents are capped, a landlord
18 may increase a tenant’s base rent by a certain percentage each year. This annual increase is
19 generally sufficient to provide landlords fair and adequate rents.

20 (b) A landlord may also file a petition with the Rent Board to increase base rents
21 beyond the annual increase, by up to an additional 7%, if the annual increase does not
22 completely cover the landlord’s increased operating and maintenance (“O&M”) expenses.
23 Examples of O&M expenses include the cost of day-to-day repairs, insurance, pest control,
24 garbage, water, and security. The purpose of an O&M increase is to help a landlord recover
25 from existing tenants the reasonable cost of keeping the building habitable, and to keep pace

1 with cost increases over time, to the extent the annual increase is not sufficient to cover those
2 cost increases.

3 (c) In recent years, more and more landlords have sought O&M increases on the
4 basis that their debt service and property tax costs have suddenly increased. But these costs
5 do not reflect amounts that were reinvested to maintain or improve the buildings. Rather, the
6 landlords claiming these increases are new buyers who are seeking to offset the costs of
7 acquiring property. The increase in property tax is based on the change in ownership and
8 reflects the high amounts that these buyers are willing to pay for these buildings; the annual
9 increase is intended to cover annual tax increases due to inflation. The increase in debt
10 service is due to the high amount of debt these buyers are willing to take on, and most rent
11 control jurisdictions in California do not allow rent increases based on increased debt service.
12 In short, property tax and debt service are not true O&M expenses, and treating them as such
13 encourages real estate speculation, fuels tenant displacement, and circumvents the purpose
14 of rent control.

15 (d) An article in the *San Francisco Chronicle* on December 11, 2017, documented
16 that many tenants in rent-controlled housing in San Francisco have recently experienced
17 exorbitant rent increases after their buildings were acquired by new owners (often large real
18 estate investment firms), largely because the owners were able to petition for O&M increases
19 to cover the cost of paying off loans taken to buy the buildings and the higher property taxes
20 that had resulted from the purchase price. Since the article was published, the Rent Board
21 has seen a dramatic spike in O&M petitions seeking increases based on property tax and debt
22 service, and many of the tenants of these landlords are now at risk of displacement. The
23 Board of Supervisors intends to prevent landlords from taking advantage of this loophole that
24 the news article exposed.

1 Section 2. The Administrative Code is hereby amended by revising Section 37.8 to
2 read as follows:

3 **SEC. 37.8. ARBITRATION OF RENTAL INCREASE ADJUSTMENTS.**

4 * * * *

5 (e) **Hearings.**

6 * * * *

7 (4) **Determination of the Administrative Law Judge: Rental Units.** Based upon
8 the evidence presented at the hearing and upon such relevant factors as the Board shall
9 determine, the Administrative Law Judge shall make findings as to whether ~~or not~~ the
10 landlord's proposed rental increase exceeding the limitations set forth in Section 37.3 is
11 justified or whether ~~or not~~ the landlord has effected a rent increase through a reduction in
12 services or has failed to perform ordinary repair and maintenance as required by State or local
13 law; and provided further that, where a landlord has imposed a passthrough ~~for property taxes~~
14 pursuant to ~~this Chapter 37~~ Section 37.3(6)(D), the same ~~costs increase in property taxes~~ shall not
15 be included in the calculation of increased operating and maintenance expenses pursuant to
16 this ~~§~~ subsection (4). In making such findings, the Administrative Law Judge shall take into
17 consideration the following factors:

18 (A) Increases or decreases in operating and maintenance expenses, including,
19 but not limited to, ~~real estate taxes;~~ water and sewer service charges; janitorial service; refuse
20 removal; elevator service; security system; insurance for the property; routine repairs and
21 maintenance; and real estate taxes and debt service as set forth in subsections (i) and (ii); and
22 reasonable and necessary management expenses as set forth in subsection (iii).

23 (i) ; provided, however, when a unit is purchased after the effective date of this
24 ordinance, For petitions filed before December 11, 2017, and this purchase occurs the Rent Board may
25 consider increased real estate taxes and increased debt service; provided, however, that if the property

1 has been purchased within two years of the date of the previous purchase, consideration shall
2 not be given to that portion of increased debt service which has resulted from a selling price
3 which exceeds the seller's purchase price by more than the percentage increase in the
4 "Consumer Price Index for All Urban Consumers for the San Francisco-Oakland Metropolitan
5 Area, U.S. Department of Labor" between the date of previous purchase and the date of the
6 current sale, plus the cost of capital improvements or rehabilitation work made or performed
7 by the seller.

8 (ii) For petitions filed on or after December 11, 2017, the Rent Board shall not
9 consider any portion of increased debt service, or that portion of increased real estate taxes that has
10 resulted from an increased assessment due to a change in ownership; provided, however, that the Rent
11 Board may consider that portion of increased real estate taxes that has resulted from the completion of
12 needed repairs or capital improvements.

13 (iii) For petitions filed on or after the effective date of this Ordinance No. _____,
14 the Rent Board may consider management expenses only to the extent those expenses are reasonable
15 and necessary, based on factors such as the need to provide day-to-day management of the building;
16 the level of management services previously required for the building; the reasonable cost of the
17 services in an arms-length transaction; whether any tenants have objected that the cost and quality of
18 the services are not in keeping with the socioeconomic status of the building's existing tenants; and
19 other extraordinary circumstances.

20 (B) The past history of increases in the rent for the unit and the comparison of
21 the rent for the unit with rents for comparable units in the same general area.

22 (C) Any findings which have been made pursuant to Section 37.7 with respect to
23 the unit.

24 (D) Failure to perform ordinary repair, replacement, and maintenance in
25 compliance with applicable State and local law.

1 (E) Any other such relevant factors as the Board shall specify in rules and
2 regulations.

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4 Section 3. Effective Date. This ordinance shall become effective 30 days after
5 enactment. Enactment occurs when the Mayor signs the ordinance, the Mayor returns the
6 ordinance unsigned or does not sign the ordinance within ten days of receiving it, or the Board
7 of Supervisors overrides the Mayor's veto of the ordinance.

8
9 Section 4. Scope of Ordinance. In enacting this ordinance, the Board of Supervisors
10 intends to amend only those words, phrases, paragraphs, subsections, sections, articles,
11 numbers, punctuation marks, charts, diagrams, or any other constituent parts of the Municipal
12 Code that are explicitly shown in this ordinance as additions, deletions, Board amendment
13 additions, and Board amendment deletions in accordance with the "Note" that appears under
14 the official title of the ordinance.

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Section 5. Severability. If any section, subsection, sentence, clause, phrase, or word of this ordinance, or any application thereof to any person or circumstance, is held to be invalid or unconstitutional by a decision of a court of competent jurisdiction, such decision shall not affect the validity of the remaining portions or applications of the ordinance. The Board of Supervisors hereby declares that it would have passed this ordinance and each and every section, subsection, sentence, clause, phrase, and word not declared invalid or unconstitutional without regard to whether any other portion of this ordinance or application thereof would be subsequently declared invalid or unconstitutional.

APPROVED AS TO FORM:
DENNIS J. HERRERA, City Attorney

By: 
MANU PRADHAN
Deputy City Attorney

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LEGISLATIVE DIGEST

[Administrative Code - Landlord Operating and Maintenance Expenses]

Ordinance amending the Administrative Code to prohibit landlords from seeking rent increases on existing tenants due to increases in debt service and property tax that have resulted from a change in ownership.

Existing Law

The Rent Ordinance allows a landlord to increase rents by a certain percentage each year (the "annual increase"). If the annual increase for a given year does not cover the amount by which the landlord's operating and maintenance ("O&M") expenses have increased that year, the landlord may file an O&M petition to increase base rents beyond the annual increase, by up to an additional 7%, in order to cover those increased costs. The Rent Ordinance lists real estate taxes, debt service, sewer service charges, janitorial service, refuse removal, security system, and elevator service as examples of allowable O&M expenses. The Rent Board has also treated building management as an allowable O&M expense.

Amendments to Current Law

The ordinance would prohibit the Rent Board from treating debt service and real estate taxes attributable to a change in ownership as O&M expenses, and would prohibit landlords from obtaining rent increases on existing tenants based on those costs, unless the landlord had already filed an O&M petition for those costs before December 11, 2017.

The ordinance would provide that the Rent Board may consider building management as an O&M expense only to the extent that the expenses are reasonable and necessary, based on various factors that are specified in the ordinance.

Background Information

December 11, 2017 is the date that the *San Francisco Chronicle* published an article concerning O&M petitions that are based on increased debt service and real estate taxes.

Separate from the annual increase and the O&M petition process, the Rent Ordinance also lets a landlord impose other types of rent increases on existing tenants, either with or without the filing of a petition, and generally lets a landlord reset the rent at market value at the start of any new tenancy.