

City of Los Angeles

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COUNCIL TRANSMITTAL: LOS ANGELES HOUSING DEPARTMENT REPORT ON THE ECONOMIC STUDY FINDINGS AND RECOMMENDATIONS TO AMEND THE FORMULA TO SET THE RENT STABILIZATION ORDINANCE ANNUAL ALLOWABLE RENT INCREASE

SUMMARY

The General Manager of the Los Angeles Housing Department (LAHD) respectfully requests approval of the recommendations in this report to amend the provisions that govern the setting of the annual allowable rent increase for rental units subject to the City's Rent Stabilization Ordinance (RSO).

RECOMMENDATIONS

That the City Council, subject to the approval of the Mayor:

1. REQUEST the City Attorney, with the assistance of LAHD, to draft an amendment of the Rent Stabilization Ordinance, Article 1 of Chapter XV of the Los Angeles Municipal Code (LAMC), to revise the methodology to establish the annual allowable rent increase for RSO rental units as follows:
 - a. Replace *Consumer Price Index All-Items for All Urban Consumers* with the *All-Items Less Shelter Index* in the methodology to establish the RSO annual allowable rent increase (LAMC 151.06.D and 151.07. A6);
 - b. Establish a floor of 2% for annual RSO rent increases;
 - c. Establish a ceiling of 5% for annual RSO rent increases;
 - d. Provide that in years when the otherwise permissible rent increase calculated by the formula above exceeds the 5% ceiling, the calculated percent above 5% shall be added (rolled over) to the subsequent years' allowable rent increase, with the total annual increase not to exceed 5%, and provide that LAHD shall publish the allowable rent increase annually by December 1st of each year; and
 - e. Delete the provision that allows an additional 1% or 2% increase for gas and/or electricity.
2. INSTRUCT LAHD to work with the Rent Adjustment Commission (RAC) to update the existing Rent Adjustment Commission Guidelines governing the Just and Reasonable rent increase program and conduct an outreach campaign to inform landlords on how to utilize the program and other cost reimbursement provisions of the RSO in order to ensure a fair return on their rental units.

BACKGROUND

In 2020, the City of Los Angeles adopted some of the strongest tenant protections in the country in order to avert widespread renter displacement and homelessness otherwise expected as a result of the economic impact of the public safety orders issued in response to the COVID-19 pandemic. Eviction protections for nonpayment of rent were maintained from March 2020 until February 1, 2024. Unless amended by the City Council, the annual allowable rent increase for RSO units of four percent (4%) commenced on February 1, 2024, and is in effect through June 30, 2025. Based on the existing formula, the annual allowable rent increase for RSO units beginning on July 1, 2025, through June 30, 2026, will be three percent (3%).

On October 31, 2023, as the City was preparing to lift the COVID-19 Tenant Protections, the City Council approved a motion (C.F. No. 23-1134), authorizing the Los Angeles Housing Department to negotiate and execute a sole-source contract with the Economic Roundtable, a non-profit, public benefit corporation, to conduct an economic study of the formula to set the RSO annual allowable rent increase, to include:

- Analysis of allowable rent increases in the California cities that have recently adopted or amended their formula for the annual allowable rent increase, including but not limited to Oakland, Bell Gardens, Antioch, Pomona, Santa Ana, and Oxnard
- The financial impact of the RSO rent freeze imposed during the COVID-19 pandemic
- A review of mandated City fees (i.e. RSO, SCEP, LASAN, RecycLA, DWP, etc.) impacting operating expenses in rental properties, including:
 - trash-hauling fees
 - water rates
 - electricity
 - insurance
 - property taxes
 - increasing labor and material costs
- Analysis of the impacts on homelessness in the City of Los Angeles, including the analysis from the 2020 U.S. Government Accountability Office study around median rent increases, for any recommended allowable rent increase caps and formulas.

This report provides the findings of the Economic Roundtable’s published study “Equitable Rent - Rent Stabilization Standards in the City of Los Angeles” dated September 2024 and proposed recommendations to amend the provisions regulating the RSO annual allowable rent increase.

The City’s Rent Stabilization Ordinance generally applies to rental properties built on or before October 1, 1978, and regulates approximately 651,000 rental units, representing nearly 74% of the City's multi-family housing stock. The RSO limits annual rent increases and allows landlords to increase rents in accordance with the Consumer Price Index, with a floor of 3% and a ceiling of 8%.

According to the U.S. Census Bureau, 63% of Angelenos are renters. Fifty percent (50%) of renters are rent burdened, paying more than 30% of household income for rent, and 30% of renters are severely rent burdened, paying over 50% of household income for rent. Los Angeles consistently ranks as one of the most rent-burdened cities in the nation.

As summarized on page 83 of the Equitable Rent Study, when the RSO was adopted in 1979, the annual allowable rent increase was set at a flat 7%. Since then, the RSO formula to set the maximum annual allowable rent increase was amended twice: in 1980, to allow an additional 1% for each utility (gas and electricity, only) and in 1985 to allow an annual increase based on the Consumer Price Index (CPI), with a ceiling of 8% and a floor of 3%.

The current RSO provisions utilize the Consumer Price Index All-Items for All Urban Consumers for the greater Los Angeles area, based on data from the Bureau of Labor Statistics from the US Department of Labor. The RSO allows a maximum annual rent increase of 100% of the change in the CPI, with a maximum 8% percent ceiling and a floor of 3%. Landlords who pay 100% of the cost of gas and/or electricity (but not water) are allowed to add an additional 1% annual rent increase for each utility, for a maximum annual increase of 10% if a landlord provides both gas and electricity.

Since the inception of the RSO in 1979, the City has undertaken four prior studies (1984, 1988, 1994, and 2009) that included an analysis of the methodology utilized to set the annual allowable rent increases. Both the 2009 study and the current study were conducted by the Economic Roundtable, a non-profit research organization based in Los Angeles.

SUMMARY OF THE MAJOR FINDINGS OF THE STUDY

The following is a summary of the major findings of the 2024 Study “Equitable Rents –Rent Stabilization Standards in the City of Los Angeles”. The full report is provided as an attachment to this report and available online at <https://economicrt.org/publication/equitable-rent/>

Los Angeles Housing Inventory

- Los Angeles has an estimated 1,549,889 total housing units for a total population of 3,822,224 residents, or 2.47 residents per unit.
- Almost two-thirds of Los Angeles residents rent the housing units in which they reside – 64 percent.
- Forty-two percent of the City’s residents live in rent-stabilized housing.
- Half of RSO properties were constructed before 1950, while another 29 percent were built from 1950 to 1970. The remainder were built in the 1970s.
- The preponderance of RSO-dominant neighborhoods is located in the Los Angeles basin, plus the Southeast San Fernando Valley.
- Rent stabilized units are older and concentrated in the urban core of Los Angeles. Non-RSO units are newer and concentrated in areas of Los Angeles that have been built-out more recently.

Los Angeles Renters

- RSO and non-RSO renters have similar demographic characteristics, including frequency of disabilities, ethnicity, level of education, age, sources of income, and English fluency.
- RSO and non-RSO renters differ in that RSO households are more frequently made up of a single person, and are more often overcrowded.
- Non-RSO households are slightly more likely to have moved recently.
- The average income of non-RSO households is 22 percent higher than the income of RSO households. However, both groups of renters have similar levels of rent burden because the average rent for non-RSO units is higher.
- Over the past three decades, rent has increased in the same ratio for RSO and non-RSO renters. However, given the higher average income of non-RSO renters, the same percent spent on housing is less likely to divert funds from other basic necessities.
- One-fifth (20%) of Los Angeles renters live in poverty based on the federal standard. More than half of these households (14% of Los Angeles renters) pay 90 percent or more of their income for rent. These highly vulnerable renters are likely to be younger, live alone, be unemployed or have annual incomes below \$20,000, and are more likely to receive public benefits. Additional findings regarding the demographics of vulnerable renter households are discussed in Chapter 4, pages 33 through 36 of the Study.

Rent Savings for RSO Tenants

- Citywide, the average rent for non-RSO units has been an average of 25 percent higher than for RSO units from 1990 through 2022. This is based on comparing all RSO units with all non-RSO units without accounting for where units are located or their size.
- There are differences in the size of RSO and non-RSO units, the shares of the RSO and non-RSO rental inventories located in different districts of the City, the income levels of renters in different districts of the City, and the average rent for RSO and non-RSO units in different districts of the City.
- Non-RSO units in the City of Los Angeles have an average of 2.1 bedrooms, whereas RSO units have an average of 1.5 bedrooms. Non-RSO units are typically bigger. This difference should be considered in estimating rent savings for RSO units.
- While it is feasible to control for the size of units in estimating the difference in rent for RSO and non-RSO units, it is not feasible to control for geographic differences.
- The rent differential between RSO and non-RSO units is the average of multiple different rental markets within the City.
- Based on comparing the rent for RSO and non-RSO units using both the number of bedrooms and total number of rooms as benchmarks, the average rent paid by RSO renters is **19 percent less** than the rent paid by non-RSO renters for units of comparable size.

Rent Increases and Homelessness

- The most frequent explanation that homeless adults in Los Angeles provide for their lack of housing is unemployment and lack of money.
- There is a direct connection between loss of income and loss of shelter, but these losses do not occur simultaneously. Disconnection from work is a degenerative dynamic - less work, less earnings, less stable living conditions, and further disconnection from work.
- One-quarter of renters in the Los Angeles region have household incomes under \$25,000. Eighteen percent of these households say it is extremely likely that they will be evicted in the next two months.
- Rent costs that exceed what tenants can pay is a primary cause of homelessness.
- Increases in income inequality lead to increases in homelessness because they simultaneously drive up the cost of housing and the percent of low-income renters who cannot afford that housing.
- There is a high rate of homelessness in Los Angeles primarily because of the interaction between the housing market and the labor market—namely, the high cost of housing and the high rate of working poverty.
- Los Angeles has relatively high local income inequality—and therefore, high homelessness—compared to the rest of the country.
- An increase in evictions is a driver of an increase in homelessness.
- The primary driver of evictions is the rising cost of housing.
- ***The eviction moratorium, rental assistance and fiscal stimulus programs were successful in preventing the rise of homelessness from being as severe as it would have been otherwise.***

2020 U.S. Government Accountability Office Study

The discussion of the study by the 2020 U.S. Government Accountability Office (GAO) is found on pages 48 – 50 in Chapter 6 of the Equitable Rent Study that discusses Rent Increases and Homelessness.

Financial Stress of Landlords by Size

- Small landlords with two to four units account for the plurality of the RSO housing inventory, 30 percent.
- The typical (median) RSO unit is in a building with 17 units.
- The buildings owned by small landlords with one to four units typically have more bedrooms than all other size classes of ownership. They provide an average of 46 percent more bedroom space than the overall average for the RSO inventory.
- Seventy-five percent of units in buildings with two to four units have two or more bedrooms, compared to 34 percent of units in buildings with five or more units.
- The average rent for units owned by small landlords is higher than the average rent for any other building size group and 20 percent higher than for the overall RSO inventory.
- When rents are compared on the basis of rent per bedroom, small landlords receive 16 percent less rent per bedroom than the overall average for RSO units.
- Fifty-seven percent of tenants in units owned by small landlords are reported by the Census Bureau to have been in their units five or more years. This compares to only 47 percent of tenants in all RSO units reaching the five-year mark, and is longer occupancy than any other ownership group. Less tenant turnover reduces lost revenue from empty units. However, it also reduces the frequency with which rents can be vacancy decontrolled and re-rented at market rates.
- Based on vacancy data from the Census Bureau, vacancy rates increase with ownership size; small landlords have the lowest vacancy rate. The person-to-person relationship between tenants in small buildings and their mom-and-pop landlords appears to make tenants more inclined to stay where they are.
- Vacancy rate data indicates small landlords have vacancy rates that closely match, or are lower than, other ownership groups.
- RSO landlords have less tenant turnover than non-RSO landlords, which reduces lost rent when units are vacant as well as costs to refurbish units for new tenants.
- Operating expenses for smaller buildings may be offset by self-management, which reduces cash outlays for managing small RSO buildings.
- Smaller RSO landlords appear to receive higher rent per unit, although lower rent per bedroom, and have lower vacancy rates than larger RSO landlords. The Study did not find evidence that they have greater financial stress than larger landlords.

Impact of the COVID Pandemic on Landlords

- Nationwide:
 - Landlords experienced a sharp increase in non-payment of rent during the COVID pandemic, which they addressed by granting more rent extensions, charging less rent fees, deferring maintenance, and listing their properties for sale.
 - Smaller landlords were more likely to experience non-payment of rent, and larger landlords were more flexible in managing this problem, for instance, by granting rental extensions or forgiving late rent fees.
 - Landlords were least likely to offer accommodations to renters of color for the same level of non-payment of rent.
- Rental assistance programs throughout the U.S. provided significant help to tenants, but did not reach as many tenants as administrators hoped due to strong resistance from landlords. However, in the City of Los Angeles, rental assistance was paid directly to tenants whose landlords declined to participate.
- In Los Angeles and Orange Counties, rental non-payment declined from 2020 to the end of 2023.
- Based on the Census Bureau's household surveys, approximately 13 percent of renter households in Los Angeles and Orange Counties are estimated to be currently behind on rent, with an average of 3.1 months unpaid.

- Since 2014, RSO properties have been far more successful in filling the average unit than non-RSO properties. This low turnover is likely due to the value that tenants find in rent-restricted units as rents and property values have risen in recent years.
- Despite earning lower rents for comparable units, on average, RSO landlords receive the compensating benefit of lower turnover costs, more stable revenue, and proportionally more revenue-generating units.
- The pandemic has had a more lasting negative effect on occupancy in non-RSO properties, where vacancy rates remain elevated.

Market Rate Rents, Restricted Rents, and Inflation

- From 2000 to 2023, the Los Angeles region had a higher rate of inflation than the rest of the United States, due entirely to housing costs. For all goods other than housing, the Los Angeles region actually became slightly more affordable than the rest of the country.
- From 2000 to 2023, housing added 0.3 percentage points to the annual national inflation rate and 0.6 percentage points to the annual Los Angeles inflation rate, accounting for 12 percent of inflation nationally and 21 percent of inflation in Los Angeles.
- From 2015 to 2024, average effective asking rents grew faster for RSO properties than for non-RSO properties (24.1 percent, compared to 15.6 percent), likely reflecting strong demand for protection against high rent hikes in an increasingly expensive market, as reflected in low vacancy rates.
- Los Angeles rents decreased significantly in the early months of the pandemic, erasing the outsized gains they had made relative to the rest of the country. From 2020 to 2023, rents grew more slowly in Los Angeles than in the rest of the United States.

Rent Regulation

- According to the Study consultants, increases in rents for RSO units are the result of the combination of increases in market rents at the commencement of a tenancy and annual allowable rent increases during tenancy.
- Annual general adjustments of rents were not permitted from May 2020 through January 2024. However, substantial rent increases, averaging 30 to 50 percent above the 2020 level, could be obtained from units with a turnover in tenants.
- Because of substantial turnover rates of about 50 percent within a four-year period, market rents are a central determinant of allowable rent levels and increases in rent under the RSO.
- From 2010 to 2020, the RSO annual allowable rent increases totaled 35.6 percent compared to a 20.9 percent increase in the CPI. In the five-year period from 2015 to 2020, the annual allowable rent increases totaled 17 percent, compared with a 12.5 percent increase in the CPI.
- Overall, due to substantial increases in market rents, move-in year is a central determinant of the current allowable rent of RSO units.

Operating Expenses and Other Costs for Low-Income Housing

- The largest expenses and losses for most Los Angeles landlords are capital expenditures, followed by vacancy, salaries and personnel, taxes, and contract services.
- The fastest growing expense from 2010 to 2022 for rent-stabilized properties has been property insurance, though it still comprises a small portion of total operating costs (4.6 percent to 8.6 percent).
- Operating expenses outpaced inflation in the Western region of the United States from 2010 to 2022, increasing 67 percent compared to 38 percent increase in the Consumer Price Index.
- Until 2019, increases in RSO rents mostly kept pace with increases in operating expenses, but have lagged inflation since the onset of the COVID pandemic.

- According to the consultants, for equity investors who have owned their properties for a long time, paid off their loans, and are now free-and-clear of debt, the average apartment unit in Los Angeles appears to be highly profitable.

Increases in Apartment Operating Costs

- In Los Angeles, operating expenses for apartments average about 35 percent of rental income.
- Assuming an average monthly rent of \$1,600 and an average operating expense ratio of 35 percent, monthly operating costs per rental unit average \$560.
- Property taxes average \$146 per unit per month for properties with five or more units and \$191 for properties with three or four units.
- Total utility costs for water, sewer, gas, and electricity generally amount to less than 10 percent of the rent. Therefore, the increases in utility rates that have exceeded the rate of inflation in recent years have not had a substantial impact on the net operating income obtained from rental properties.
- The Study authors project management expenses of four percent for offsite management expenses.
- Insurance costs formerly amounted to only about two or three percent of the rents but may have doubled within the past few years and continue to increase.
- The balance of rental income net of operating expenses - net operating income - is the return on the investment in the property, which is available to cover debt service and provide cash flow.

Returns from Rental Properties

- Average market values of RSO units have doubled over the last ten years from about \$150,000 to \$300,000 per unit and are nearly five times above their 2000 level.
- Historically, investors' expectation is that the cash flow will increase as rents and net operating income increase above their levels at the time of purchase, while mortgage payments will decline relative to overall income. This expectation and the leveraged nature of investment in rental property has made investments in rental properties attractive, notwithstanding low cash returns at the outset.
- Seventy-four percent of RSO units were purchased before 2015; thirty-eight percent were purchased before 2000. The average length of ownership is virtually the same for different size properties.
- Net operating income from rental housing investments has grown at faster rates than the CPI (3.9 percent versus 2.6 percent).
- The Study consultants conclude that there has been substantial growth in the net operating income of rental units covered by the RSO, although operating expenses have outpaced increases in the CPI.

California Rent Stabilization Laws

- In the 1980s, rent legislation was adopted by Los Angeles, San Francisco, Oakland, San Jose, Santa Monica, Berkeley, and West Hollywood and a few other cities.
- In the last eight years, the tightening of the rental market has led to the adoption of local rent legislation in fifteen other jurisdictions, including Los Angeles County, Culver City, Inglewood, and Pasadena and to the adoption of a state ceiling on increases in apartment rents of units that are not regulated by local ordinances. Eight of those ordinances were adopted between 2020 and 2022.
- Most rent ordinances tie annual allowable rent increases to all or a portion of the percentage increase in the CPI and place a ceiling on the allowable increase pursuant to the CPI standard.
- Fifteen of the ordinances limit the annual rent increase to less than 100 percent of the increase in the CPI.
- Twenty-two of the ordinances now in effect place a ceiling of either three, four, or five percent on allowable rent increases based on a CPI standard, or fix the annual increase amount at four or five percent.

- Under Los Angeles's RSO in effect prior to the pandemic, the allowable annual increases were greater than those permitted under a majority of the ordinances now in effect in other cities.
- In the decade before the pandemic, from 2010 to 2020, the result of the RSO standard in effect compounded move-in rents set under shortage conditions with allowable rent increases during tenancies that exceeded the CPI increase in years with low inflation.

Impacts of Alternative Policies Related to the Efficacy of the RSO Annual Adjustment

- The RSO provides security of tenure by limiting the rent increases after a tenant takes possession of the rental unit.
- Because of vacancy decontrol, initial rents are not regulated, so the RSO does not preserve the affordability of housing, except for long-term tenants, who constitute a minority of the tenant population. This limitation on rent control is mandated by state law, the Costa Hawkins Act. The City of Los Angeles, along with all rent-control jurisdictions in California, is required to have vacancy decontrol.
- The impact of the RSO on properties differs based on the frequency of tenant turnovers.
- Historically, questions and criticisms have been raised about the use of the *CPI All-Items Index* to determine annual increases on the basis that this index is based on the increases in the costs of a market basket of goods purchased by an average household, which differ substantially from basket of expenses associated with the operating of an apartment building.
- Apartment operating costs only constitute about 35 percent of rental income, while the annual general adjustment applies to all of rental income including the other 65 percent which is net operating income.
- In the past, some jurisdictions have conducted annual operating cost studies of the types of expenses incurred by apartment owners in order to tie allowable annual rent increases to trends in apartment operating costs. However, jurisdictions that used this methodology subsequently switched to a CPI standard.
- There are a number of CPI indexes that are based on the prices of particular commodities or types of services.
- Most discussion and consideration of the Consumer Price Index is centered on *CPI All-Items Index*.
- The *All-Items Less Shelter Index* is the CPI index recommended for use in determining the annual allowable rent increase. This would remove the circularity associated with using trends in market rents, which are heavily based on shortage conditions that motivated the adoption of the RSO.
- Annual rent increases should cover increases in apartment operating costs. An annual increase in the range of 35 percent of the percentage in the CPI would cover those cost increases in years in which operating costs increased at the same rate as the CPI, but would not allow for any growth in net operating income.
- An alternative to setting a fixed ceiling on allowable annual rent adjustments is to use a descending percentage of CPI increases above a specified amount. This type of standard recognizes the differences between different amounts of increase in the CPI.
- A disadvantage of allowing greater rent increases for small properties is that tenants in those properties would experience larger rent increases than the balance of the tenant population, although the rent levels of their units and the rate of increase in their rents may not differ from the average for other units.

Allowable Additional Rent Increases for Apartment Owners Who Pay for Gas &/or Electricity

- Under the RSO, apartment owners who cover either gas or electricity costs are permitted additional annual rent increases of one percent for each of these services. This impacts the rents of about 20 percent of all RSO units. In about eight percent of all units, an additional two percent is permitted based on the provision of both services. In 11 percent of all units, landlords pay for gas, but not electricity. In 1.4 percent of all units, landlords pay for electricity but not gas.
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Service	Percent of Units
Gas & Electricity	7%
Gas, But Not Electricity	11%
Electricity, But Not Gas	1.4%

Source: Economic Roundtable team analysis; City of Los Angeles Housing Department Rent Registry 2024.

- The RSO provisions allowing a fixed annual adjustment for these services is unique among California rent stabilization ordinances
- In tenancies of five years, the additional rent increase could be in the range of \$150 to \$240 for each service provided. This amount exceeds the total cost of the utility service.
- In other jurisdictions, the permitted amounts are based on the average amounts of the rent increases that would be required to cover the actual increases in costs of providing electricity and/or gas, rather than being a permanently fixed annual amount.
- Los Angeles’s allowance of a one percent annual increase for each of these costs is disproportionate to actual increases in the costs of master-metered electricity and gas. ***The Economic Roundtable recommends that the increases in utility costs that are passed through to renters should not exceed the average actual amount of increases in those costs rather than a permanently fixed amount and should be limited to years in which there are significant increases in these costs.***

Accessory Dwelling Units

- ADUs represent an opportunity to expand the City’s inventory of affordable housing with modest capital investments.
- The number of “legal” ADU’s has grown since 2017, with a total of 19,760 in the city.
- The consultants project that 6,123 ADUs will be produced in 2024, the City’s highest single-year total yet.
- Over 11,800 building permits have been issued for unbuilt ADUs.
- The average ADU in the City of Los Angeles is 816 square feet.
- The average valuation is \$61,000 each, or \$92 per square foot.
- Legal ADUs provide 2.1 percent of the City’s rental housing stock. ADUs alone cannot fix the City’s affordable housing shortage.
- The consultants recommend that the Planning Department completes its studies of potential modifications in the building and zoning codes that would encourage construction of more ADUs.
- It is recommended that the City consider providing economic incentives that will stimulate more ADU production.

Recommendations for Additional Data

In addition to the findings above, the Economic Roundtable submitted a number of additional recommendations for additional studies and data:

- The Los Angeles Housing Department should be provided with data from the Los Angeles Department of Water and Power on average utility costs for buildings covered by the RSO on an annual basis. The information should include average water and electricity costs for master-metered buildings.
- The Sanitation and Environment Department should provide data on average costs for solid waste collection, both for RSO buildings with four or less units and buildings with five or more units.
- The consultants also noted that about 69 percent of all RSO units are properly registered in the LAHD Rent Registry and that LAHD should have increased funding in order to enforce the registration requirement. Requests for additional positions for the Rent Registry will be submitted in the Department’s 2025-26 budget request.

POLICY OPTIONS FOR COUNCIL CONSIDERATION

In order to understand the analysis in the Study and conclusions, it is important to understand how the RSO operates in the Los Angeles rental market. While the RSO limits the maximum annual allowable rent increase that landlords are permitted to impose, landlords make economic and business decisions about how much to raise the rent each year and for which units. The RSO sets an upper maximum limit on how much a landlord may legally raise the monthly rent for each RSO rental unit. A landlord may raise the rent by any amount up to the maximum percentage, may elect to not to raise the rent for a new tenancy that is already at market rent, or may take individual tenants' personal situation into consideration. Thus, it is not accurate to assume that rents for all RSO rents are raised by the maximum allowable amount each year. Rather, landlords make these decisions on a case-by-case basis.

The Los Angeles RSO, as all jurisdictions in California, must adhere to state law (the Costa Hawkins Act) that mandates vacancy decontrol when rental units turn over, with limited exceptions. The Rent Stabilization Ordinance is not strict rent control, rather it is a rent *stabilization* law that protects tenants from excessive rent increases during their tenancies. It is not designed to and cannot ensure housing affordability. As noted on page 143 of the Study: "The RSO provides security of tenure by limiting the rent increases of a tenant after taking possession." This is true in all rent-regulated jurisdictions in California, because vacancy decontrol is mandated under state law.

In setting the methodology for setting the maximum annual allowable rent increase for RSO units, City policy makers must determine the following criteria:

1. The most appropriate CPI Index;
2. The percentage of the CPI Index on which to base the calculation;
3. The maximum percent by which rents may be increased (the "ceiling") and the minimum percent by which rents may be increased (the "floor");
4. Whether to allow an additional adjustment for landlord paid utilities and, if so, how much.

Chapter 15 of the Study provides information on the rent increase formulas for 33 rent stabilized jurisdictions plus the statewide Tenant Protections Act of 2019 (for a total of 34 jurisdictions).

The Study consultants conclude that apartment operating costs constitute only about 35 percent of rental income. However, this excludes mortgage costs as well as capital expenditures, replacement of major building systems, deposits into reserves, and debt service payments, all of which are real expenses that must be taken into account in order to calculate fair and reasonable returns on investments in rental property. These costs are partially addressed through the RSO provisions that allow an annual allowable rent increase based on 100% of the CPI and maintain a minimum percentage as the floor for the annual allowable rent increase. LAHD further notes that while leveraged investments in rental property may be attractive notwithstanding low cash returns at the outset, this could change as operating costs increase relative to income. The RSO features several cost recovery programs that provide landlords with the opportunity to offset investments in their rental properties, further discussed in the section on outreach and education.

CPI Index – The Study recommends utilizing the *All-Items Less Shelter Index* rather than the Consumer All Items index in the formula to determine the annual allowable rent increase. This would remove the redundancy of utilizing housing costs and market rents in determining future RSO rents. LAHD concurs with this recommendation.

Percentage of CPI – The current City of Los Angeles RSO sets the annual rent increase at 100% of the CPI. In 2009, the Economic Roundtable reported that: "An important finding is that the current method of determining the annual allowable rent increase utilizing the CPI is the best available economic benchmark for setting rent

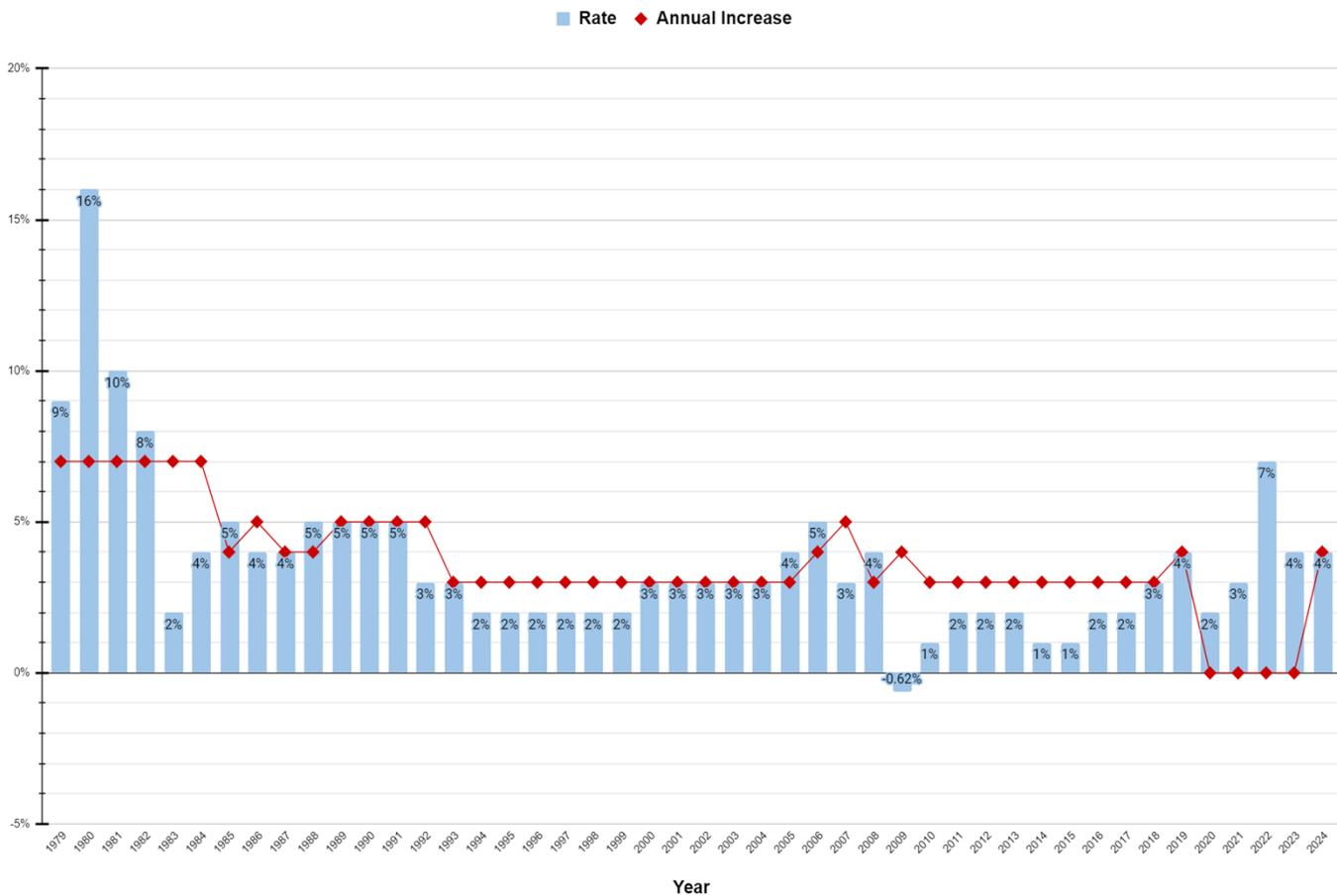
increases and the best available measure of an allowance for increases in operating costs. The CPI annual increase standard fairly balances the interests of renters and owners.” (<https://economicrt.org/publication/economic-study-of-the-rent-stabilization-ordinance-rso-and-the-los-angeles-housing-market/> C.F. No. 04-0777).

As reported on page 126 of the current Study, 15 of 33 jurisdictions (45%) allow a rent increase based on *less* than 100% of the CPI, with percentages ranging from 60% to 80% of the CPI. Fourteen (14) jurisdictions (42%) including Los Angeles calculate the annual rent increase based on 100% of the CPI, including 4 jurisdictions that allow the full CPI *plus* 5%. Four (4) jurisdictions (12%) set a fixed annual percentage of either 4% or 5%, regardless of changes in the CPI. **When jurisdictions that set a fixed percentage are included, the majority (53%) of California rent control programs, including the City of Los Angeles, employ a formula that allows annual rent increases based on 100% of the CPI except in years when the CPI is higher than 4% or 5%.** (Note: for this analysis, the city of Bell Gardens which utilizes a unique methodology is excluded.)

Ceiling and Floor – The data on the maximum ceiling and minimum floor for annual allowable rent increases is detailed on pages 126-127 of the Study. While all rent-regulated jurisdictions place a ceiling on annual allowable rent increases ranging from 3% to 10%, only 13 of 34 rent regulation programs (38%) have a minimum annual allowable rent increase (floor), ranging from 1% to 5%. For reference, the City’s current floor is 3%. The Study notes that 22 jurisdictions (65%) currently place a maximum of 3%, 4% or 5% on the percentage allowed for an annual increase for regulated rental units.

One of the major findings of the Study is that due to the 3% floor on annual allowable rent increases, the Los Angeles RSO has permitted higher increases than other jurisdictions in years when the CPI rate is under 3%. The following chart compiled by LAHD indicates the CPI index and RSO annual allowable rent increases since the adoption of the RSO in 1979:

CPI Percentage Increase Over Prior Year



Note: In the table above, the CPI increase is reflected in the annual allowable increase for the following year.

Utilities – The City’s current maximum is 8%, but if a landlord pays the full cost of gas and/or electricity, the landlord may charge an additional 1% for each utility for a maximum total annual adjustment of 10%. About 20% of RSO rental units are master-metered and, therefore, subject to the additional annual rent increase for gas and/or electricity. Chapter 16 of the Study provides an analysis of the additional allowable rent increase for utility costs. The Study notes that this provision of the RSO is unique among all of the rent regulated jurisdictions and that the cumulative effect of this allowance exceeds the actual cost of the utility service. Furthermore, Los Angeles’s allowance of a 1% annual increase for each of these costs is disproportionate to actual increases in the costs of master-metered electricity and gas. The Economic Roundtable recommended that the increases in utility costs that are passed through to renters should not exceed the average actual amount of increases in those costs.

Small Landlords – LAHD was asked to report back on the financial impact of the COVID emergency measures and whether there should be special consideration for property owners considered “mom and pop” landlords. The RSO defines small landlords as those who own four or less rental units. Chapter seven of the Study reviews the financial condition of landlords by building size and notes that landlords with four units or less make up thirty percent of the RSO inventory, the biggest share of the by building size. Key findings include:

- The average rent for units owned by small landlords is higher than the average rent for any other building size group and 20 percent higher than for the overall RSO inventory.
- Fifty-seven percent (57%) of tenants in units owned by small landlords are reported by the Census Bureau to have been in their units for five or more years, compared to only 47 percent of tenants in all RSO units,

longer occupancy than any other ownership group. Less tenant turnover reduces lost revenue from empty units, but also reduces the frequency with which rents can be vacancy decontrolled and re-rented at market rates.

- Small landlords have the lowest vacancy rate. The person-to-person relationship between tenants in small buildings and their mom-and-pop landlords appears to make tenants more inclined to stay where they are.
- Operating expenses for smaller buildings may be offset by self-management, which would reduce cash outlays for managing small buildings.
- Smaller RSO landlords appear to receive higher rent per unit and have lower vacancy rates than larger RSO landlords. The Study did not find evidence that they have greater financial stress than larger landlords.
- A disadvantage of allowing larger rent increases for small property owners is that their tenants would be subject to larger rent increases than other tenants, simply because of where they rent.

With regard to the consideration of creating a different regulation for allowable rent increases for small landlords, the Study noted that traditionally rent regulations have provided for uniform annual allowable increases for all properties covered by the regulation. “The paradigm has been that rent increases should be stabilized and exceptions to the across-the-board rule would be based on operating cost factors, service levels, and history of rent increases for the particular property, rather than the personal circumstances or purchase financing arrangements of the owner or the size of the property. In fact, in fair return cases under rent regulations, appellate courts in California and other states have ruled that differences in allowable rents based on differences in financing arrangements have no rational basis.”

The Study goes on to explain that “a flip side of the view that ‘mom-and-pops’ have been squeezed is that, apart from the freeze period, they have been the beneficiaries of the rapidly increasing rent levels prior to the freeze, and during the freeze have been able to obtain large increases in rents as units have turned over. Consequently, they have realized large increases in cash flows and benefited from large appreciation of investments that were substantially leveraged at the outset. The data from the LAHD registration database indicates that the average rents in properties with four units or less increased from \$1,502 in 2017 to \$1,876 by January 2023, an increase of 25 percent, compared to the 24.3 percent increase in the CPI.”

The Study consultants further note that “a common view has been that if mom-and-pops are not permitted higher rent increases, they will be replaced by out of town investors. An alternative view is that if higher rent increases are permitted for smaller properties - out of town investors will pay even more per unit for those properties than for larger properties and that the increased values of smaller properties, which are already approaching \$400,000 per unit for three and four unit properties, will provide even greater incentives for the mom-and-pops to sell.”

LAHD RECOMMENDATIONS

Los Angeles is a majority renter city, with the majority of tenants rent-burdened. The Study describes the continued vulnerability of renters, with 20% of Los Angeles renters in poverty and 10% paying over 90% of income for rent (page 30), as well as the findings of the GAO Study that the primary driver of evictions is the rising cost of housing (pages 48-50). The City Council may consider the following amendments to the RSO to lessen the impact of annual allowable rent increases on renters of RSO units and provide a more sustainable rate of annual rent increases for RSO tenants:

1. CPI Index - Retain the methodology to calculate the annual increase based on 100% of the Consumer Price Index (CPI), but replace the All-Items Index with the CPI All Items-Less Shelter Index, in order to remove the redundancy of including the cost of housing in the formula that sets rent increases for RSO rental units.

While it has been suggested to utilize a lesser percentage of the CPI, such as 60%, this may not account for mortgage costs, capital expenditures, replacement of major building systems, deposits into reserves, and debt service payments. It also does not factor in the impact of 4 years of zero percent annual allowable rent increases from 2020 until 2024 during which the City's COVID-19 emergency measures were in effect. During this time, landlords had to forego cumulative rent increases of 16% which would have otherwise been allowed under the RSO, as well as increased fees and operating costs discussed in Chapters 11 and 12 of the Study. Permitting 100% of the CPI also provides landlords with the cash flow and operating income to be able to afford to invest in upgrades and improvements in aging RSO properties, which by definition are more than 46 years old, with some buildings built 100 years ago. The City must promote landlords' ability to maintain and upgrade rental properties in order to prevent the disastrous deterioration in the quality of the rental housing stock recently demonstrated in several portfolios of the City's aging housing inventory.

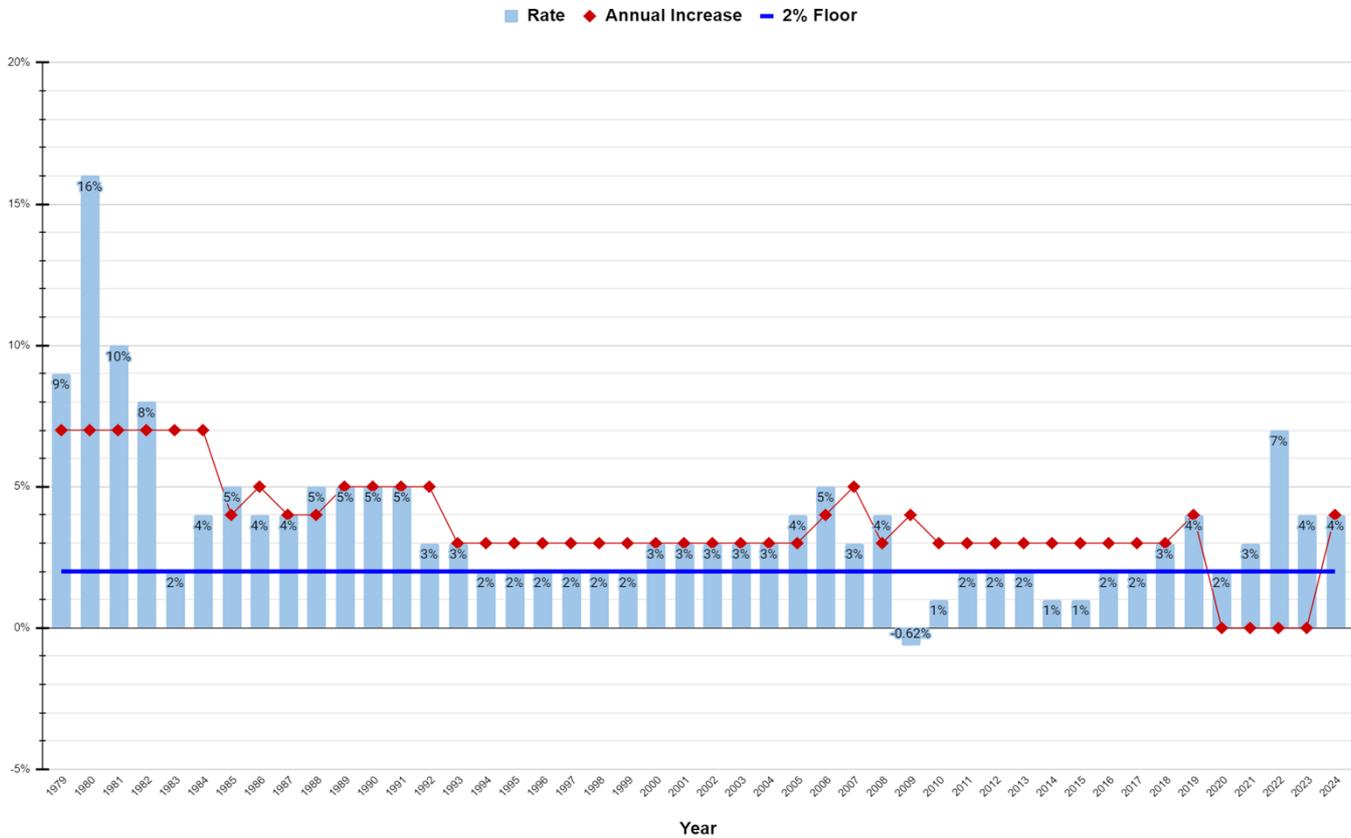
Chapter 12 of the Study notes that operating expenses have outpaced increases in the CPI. Owners of RSO units were subject to the financial impacts of the pandemic rent freeze and escalating operating costs, including trash-hauling fees, water rates, electricity, insurance, property taxes, labor and material costs. These increases are normally partially offset by the annual allowable RSO rent adjustment, as well as by higher rents upon turnover (vacancy decontrol). Owners of RSO units need sufficient income to reinvest in their rental properties and prevent the deterioration of the aging RSO housing stock with old infrastructure and building systems that require upkeep.

2. RSO Ceiling - Revise the maximum annual allowable rent increase to 5%, in line with the majority (65%) of rent regulated jurisdictions in California. In order to allow landlords to keep up with inflation and invest in their rental properties in future years, the 5% annual cap should be adopted with a provision to allow "banking" of CPI rates higher than 5% to future years, while maintaining the 5% cap every year. LAHD must track and publish the allowable rate every year.
3. RSO Floor - Modify the floor for the annual RSO rent increase to 2%, rather than the current 3%. As illustrated in the next chart, a 2% floor would conform with the CPI for all but 4 years (91%) of the 46-year history of the RSO from 1979 – 2024. LAHD made a similar recommendation in 2009 at the time of consideration of the last major Study of the RSO; however, the recommendation was not adopted at that time.

Substitution of the CPI All Items-Less Shelter Index for the All-Items Index, as recommended in this report, and utilizing a 2% floor still results in an annual rent increase reflecting the actual change in the CPI in the vast majority of years - 76% (35 of 46 years).

In the outlier years when inflation is less than 2%, the 2% floor is a useful tool to provide landlords with long-term RSO tenants with stability in their financial return from their investment in rental properties and allow for sufficient income to cover City-mandated fees and rising operating costs. In addition, a 2% floor may permit landlords with long-term tenants to gradually recover from limits on any rent increases for long-term tenants imposed during the pandemic years (2020-2023), when they were required to forego 16% rent increases per the existing RSO provisions. The following table illustrates the effect adoption of a 2% floor for the annual allowable rent increase.

CPI Percentage Increase Over Prior Year



Note: In the table above, the CPI increase is reflected in the annual allowable increase for the following year.

4. Allowable Rent Increase for Utilities - As discussed in Chapter 16 of the Study, Los Angeles is the only jurisdiction that permits an allowance of an additional 1% - 2% for gas and electricity. In the case of long-term tenancies, the additional rent increase exceeds the total cost of the utility service. LAHD additionally notes that the cost of increased utility costs is already built into the 100% of the CPI which is the basis of the annual allowable rent increase. Therefore, allowing an additional 1% - 2% “double counts” those increased operating costs for utilities. LAHD recommends that the City Council repeal the provision that permits an additional 1% - 2% increase for gas and electricity.

Outreach and Education on the Just and Reasonable and RSO Cost Recovery Programs

In the findings on small landlords, the Study authors note that “in the context of vacancy decontrols, the annual general adjustment standard does not have a significant impact on ownership patterns of smaller properties” and recommend that if higher rent increases are allowed for smaller properties, other conditions should be attached relating to the overall income of the property compared to prior years and that a standard of this type should be as objective and easy as possible for applicants to document for applications purposes.

The RSO allows landlords to apply for “Just and Reasonable” rent increases (LAMC 151.07.B), based on landlords’ operating income and expenses including property taxes, operating and maintenance costs, capital improvements, and other factors, in comparison to increases in the CPI. This program is particularly useful for landlords with historically low rents. However, that program is not often accessed by landlords. LAHD will work with the Rent Adjustment Commission to update the existing regulations for this program and develop an education and outreach plan, with a focus on small landlords in order to promote awareness and utilization of this

program, which can serve as a safeguard for “mom and pop” and other landlords who are not able to obtain sufficient revenue from their rental units to maintain their operating income in line with the CPI. LAHD will expand outreach and education on the Just and Reasonable program as well as other existing programs that allow landlords to partially recover costs of upgrades to their rental properties including:

- Capital Improvement
- Seismic Retrofit
- Primary Renovation
- Rehabilitation

The table below compares the current provisions and the proposed amendments to the RSO annual allowable rent increase formula.

RSO ANNUAL ALLOWABLE RENT INCREASE FORMULA		
COMPARISON CURRENT RSO PROVISIONS – PROPOSED AMENDMENTS		
Formula Indicators	Current RSO Provisions	Proposed RSO Provisions
CPI Index	Consumer All-Items	Consumer All-Items Less Shelter
% CPI Allowed	100%	100%
Ceiling	8% - 10%	5%
Floor	3%	2%
Rent Banking	“Use It, or Lose It”	Allowed per LAHD Authorization/Publication
Utilities	+ 1% - 2%	0
FY 2025-26 Projected %	3%	2%

CONCLUSION

The RSO statement of purpose states that “it is necessary and reasonable to regulate rents, so as to safeguard tenants from excessive rent increases, while at the same time providing landlords with just and reasonable returns from their rental units.” RSO rental units house the majority of City residents. The recommendations presented above build on the Study findings and recommendations, and represent a careful balance of protecting tenants from destabilizing rent increases while providing landlords with a fair return on their investment in order to

prevent deterioration of the City's valuable RSO housing stock and incentivize landlords' to upgrade and improve their rental properties, in order to preserve safe and decent rental units for the majority of City residents.

FISCAL IMPACT

There is no fiscal impact to the General Fund resulting from the recommendations included in this report.

Approved By:



TRICIA KEANE
Interim General Manager
Los Angeles Housing Department

ATTACHMENT:

Equitable Rent Rent Stabilization Standards in the City of Los Angeles September 2024



Equitable Rent

Rent Stabilization Standards in the City of Los Angeles

September 2024



ECONOMIC
ROUNDTABLE

Knowledge for the Greater Good

Equitable Rent

Rent Stabilization Standards in the City of Los Angeles

September 2024

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Underwritten by the
City of Los Angeles Housing Department

Report available at: www.economicrt.org

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1. Executive Summary

*Photo credit:
Economic Roundtable*

The Context for Rent Regulation

About one million of Los Angeles' 1.5 million households rent their homes. About 650,000 of those homes are in units covered by the rent-stabilization ordinance (RSO), which is applicable to units constructed before 1979.

Rent increases for units covered by the RSO occur in two ways. First, when a new tenant moves in, rents may be set at market levels because there is no ceiling on the initial rent for a new tenant. During a tenancy, rents may be increased by the permitted annual across-the-board increases.

About half of RSO units turnover within a four-year period, so market-rate rents for new tenants are a central determinant of allowable rent levels and increases in the rent of RSO units. The average rent of tenants who move into RSO units in 2024 is about 50 percent above the average in 2017.

In the decade before the pandemic freeze on annual rent increases, from 2010 to 2020, the annual allowable RSO rent increases totaled 36 percent. This far exceeded the 21 percent increase in the Consumer Price Index (CPI). Within the last half of the decade, from 2015 to 2020, the annual allowable rent increases totaled 17 percent, compared with a 13 percent increase in the CPI.

The move-in year is the central determinant of the allowable rent for RSO units. Long-term tenants have substantially lower rents. The savings are minimal for tenants who stay in their units for only a few years.

Rent Savings for RSO Tenants

Citywide, the average rent for non-RSO units is 25 percent higher than for RSO units. This is based on comparing all RSO units with all non-RSO units without accounting for the size of units. However, non-RSO units, which are those built after October 1, 1978, are typically larger than RSO units.

Based on a comparison of the rent for RSO and non-RSO units taking into account both the number of bedrooms and the total number of rooms as benchmarks, the average rent paid by RSO renters is 19 percent less than the rent paid by non-RSO renters for units of comparable size.

Returns from Rental Properties

There has been substantial growth in the net operating income of rental units covered by the RSO. Although operating expenses have increased at greater rates than the Consumer Price Index (CPI), net operating income has grown more rapidly than the CPI.

The average market value of rental properties subject to the RSO has doubled over the last ten years, from about \$150,000 to \$300,000 per unit. The average market value is nearly five times greater than in 2000. The increase in the values over the past decades is an outcome of the combination of increasing net operating income levels and declining mortgage interest rates (which in turn have led to a decline in capitalization rates.)

The standard expectation of investors in apartment properties is that the cash flow and the value of the property will increase during the period of ownership, as rents and net operating income increase, and mortgage payments take up a declining portion of net operating income. This expectation and the leveraged nature of investments in rental property make investments in rental properties attractive, notwithstanding low cash flows at the outset.

Seventy-four percent of the *units* under the RSO were purchased before 2015. Thirty-eight percent were purchased before 2000. The length of ownership is virtually the same for all sizes of RSO properties.

Financial Stress of RSO Landlords by Building Size

Properties with two to four units account for 30 percent of all RSO *units*. The owners of these properties are often called “mom-and-pop landlords.”

Rental units in two to four unit buildings typically have more bedrooms than all other size classes of RSO ownership. They provide an average of 46 percent more bedroom space than the overall average for the RSO inventory.

When rents are compared based on *units*, the average rent for two to four unit buildings is 20 percent higher than for the overall RSO inventory. However, when rents are compared on the basis of rent per *bedroom*, the rents in these buildings are 16 percent less than the overall average for RSO units.

RSO landlords have slightly less tenant turnover than non-RSO landlords, which reduces lost rent when units are vacant as well as costs to refurbish units for new tenants. However, it also reduces the frequency with which rents may be reset to market rates because of vacancies.

Smaller RSO landlords appear to receive higher rent per unit, although lower rent per bedroom, and have lower vacancy rates than larger RSO landlords. There is not clear evidence that they have greater financial stress than larger landlords.

A disadvantage of allowing larger rent increases for small properties is that tenants in those properties, regardless of whether their rents were above or below the average, would experience larger rent increases than the balance

of the tenant population. Thirty percent of RSO units are on properties with two to four units.

RSO and Non-RSO Renters Compared

RSO renters differ from non-RSO renters in that they are more frequently single adults or over-crowded. The average income of non-RSO households is 22 percent higher than RSO households. However, both groups of renters have similar levels of rent burden because the average rent for non-RSO units is higher.

Vulnerable Renters

One-fifth of Los Angeles renters have incomes below the federal poverty threshold. Census Bureau data shows that more than half of them spend over 90 percent of their household income for rent. These vulnerable renters live in both RSO and non-RSO units.

Vulnerable renters are more likely to be under 35 years old, live alone, be unemployed, have annual incomes below \$20,000, and receive public benefits. The presence of a disability makes the household more likely to be vulnerable, as does being a single parent, having limited English ability, or being African American.

Rent Increases and Homelessness

The most frequent explanation that homeless adults in Los Angeles give for their lack of housing is unemployment and lack of money. There is a direct connection between loss of income and loss of shelter, but these losses do not occur simultaneously. Disconnection from work is a degenerative dynamic - less work, less earnings, less stable living conditions, and further disconnection from work.

Increases in income inequality lead to increases in homelessness because they simultaneously drive up the cost of housing and the percent of low-income renters who cannot afford housing.

There is a high rate of homelessness in Los Angeles primarily because of this interaction between the housing market and the labor market—namely, the high cost of housing and the high rate of working poverty.

An increase in evictions is a driver of an increase in homelessness. The primary driver of evictions is the rising cost of housing. The eviction moratorium, rental assistance and fiscal stimulus programs were successful in preventing the rise of homelessness from being as severe as it otherwise would have been.

Impact of the Covid Pandemic on Landlords

Landlords experienced a sharp increase in non-payment of rent during the Covid pandemic, which they addressed by granting more rent extensions, charging less late fees, deferring maintenance, and listing their properties for sale. During this period, their right to evict tenants for non-payment of rent was substantially curtailed.

Landlords nationwide were least likely to offer adjustments to renters of color for the same level of non-payment of rent.

Rental assistance programs throughout the U.S. were significantly helpful to tenants and, in turn, their landlords, but they did not reach as many tenants as administrators often hoped due to strong resistance from some landlords. However, in Los Angeles, rental assistance was paid directly to tenants whose landlords declined to participate.

In Los Angeles and Orange Counties, rental non-payment has been declining from 2020 to the end of 2023.

Census surveys indicate that approximately 13 percent of renter households in Los Angeles and Orange Counties are currently behind on rent, with an average of 3.1 months of rent unpaid by those households.

Accessory Dwelling Units (ADUs)

ADUs are an opportunity to expand the City's inventory of rental housing with modest capital investments.

We recommend that the Planning Department complete its studies of potential building and zoning code changes that would encourage construction of more ADUs, and that the City consider providing economic incentives, rather than just code changes, to support ADU production.

Fees could be waived or the ADUs could be exempted from parking requirements when homeowners agree to limits on rents or rent increases, or offer their units only to low-income tenants. Additionally, the permitting process could be streamlined to reduce the time, uncertainty, and expense that deter homeowners from applying for approval.

Market-Rate Rents, Restricted Rents, and Inflation

From 2000 to 2023, the Los Angeles region had a higher rate of inflation than the rest of the United States. This was due entirely to increases in housing costs. For all consumer goods other than housing, the Los Angeles region actually became slightly more affordable than the rest of the country.

Los Angeles rents decreased significantly in the early months of the pandemic, erasing the outsized gains they had made relative to the rest of the country. From 2020 to 2023, rents grew more slowly in Los Angeles than in the rest of the United States.

From 2015 to 2024, asking rents grew faster for properties under the Rent Stabilization Ordinance (RSO) than for non-RSO properties (24 percent, compared to 16 percent), likely reflecting strong demand for protection against high rent hikes in an increasingly expensive housing market.

Operating Expenses for Low-Income Housing

The largest expenses and losses for most Los Angeles landlords are capital expenditures, followed by vacancies, salaries and personnel, property taxes, and contract services.

Operating expenses for low-income housing outpaced inflation in the Western region of the United States from 2010 to 2022, increasing 67 percent compared to a 38 percent increase in the Consumer Price Index.

Until 2019, RSO rents mostly kept pace with operating expenses, but have lagged inflation since the onset of the Covid pandemic.

Increases in Apartment Operating Costs

In Los Angeles, operating expenses for apartments average about 35 percent of rental income. The balance of rental income after subtracting operating expenses - net operating income - is the return on the investment in the property, which is available to cover debt service and provide cash flow to owners.

Insurance costs, which formerly amounted to only about two or three percent of the rents, may have doubled within the past few years and are increasing in a steep upward trajectory.

Assuming an average monthly rent of \$1,600 (the exact average for all RSO units is \$1,629), and an average operating expense ratio of 35 percent, monthly operating costs per rental unit average \$560.

Rent Increases for Landlords Who Pay for Gas and/or Electricity

Under the RSO, apartment owners who cover either gas or electricity costs are permitted additional annual rent increases of one percent for each of these services.

In about 20 percent of all RSO units, the rent covers one or both of these services. A two percent annual increase is permitted for about eight percent of units based on the provision of both services. A one percent annual

increase is permitted for 11 percent of units where the landlord pays for gas, but not electricity. Similarly, a one percent annual increase is permitted for 1.4 percent of units where the landlord pays for electricity but not gas.

The approach under the RSO of permitting a ***fixed-amount annual increase*** for these services is unique among California rent stabilization ordinances.

The allowance of a one percent annual increase – typically \$15 per unit per month or more – for each of these costs is disproportionate to actual increases in the cost of master-metered electricity and gas. Typically, each of these services has an overall cost of \$100 per unit per month or less. The passthrough standard incorporates an assumption that the cost of the services is increasing at the rate of 15 percent per year.

In the case of a five-year tenancy, the additional rent increase could be in the range of \$75 to \$120 for each service provided. This amount exceeds the total cost of the utility service.

Under other rent stabilization ordinances that have provided apartment owners with extra rent increases to cover increases in utility costs, the permitted amounts have been: 1) based on the average amounts of the rent increases that would be required to cover the actual increases in costs of the utilities rather than being a permanently fixed annual amount, and 2) limited to years in which there were significant increases in these costs.

The Economic Roundtable recommends that Los Angeles adopt a similar policy, accompanied by a requirement that LADWP provide data on average electricity costs for master-metered properties covered by the RSO.

Allowable Annual Rent Adjustments in Other California Cities

Rent stabilization ordinances are currently in effect in 33 California jurisdictions.

In the 1980's, rent legislation was adopted by Los Angeles, San Francisco, Oakland, San Jose, Santa Monica, Berkeley, West Hollywood, and a few other cities.

Within the last eight years, the tightening of the rental market has led to the adoption of local rent legislation in fifteen other jurisdictions. These include Los Angeles County unincorporated areas, Culver City, Inglewood, and Pasadena. It has also led to the adoption of a statewide ceiling on increases in apartment rents for all units that are over 15-years old and not already regulated by local ordinances. Eight of those local ordinances were adopted between 2020 and 2022.

Of the 33 ordinances now in effect, most tie annual allowable rent increases to all or a portion of the percentage increase in the CPI.

Thirteen of the 33 ordinances limit the annual rent increase to less than 100 percent of the percent increase in the CPI.

Twenty of the 29 ordinances that include a CPI standard also place a ceiling of either three, four, or five percent on the allowable increase based on the CPI standard.

Under the annual increase standard in the City of Los Angeles RSO in effect prior to the pandemic, the allowable annual increases were greater than those that are now permitted under a majority of the ordinances.

During the past decade, when the CPI increased by only one or two percent a year, the three percent floor on the annual allowable rent increase was greater than the increase in the CPI.

Consequently, the outcome of the RSO annual increase standard in effect before the pandemic was to compound move-in rents set at market levels under shortage conditions with annual rent increases for tenants after they moved in that exceeded the increase in the CPI in years with low inflation.

RSO Rent Protection

The RSO provides secure tenure by limiting rent increases after a tenant taking possession. However, because the initial rent is not regulated, the RSO does not preserve the affordability of housing, except for long-term tenants. Only 53 percent of RSO tenants have been in their units for five or more years.

The Annual Increase Standard

Under the RSO and most other California rent ordinances, the annual allowable rent increase is tied to the *Consumer Price Index All-Items for All Urban Consumers (CPI-U)* for the local region. The Bureau of Labor Statistics (BLS) publishes this data monthly. The index is based on increases in the cost of a market basket of goods purchased by an average household, which differ substantially from the basket of costs associated with operating an apartment building.

About one-third of the weight in the *All-Items Index* is based on increases in rents. Therefore, in years when increases in rents exceed increases in other costs, the *All-Items Index* incorporates the impact of housing shortages that led to the adoption of the RSO.

The BLS also publishes an *All-Items Less Shelter Index*, which does not incorporate rents in its weighted index. In recent years, increases in the *All*

Items Index have exceeded the increases in the *All-Items Less Shelter Index*. We recommend that Los Angeles use the *All-Items Less Shelter Index* in order to avoid the “circularity” associated with the use of the *All-Items Index*.

One purpose of the annual allowable rent increase is to offset increases in apartment operating costs. Another purpose is to allow growth in net operating income, which is available to cover debt service and provide cash flow. An annual increase in the range of 35 percent of the CPI increase would cover those cost increases in years in which operating costs increase at the same rate as the CPI, but would not allow for any growth in net operating income. In fact, operating expenses have been increasing at a greater rate than the CPI.

While ordinances commonly set a ceiling on allowable annual rent increases, an alternative to a fixed ceiling is a descending percentage of CPI increases above a specified amount, (e.g., 100 percent of the CPI increase up to x percent, 50 percent of the CPI increase above y percent). This type of standard takes into account the impact of large rent increases on tenants.

Compliance Issues

Currently, about 69 percent of all RSO units are properly registered in the RSO Rent Registry, leaving 31 percent with unknown rent amounts and dates of last tenant move-in.

This requirement is important because lack of full compliance raises the possibility that there are systematic differences between properly registered units, which provided much of the statistical basis for the analysis in this report, and policy considerations based on this analysis, and units that are not properly registered.

Information about the actual amount of increases in utility costs of apartment owners is essential to inform the public and City Council about the impact of these increases relative to rental income. Repeated efforts by the Economic Roundtable to obtain information from the Los Angeles Department of Water and Power (LADWP) about increases in utility costs were fruitless apart obtaining data on average water costs for apartment buildings.

Reliable data for buildings covered by the RSO on average costs of water, sewer, and master-metered electricity for all size properties, and refuse collection costs for buildings with less than five units, can be compiled from LADWP billing data. Refuse collection cost data for buildings with more than five units can be compiled from data that refuse collection franchisees provide to the Department of Sanitation and Environment.



2. Los Angeles Housing Inventory

*Photo credit:
Economic Roundtable*

Housing Inventory

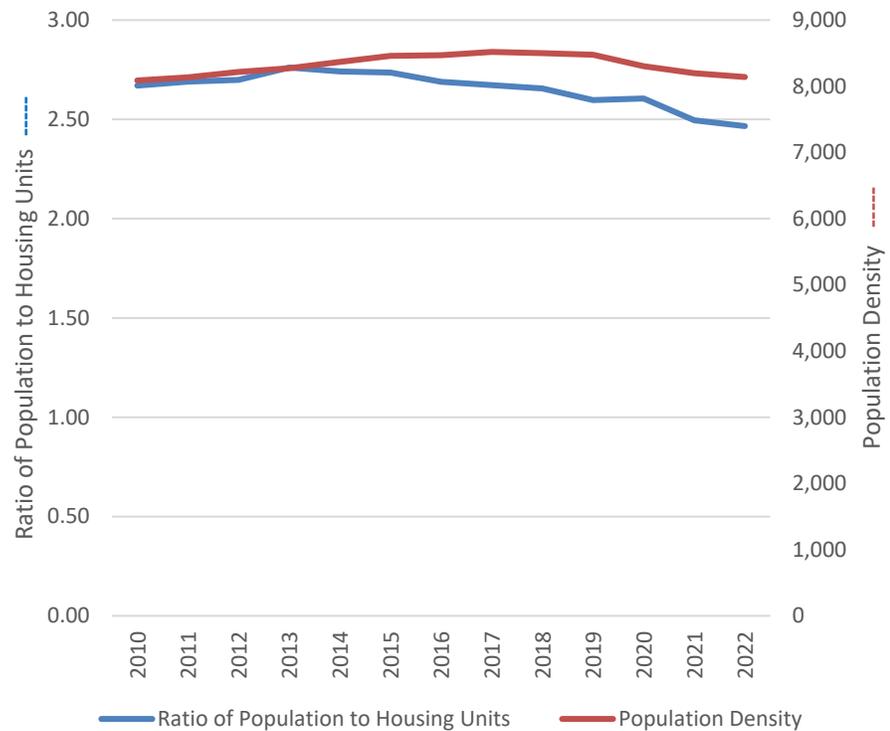
Housing Units and Population

The City of Los Angeles has an estimated 1,549,889 total housing units for a total population of 3,822,224 residents, or about 2.47 residents per unit.¹ The City remains the second largest in the nation, and the largest city in California by a wide margin.²

Los Angeles' highest ratio of 2.76 residents per housing unit occurred in 2013, while its population density peaked in 2017 at just over 8,500 residents per square mile (Figure 1). Both ratios have declined slightly in recent years, with the estimated total population of the City dropping after a 2017 high of 4 million residents.

The number of residents per housing unit has decreased slightly, due to steady private-sector production of more housing, and city government planning policies encouraging in-fill development at greater densities – especially along transit corridors.³ This progress is modest in the face of the ongoing City and regional shortage of affordable housing, reflected in high rents, overcrowding, and housing instability.

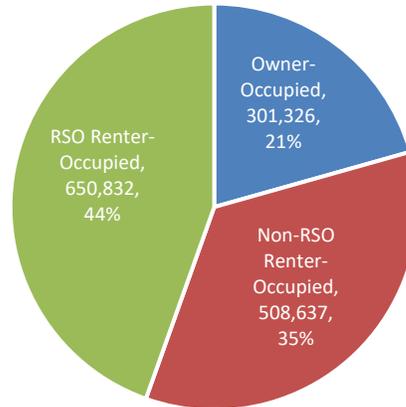
Figure 1: Population Density and Ratio of Total Population to Housing Units, City of Los Angeles



Source: Economic Roundtable analysis; U.S. Census Bureau. Decennial Census of Population and Housing, P1 Total Population, and H1 Total Housing; U.S. Census Bureau. American Community Survey 1-year Estimates Detailed Tables, S0201: Selected Population Profile in the United States, and B25001: Housing Units. Density calculated based on the fixed city land area of 469.49 square miles.

Among the City’s housing units, 21 percent are occupied by the owners, while the majority are rented housing units – 79 percent (*Figure 2*). A plurality of the City’s housing units (44 percent), are rent-stabilized units under the jurisdiction of the City’s Rent Stabilization Ordinance (RSO), generally covering rental properties built on or before October 1, 1978.⁴ Over a third (35 percent) are market-rate rental units built after that date.

Figure 2: Housing Unit Inventory

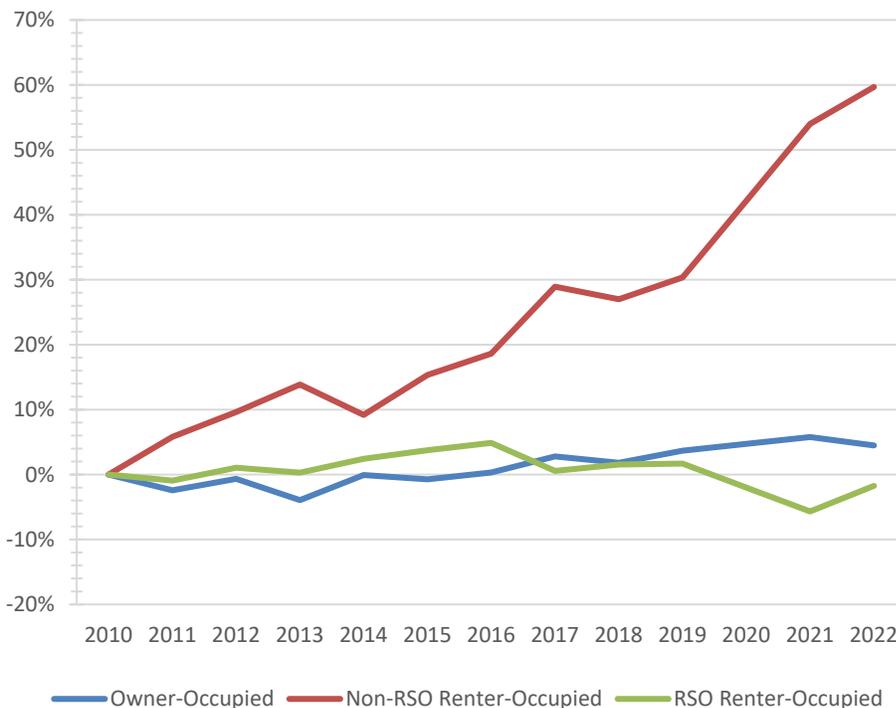


Source: Economic Roundtable analysis; LAHD. 2024. Dataset A: RSO Inventory, Dataset B: RSO Exemptions; Los Angeles County Assessor. 2024. SBF Abstract (DS04). Condominium units are included.

The City of Los Angeles

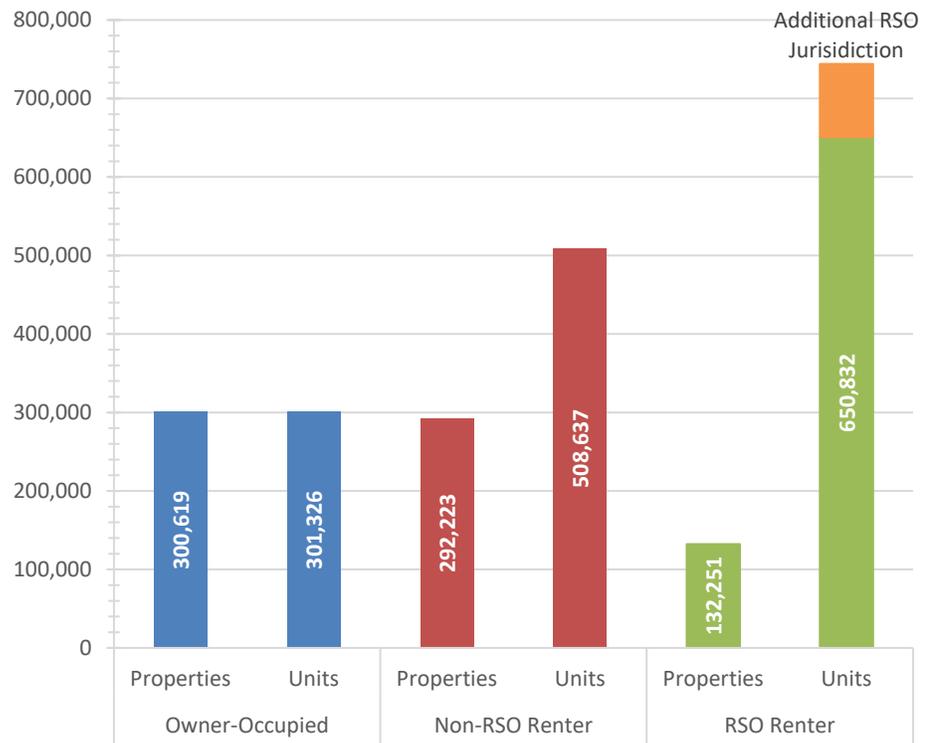
Housing Department oversees more than 650,000 total RSO units,⁵ with some of those rental units being exempt⁶ or vacant.⁷ While the number of RSO properties is effectively capped since October 1, 1978, and owner-occupied housing has held steady, market-rate rental housing units (non-RSO) have been growing. Since 2010 alone, this latter housing segment has increased by 60 percent in the City (*Figure 3*).

Figure 3: Housing Inventory Change by Tenure and RSO Status, City of Los Angeles



Source: Economic Roundtable analysis; US Census. American Community Survey, 1-Year Estimates: B25036: Tenure by Year Structure Built, 2010-2022. Universe: Occupied Housing Units. Notes: Excludes vacant units; RSO estimate includes up through 1979; Due to COVID data limitations in 2020, that year is an average of 2019 and 2021 due to COVID data limitations. Percentages are sample-based estimates, less accurate than record counts in Figures 2 and 4.

Figure 4: Housing Inventory by Tenure, RSO Status and Exemptions in 2024, Current Properties and Units, City of Los Angeles



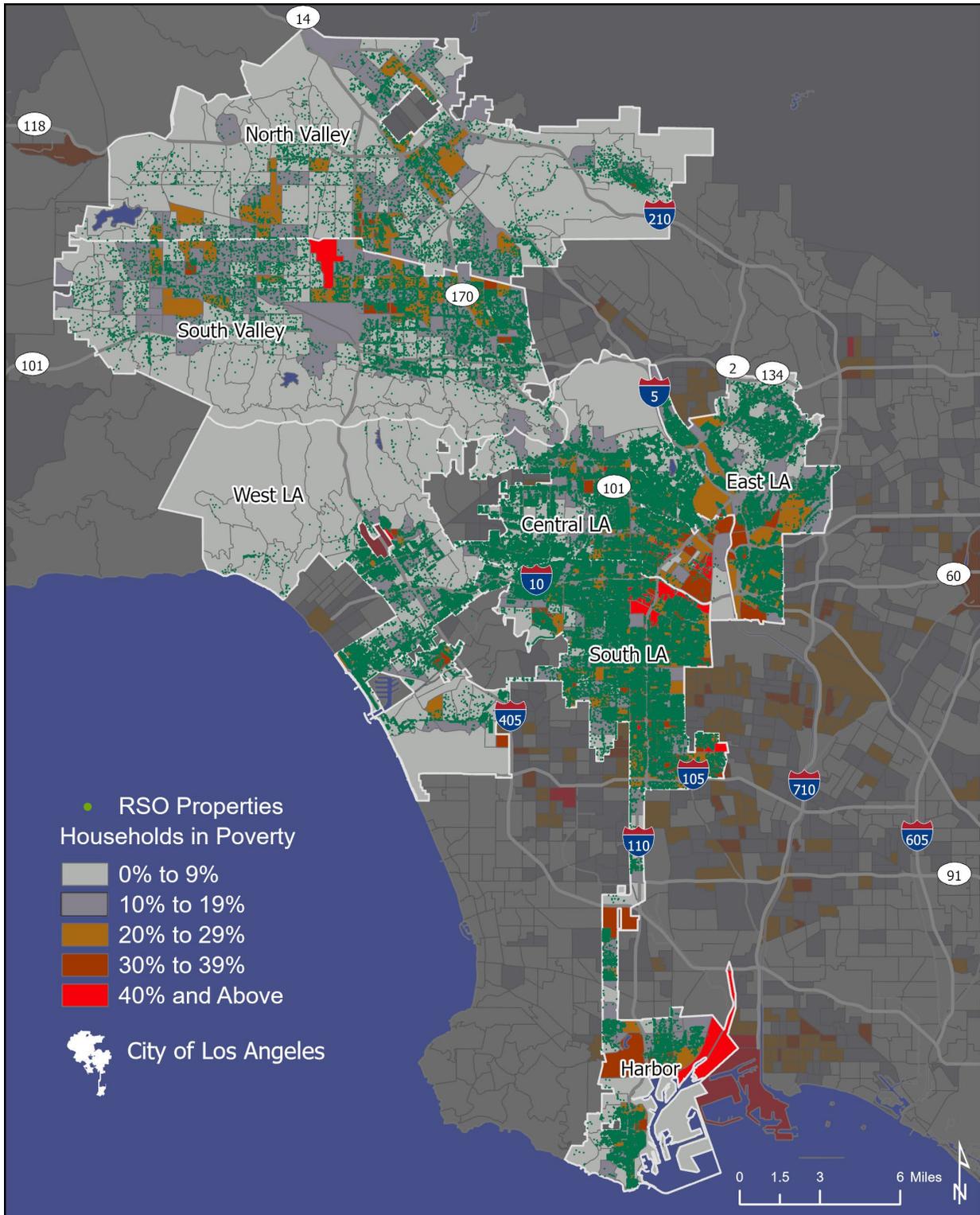
Source: Economic Roundtable analysis; Los Angeles Housing Department. 2024. Dataset A: RSO Inventory; Report Dashboard for RSO – LAHD; Los Angeles County Assessor. 2024. SBF Abstract (DS04). Note: The higher non-RSO renter-occupied housing unit count (red) and lower owner-occupied housing unit count (blue) are corrections of U.S. Census estimates, based upon County Assessor’s homeowner exemptions and City Housing Department RSO property owner exemptions. Condominium units are included.

The current citywide inventory of all housing properties and units, inclusive of RSO status, tenure,⁸ and exemptions is shown in *Figure 4*. Several factors determine whether units are regulated by the RSO. Single-family homes can be occupied by their owners or rented to others, and RSO units in apartment buildings and condos can be occupied by the building owner, their family members, or paid building managers. Based on analysis of City of Los Angeles Housing Department and Los Angeles County Assessor’s office records, we calculate that Citywide there are:

- Just over 300,000 *owner-occupied* housing units, principally single-family homes but also condominiums with homeowner exemptions, plus RSO units with owner exemptions.⁹
- Just over 508,000 non-RSO renter-occupied housing units, including those in multi-family buildings constructed after October 1, 1978 (including condos), plus those on single-family properties with no home owner exemptions.
- Over 650,800 RSO rental units in multi-family buildings built before October 1, 1978, including rented condos. The orange segment in *Figure 4* is an additional 93,000 units under RSO jurisdiction, but currently not rented or exempt.¹⁰

The location of RSO units is shown against a color backdrop that indicates the percent of households that are in poverty in *Figure 5*.

Figure 5: Location of Rental Housing Properties Under the Rent Stabilization Ordinance (RSO)



Source: Economic Roundtable analysis; Los Angeles Housing Department. 2024. Dataset A: RSO Inventory; Report Dashboard for RSO – LAHD. Note: Dots on the map show the location of each rental housing property under jurisdiction of the RSO. All RSO properties, whether five or 50 units, are the same size on the map, and adjacent RSO properties blur together due to the citywide scale of the map.

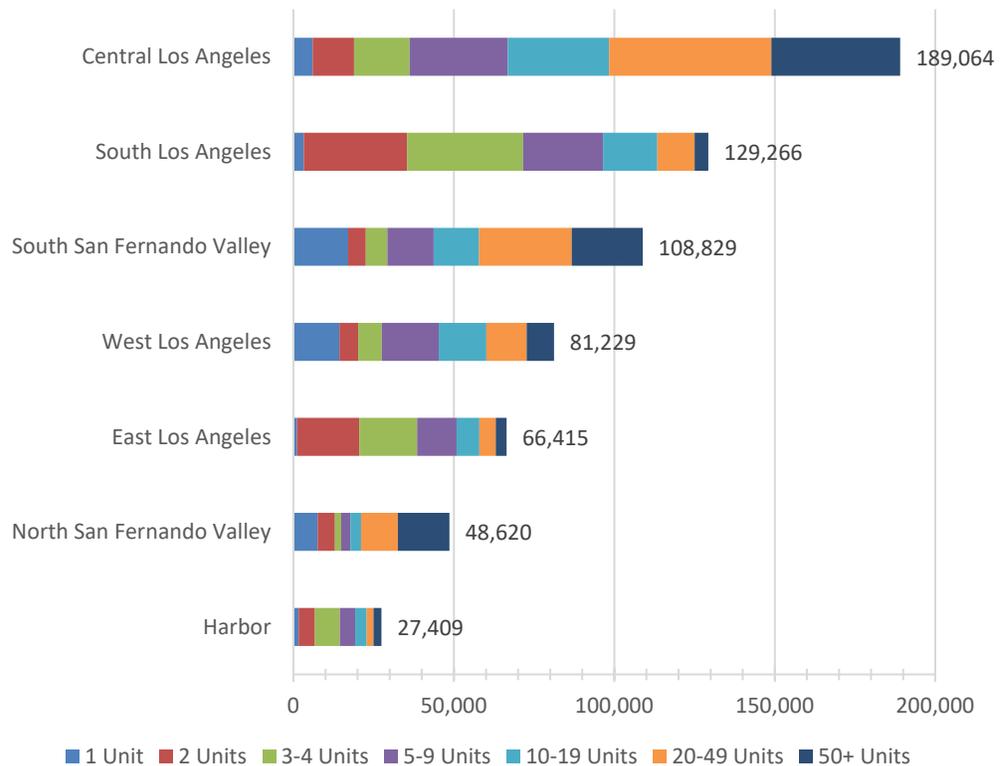
South Los Angeles has the greatest number of RSO *properties* (as opposed to *units*), followed by the South San Fernando Valley and Central Los Angeles. The Harbor has the fewest RSO properties, while the North San Fernando Valley has the next fewest (See Appendix Table 31).

Central Los Angeles, South Los Angeles and the South San Fernando Valley have the greatest number of RSO *units*, respectively, while the Harbor and North San Fernando Valley have the fewest. It is noteworthy that while South Los Angeles has the second greatest number of RSO units, more of them are on parcels with four or fewer units than in any other planning district (See Appendix Table 32).

Among the City of Los Angeles’ planning districts with greatest numbers of RSO properties and units, there are striking differences in the composition of their housing stock by building size, as shown in Figure 6.

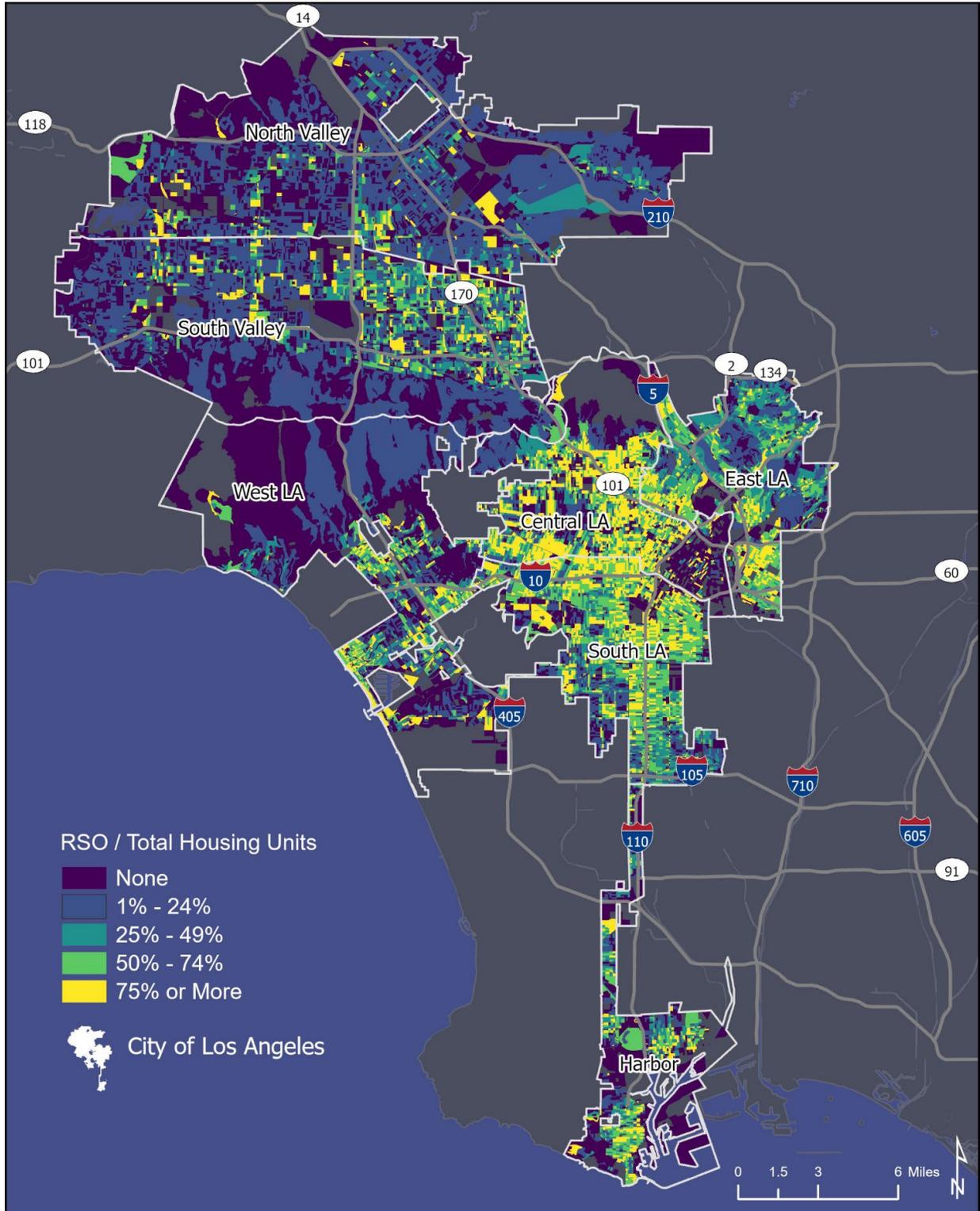
Central Los Angeles is the planning district where the most RSO units are located – just under 190,000. Almost half are in large apartment building properties of 20 or more units each. In contrast, over half of RSO units located in South Los Angeles are found in duplex, triplex or fourplex buildings. Another notable trend is the prevalence of “single-unit” RSO properties in the San Fernando Valley and West Los Angeles, where there are a significant number of multi-family condominium buildings where individual units that fall under the jurisdiction of the ordinance.¹¹

Figure 6: Percent of RSO Units by Building Size and Planning District



Source: Economic Roundtable analysis; Los Angeles Housing Department, 2024. Dataset A: RSO Inventory; Report Dashboard for RSO – LAHD. Link: <https://housing2.lacity.org/rso> Note: Districts are sorted descending by largest number of RSO units.

Figure 7: RSO Units as a Share of All Housing Units per Block, City of Los Angeles



Source: Economic Roundtable analysis; Los Angeles Housing Department. 2024. Dataset A: RSO Inventory; Report Dashboard for RSO – LAHD; U.S. Census Bureau. 2020. Decennial Census of Population and Housing, PL94-171 Redistricting Summary File Table H1 (variable H0010001 Total Housing Units). Note: This map uses a straight ratio of LAHD RSO units per block, divided by US Census total housing units per block.

RSO Inventory

RSO Housing as a Share of All Housing

The RSO share of housing units in each block is illustrated in *Figure 7*, showing how rent-stabilized units make up half to three-quarters of all housing in many neighborhoods.

The preponderance of RSO-dominant neighborhoods are located in the Los Angeles basin, which includes most of the Central and South Los Angeles planning districts. There are additional concentrations in East Los Angeles, San Pedro, Wilmington, the Southeast San Fernando Valley, Palms, Venice, Westwood, and other pockets.

Hillside communities tend to have a very low share, or no, RSO housing among their housing stock.

Age of RSO Inventory: Properties and Units

Half of RSO *properties* were constructed before 1950, while another 29 percent were built from 1950 to 1970. Twenty percent were built in the 1970s, and a small fraction have more recent construction dates (*Figure 8*, and *Appendix Table 33*).¹²

As for the construction date of RSO *units* across the City, 43 percent were constructed before 1950, another 42 percent were built from 1950 to 1970, and the balance of units – 16 percent – were built since 1970 (*Figure 9* and *Appendix Table 34*).

Figure 8: Percent of RSO Properties by Decade Built

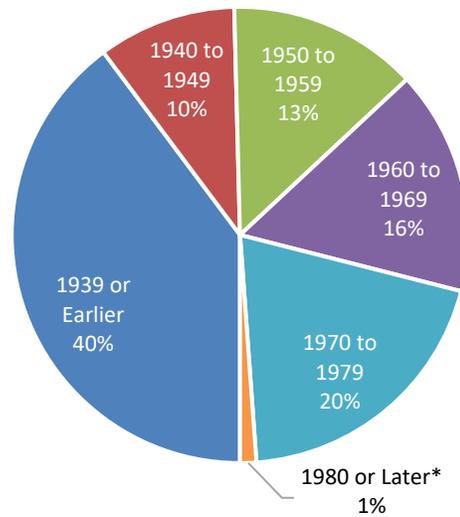
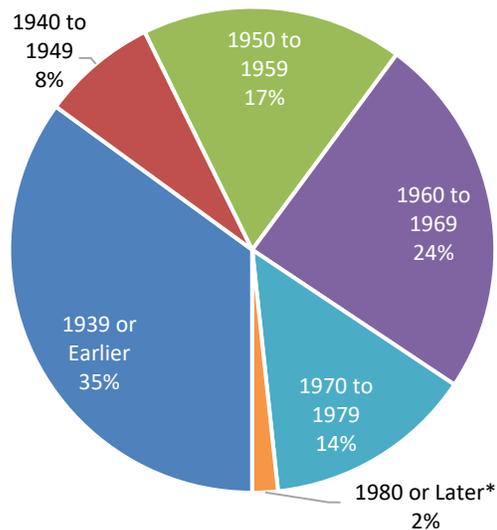
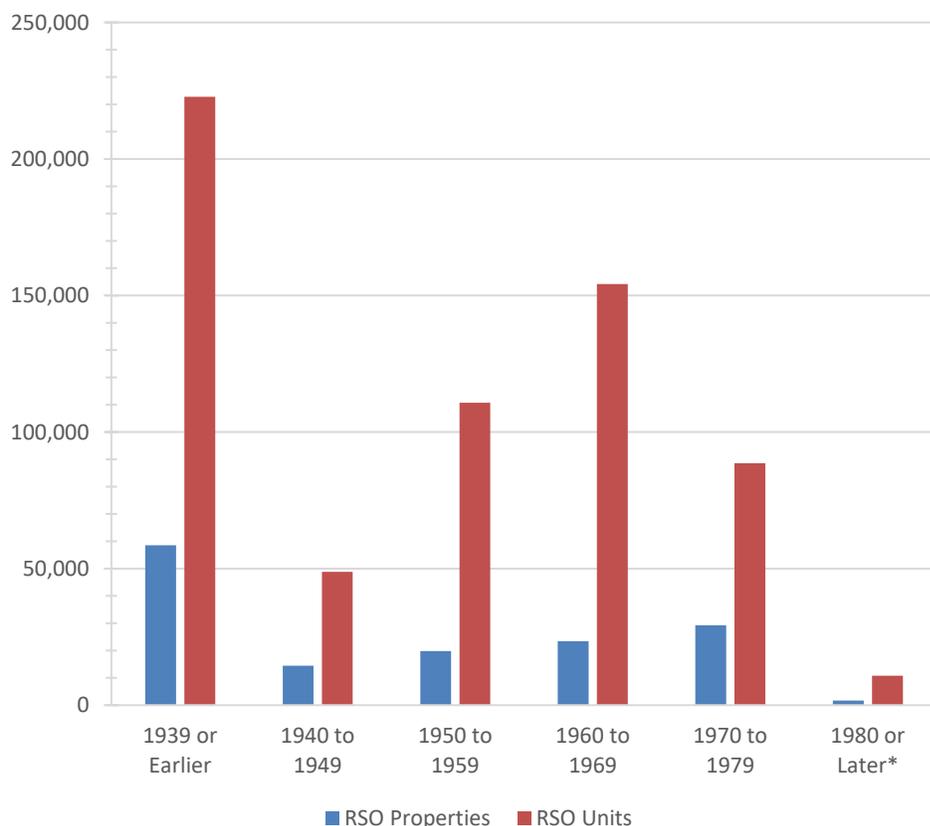


Figure 9: Percent of RSO Units by Decade Built



Source: Economic Roundtable analysis; Los Angeles Housing Department. 2024. Dataset A: RSO Inventory; Los Angeles County Assessor. 2023. SBF Abstract (DS04). Note: * See endnote about 1980 or later.

Figure 10: Numbers of RSO Properties and Units by Decade Built



Source: Economic Roundtable analysis; Los Angeles Housing Department. 2024. Dataset A: RSO Inventory; Los Angeles County Assessor. 2023. SBF Abstract (DS04). Note: * See endnote about 1980 or later.

The number of RSO properties and units built in each decade are shown side-by-side in *Figure 10*.

The era before World War II saw the City being dramatically built out. Construction slowed during the war. After the war, single-family tract housing became the dominant type of housing development.

Subsequent decades saw multi-family construction – properties and units now under RSO jurisdiction – in the San Fernando Valley and West Los Angeles planning districts, along with the replacement of some older single-family homes with apartment buildings in the Central, South and East planning districts. The window for inclusion in RSO governance closed when the RSO was enacted in 1979, capping the size of this housing segment.

RSO Condominium Units

The complete inventory of housing units under the jurisdiction of the RSO is described in this chapter. This includes roughly 46,000 condominium units built and certified for occupancy before October 1, 1978. These condominiums make up seven percent of the total RSO

inventory, although this portion of the RSO inventory fluctuates due to being rented out to tenants some years, and occupied by owners or left vacant during other years.

In the following chapters, condominium units are excluded from tables and figures that breakout the RSO inventory by number of units on the parcel. This is because they show up as one-unit properties due to their discrete ownership and separate property records in the Los Angeles County Assessor's records. However, nearly all are attached to larger multi-family residential buildings.

The landlords may own one or just a few condominium units, but in reality the units have characteristics of very large RSO properties. The RSO applies only to properties on parcel with two or more units, but includes condominiums. In the following chapters, we avoid putting them into a category of "one to four units," and instead limit the smallest category to "two to four units," with condominiums excluded.

Findings

- Los Angeles has an estimated 1,549,889 total housing units for a total population of 3,822,224 residents, or 2.47 residents per unit.
- Almost two-thirds of Los Angeles residents rent the housing units in which they reside – 64 percent.
- Forty-two percent of the City's residents live in rent-stabilized housing.
- Half of RSO properties were constructed before 1950, while another 29 percent were built from 1950 to 1970. The remainder were built in the 1970s.
- The preponderance of RSO-dominant neighborhoods are located in the Los Angeles basin, plus the Southeast San Fernando Valley.



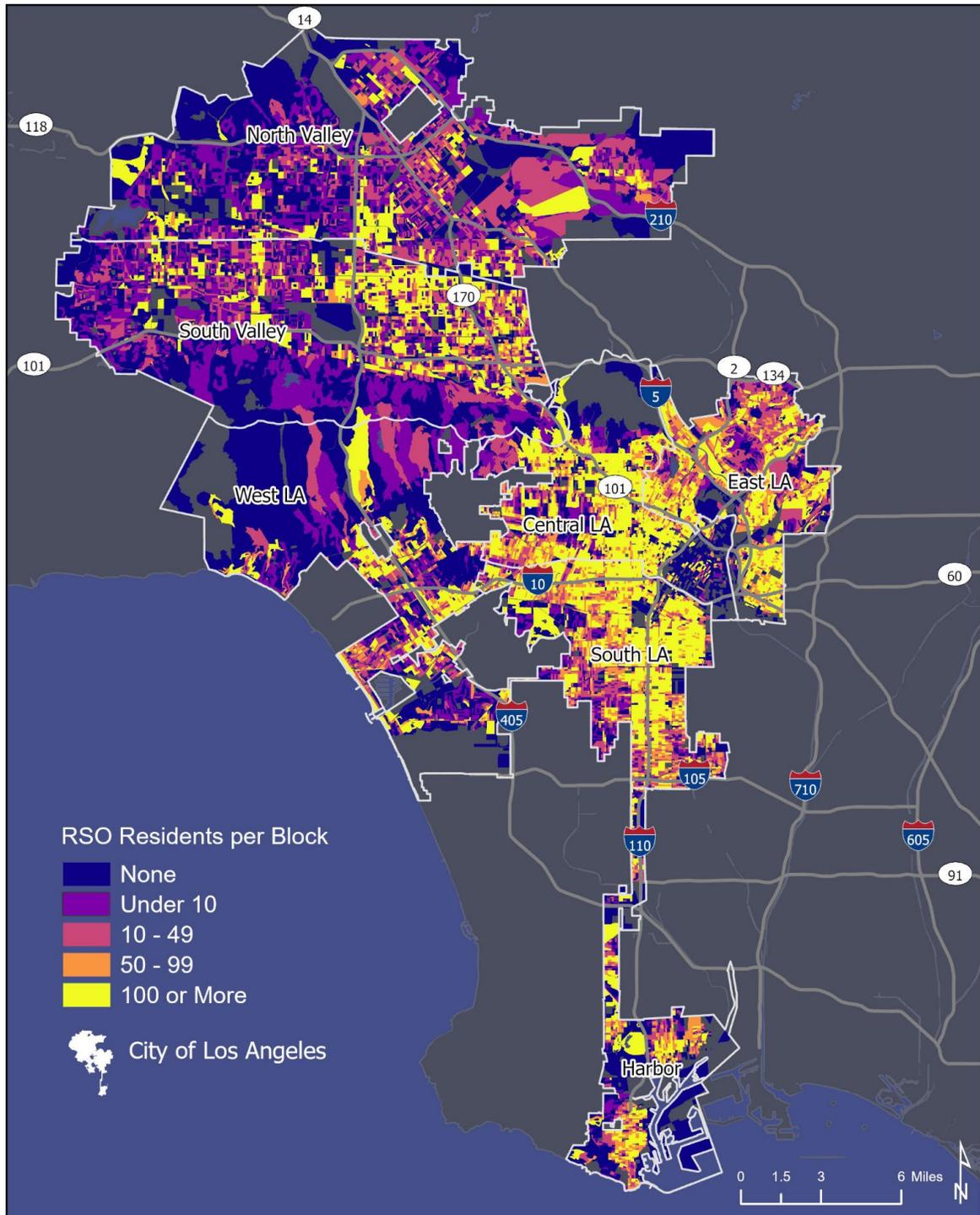
3. Los Angeles Renters

*Photo credit:
Economic Roundtable*

Location of RSO Tenants

Rent stabilized units are concentrated in the urban core of Los Angeles, as can be seen in *Figure 11*.¹³ These units are the City's oldest rental housing,

Figure 11: Population Density of Tenants in Rent Stabilized (RSO) Housing

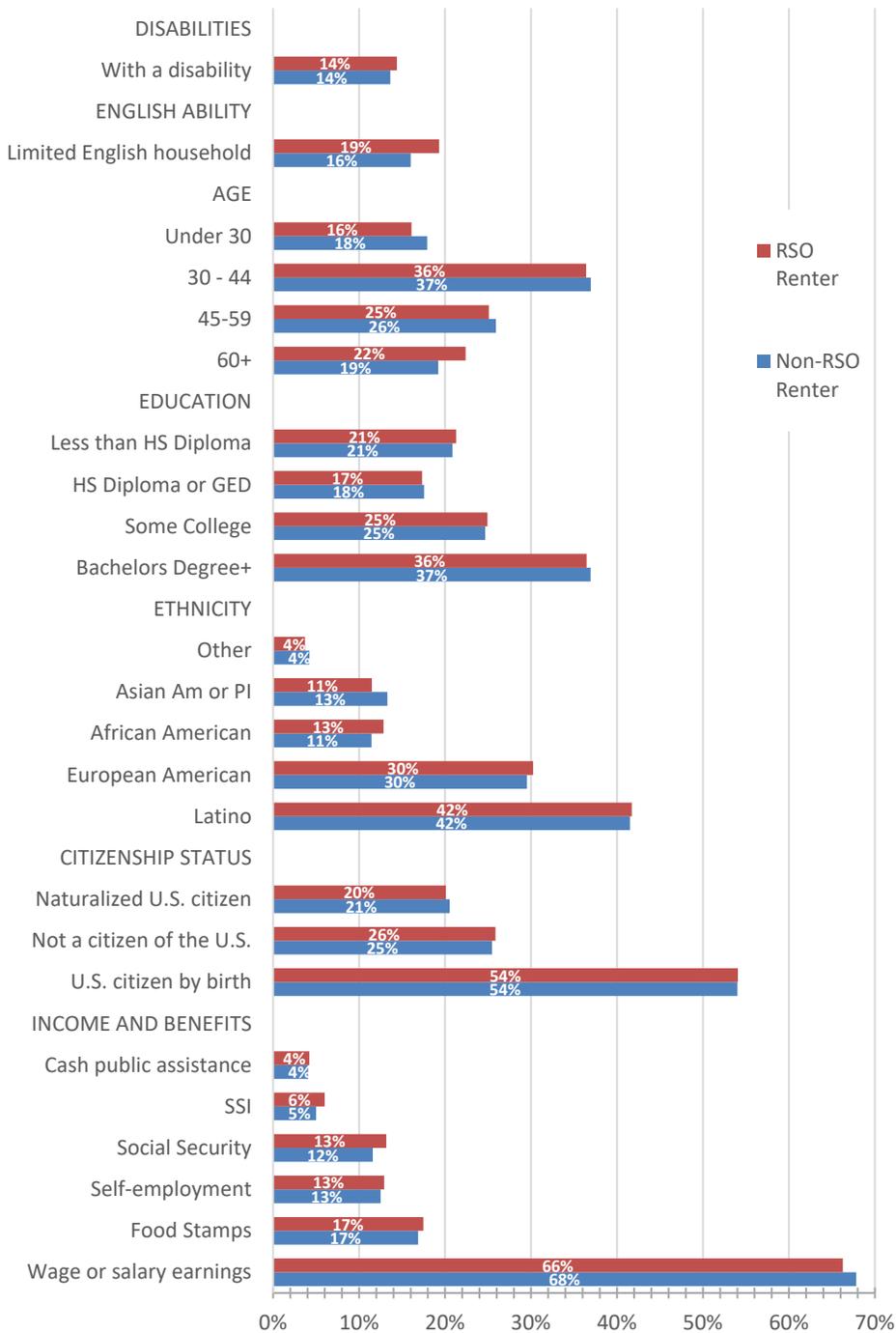


Source: Economic Roundtable analysis; City of Los Angeles Housing Department RSO Rent Registry; U.S. Census Bureau, 2020, Decennial Census of Population and Housing, PL94-171 Redistricting Summary File Table P1. Note: RSO Residents per Block = ((RSO Units per block / Total Housing Units per block) * Total Population per block).

built before October 1, 1978, when the Rent Stabilization Ordinance (RSO) took effect. There are 125 or more RSO residents per block in Central and South Los Angeles.

Newer apartments that were built later as northern and western communities in the San Fernando Valley were developed, as well as newer apartments in other parts of the City, are not subject to the RSO.

Figure 12: Similarities of RSO and Non-RSO Renters



Data source: U.S. Census Bureau Public Use Microdata Sample 2018-2022.

The Southeast San Fernando Valley communities of Van Nuys, Valley Glen, Sherman Oaks, North Hollywood, Toluca Lake are also home to large numbers of RSO renters, followed by Silver Lake, Echo Park, El Sereno, and Boyle Heights in East Los Angeles.

Some West Los Angeles neighborhoods – such as Palms, Pico Robertson, Venice, Westchester, Sawtelle and Westwood – as well as the Harbor communities of San Pedro, Wilmington and Harbor City, have pockets with high numbers of RSO renters.

Attributes of RSO and Non-RSO Households

Similarities

RSO and non-RSO renters have similar demographic characteristics, as shown in *Figure 12*.¹⁴ This includes presence of disabilities, ethnicity, level

Figure 13: Differences between RSO and Non-RSO Renters



Data source: U.S. Census Bureau Public Use Microdata Sample 2018-2022.

of education, age, sources of income, and English fluency. In both populations of renters, the largest ethnic groups are Latinos and almost two-thirds of renters do not have a four-year college degree.

Differences

There are significant differences in the household structure and housing conditions of RSO and non-RSO renters, as shown in *Figure 13*. RSO renters are more likely to live alone, in one-person households made up of a single female or male. More non-RSO renters are married couples.

More RSO units are overcrowded or severely overcrowded with more than 1.5 tenants per room.

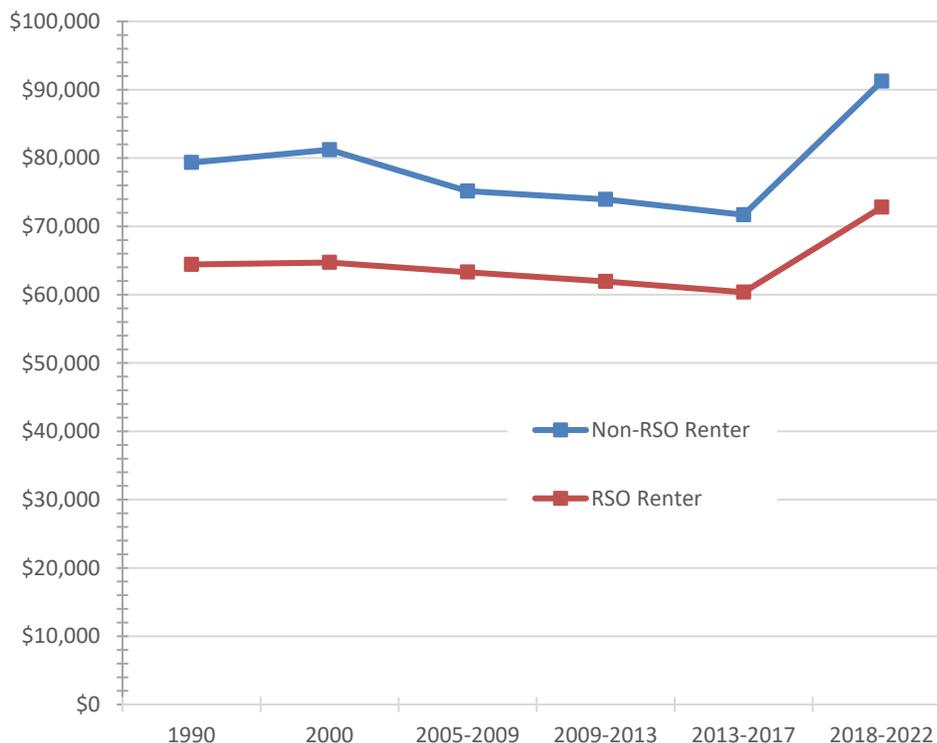
Non-RSO renters are more likely to have moved into their unit in the past year, whereas more RSO renters have been in their units more than a year.

Financial Condition of RSO and Non-RSO Renters

Household Income

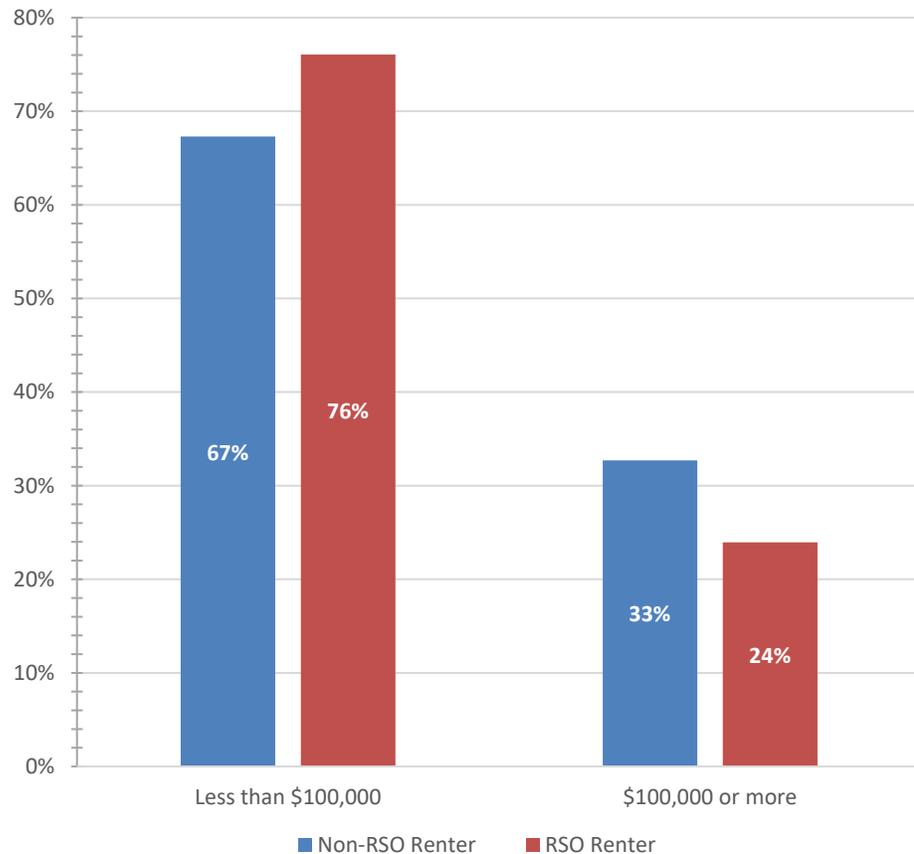
Over the past three decades the gap between the household incomes between RSO and non-RSO renters has remained roughly constant, as

Figure 14: Average Household Income of RSO and Non-RSO Renters in 2022 Dollars



Data source: U.S. Census Bureau Public Use Microdata Samples.

Figure 15: Household Incomes of RSO and Non-RSO Renters in 2022 Dollars



Data source: U.S. Census Bureau Public Use Microdata Sample 2018-2022.

shown in *Figure 14*. There has been slight year-to-year variation, but overall, throughout the past three decades, the income of non-RSO households has been 22 percent higher than the income of RSO households.

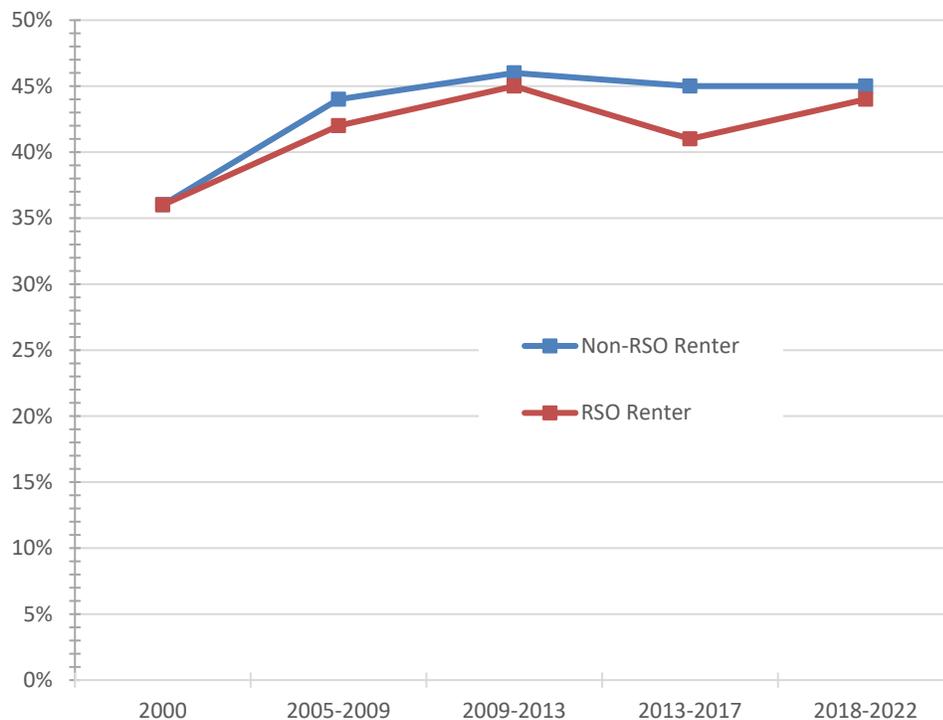
Income Distribution

On average, non-RSO households are more affluent than RSO households, as shown in *Figure 15*. Non-RSO households are more likely to have incomes over \$100,000 (29 vs 20 percent). RSO households are more likely to have incomes under \$80,000 (71 vs 63 percent).

Rent Burden

On average, over the past three decades, the rent burden for non-RSO households has been four percent higher than for RSO households, as shown in *Figure 16*. This long-term similarity in rent burden indicates that rent has increased in the same ratio to income for both groups of renters.

Figure 16: Average Gross Rent as Percent of Household Income



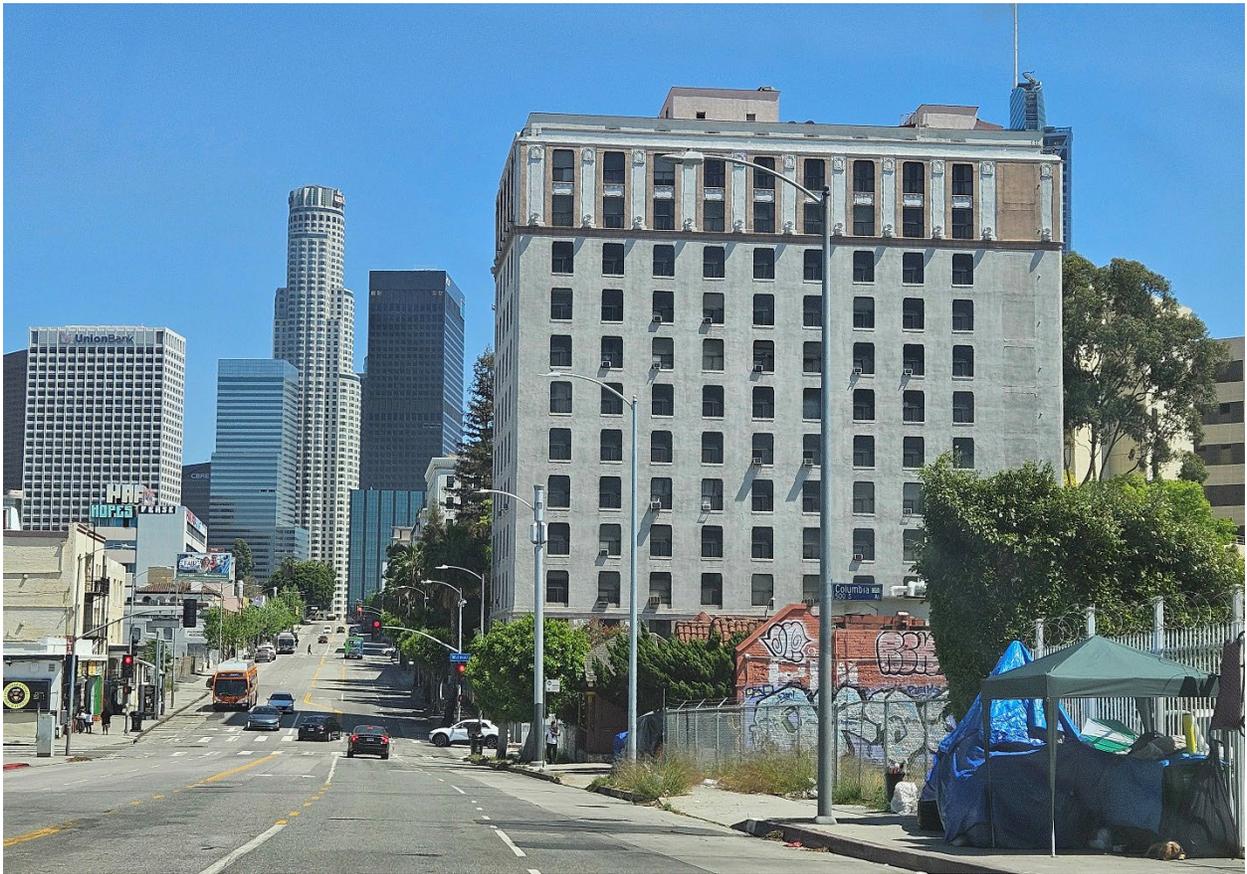
Data source: U.S. Census Bureau Public Use Microdata Samples.

However, given the higher average income of non-RSO renters, the same percent spent on housing is less likely to divert funds away from other basic necessities. Rent burden is only one incomplete measure of housing insecurity.¹⁵

Findings

- Rent stabilized units are older and concentrated in the urban core of Los Angeles. Non-RSO units are newer and concentrated in areas of Los Angeles that have been built-out more recently.
- RSO and non-RSO renters have similar demographic characteristics, including frequency of disabilities, ethnicity, level of education, age, sources of income, and English fluency.
- RSO and non-RSO renters differ in that RSO households are more frequently made up of a single person, and are more often overcrowded.
- Non-RSO households are slightly more likely to have moved recently.
- The average income of non-RSO households is 22 percent higher than the income of RSO households. However, both groups of renters have similar levels of rent burden because the average rent for non-RSO units is higher.

- The similarity in the level of rent burden for RSO and non-RSO renters over the past three decades indicates that rent has increased in the same ratio to income for both groups of renters. However, given the higher average income of non-RSO renters, the same percent spent on housing is less likely to divert funds away from other basic necessities.



4. Attributes of Vulnerable Renters

*Photo credit:
Economic Roundtable*

Poverty and Rent Burden

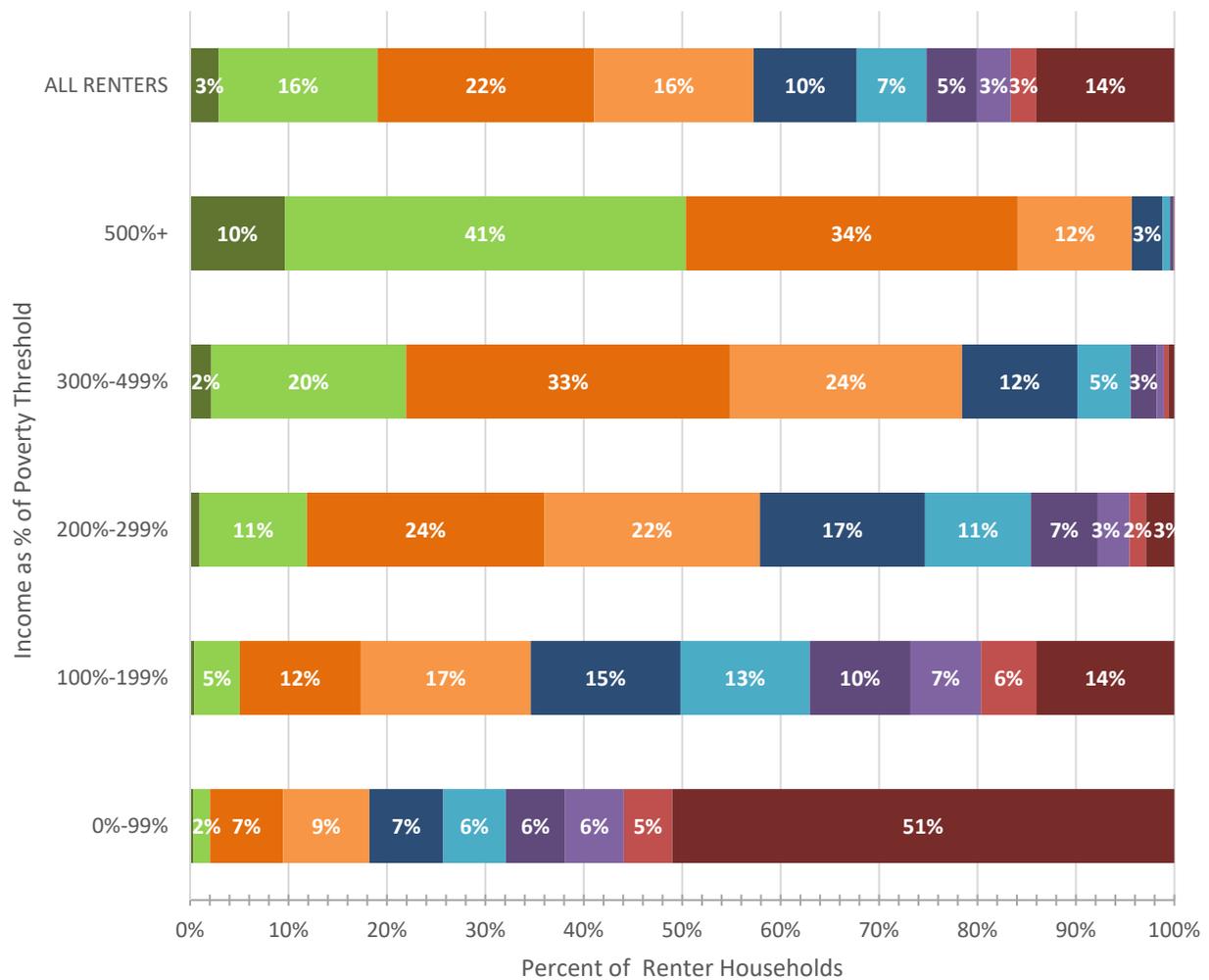
One-fifth of Los Angeles renters are in poverty, based on the federal benchmark. Over half of renter households that are in poverty spend over 90 percent of their household income for rent, as shown in *Figure 17*.

Renters with this double liability of poverty and overwhelming rent burden make up 10 percent of all Los Angeles renters. The share is similar for both RSO and non-RSO renters. These are the *most vulnerable renters*.

Progressively smaller shares of renters in higher income groups are also overwhelmingly rent burdened. Fourteen percent of all City of Los Angeles renters spend 90 percent or more of their income for rent.

Thirty-two percent of the City’s renters are severely rent burdened, spending 50 percent or more of household income for rent. Eighty-one

Figure 17: Percent of Household Income Spent for Rent by City of Los Angeles Renters



Percent of income spent on rent:

■ 0%-9% ■ 10%-19% ■ 20%-29% ■ 30%-39% ■ 40%-49% ■ 50%-59% ■ 60%-69% ■ 70%-79% ■ 80%-89% ■ 90%+

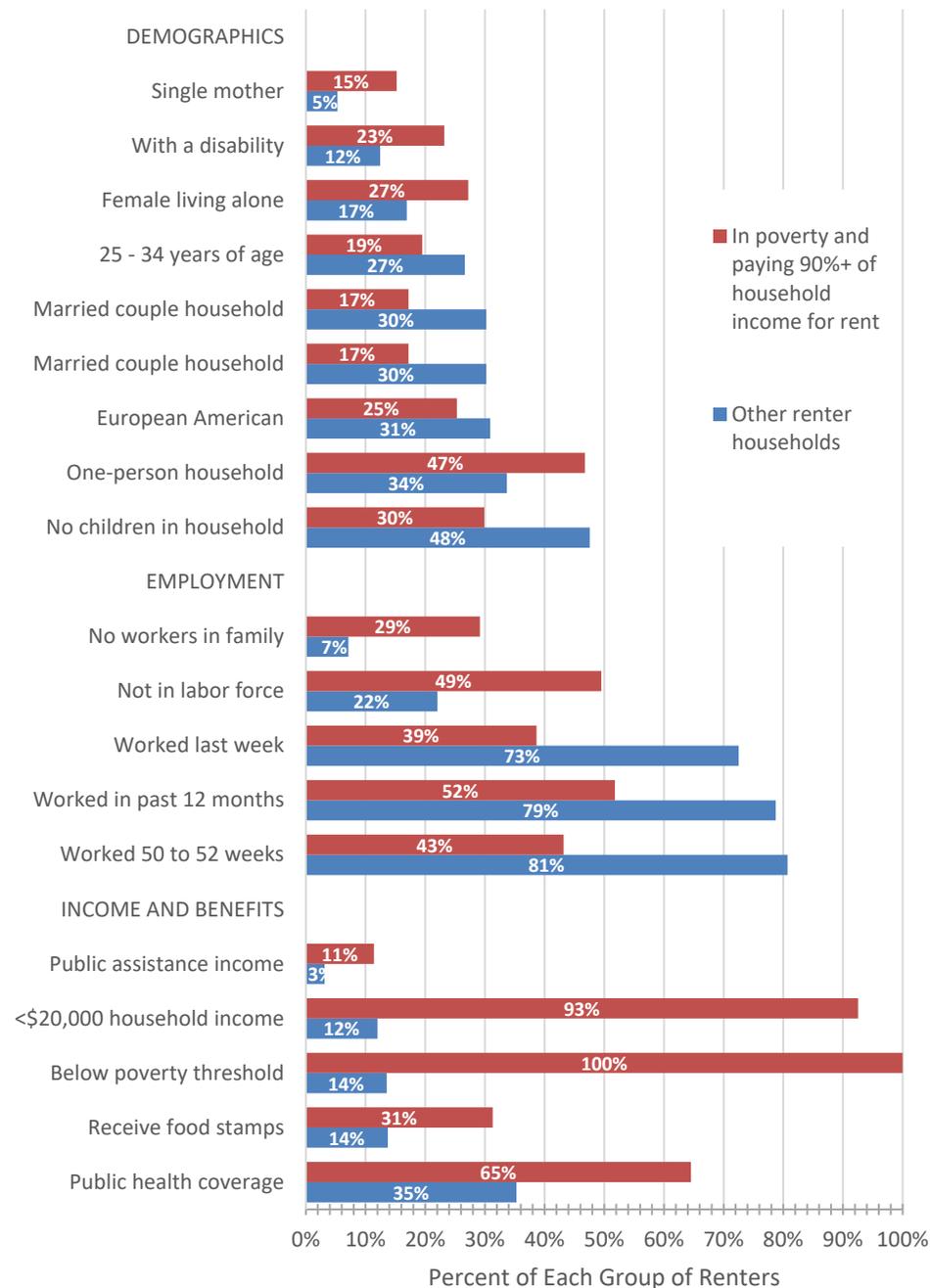
Data source: U.S. Census Bureau Public Use Microdata Sample 2017-2021.

percent of severely burdened households have incomes near or below the poverty level, that is, below 200 percent of the federal poverty threshold.

Overwhelmingly Rent Burdened Renters

Highly vulnerable renters differ from other renters based on: age – they are more likely to be younger, household structure – they are more likely to

Figure 18: Attributes that Distinguish Los Angeles Renters in Poverty and Paying 90%+ of their Income for Housing from Other Renters



Data source: U.S. Census Bureau Public Use Microdata Sample 2017-2021.

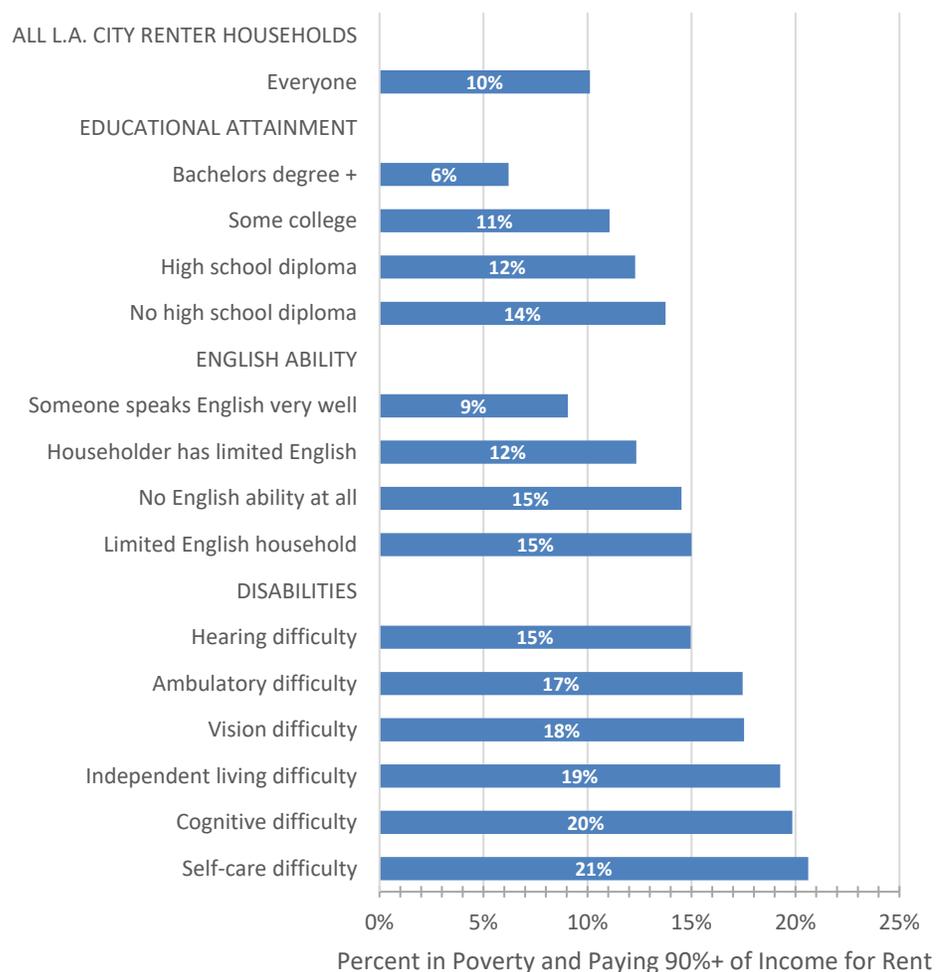
live alone, employment status – they are more likely to be unemployed, income – they are more likely to have annual incomes below \$20,000, and they are more likely to receive public benefits. These comparisons are shown in *Figure 18*.

Attributes that Elevate the Likelihood of being in Poverty and Paying 90 Percent or More of Income for Rent

Probability based on Education, English Ability and Disabilities

The likelihood of being among the most vulnerable renters increases as individuals’ level of education decreases, as shown in *Figure 19*. The probability is only six percent if the head of household has a four-year college degree compared to 14 percent for those without a high school diploma.

Figure 19: Probability of being in Poverty and Paying 90%+ of Income for Rent Based on Education, English Ability and Disabilities



Data source: U.S. Census Bureau Public Use Microdata Sample 2017-2021.

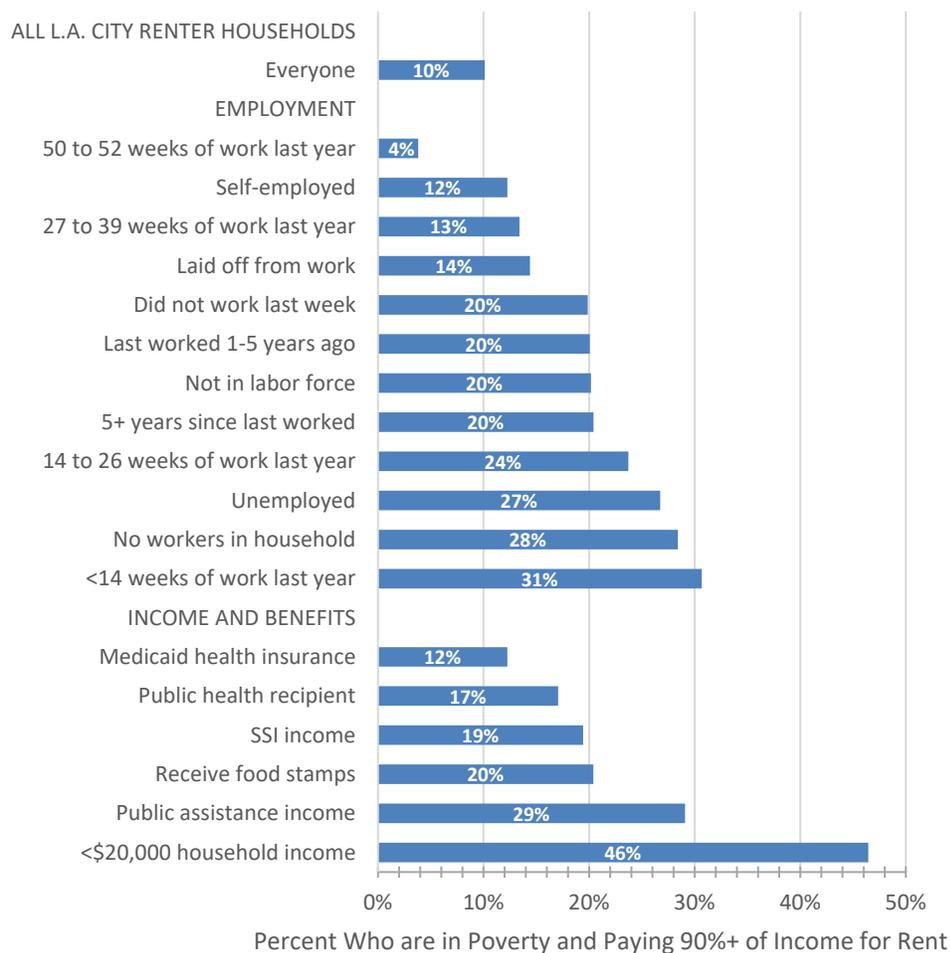
If the entire household has limited English ability there is a 15 percent probability that they will be among the most vulnerable renters. The probability goes down to nine percent if someone in the household who is over 14 years of age speaks English fluently.

The presence of a disability makes the household more vulnerable. If the householder has a hearing disability, there is a 15 percent probability that the household will be in poverty and paying 90 percent or more of their income for rent. The probability increases to 17 percent for ambulatory difficulties, 18 percent for vision difficulties, 19 percent for independent living difficulties, 20 percent for cognitive difficulties, and 21 percent for self-care difficulties.

Probability based on Employment, Income and Public Benefits

The employment status of the head of household and use of public benefits by household members are linked to the probability of being among the most vulnerable renters, as shown in *Figure 20*.

Figure 20: Probability of being in Poverty and Paying 90%+ of Income for Rent Based on Employment, Income and Public Benefits



Data source: U.S. Census Bureau Public Use Microdata Sample 2017-2021.

If the head of household worked full-time in the previous year, there is only a four percent probability that the household will be among the most vulnerable renters. The probability increases to 14 percent if the householder is laid off from work and 20 percent if the householder did not work in the past week.

Working only 14 to 26 weeks in the past year causes income volatility and precarious connections to benefits programs, and is associated with a 24 percent probability of being among the most vulnerable renters.

Unemployment increases the probability to 27 percent and having no workers in the household increases it to 28 percent. If the householder worked less than 14 weeks in the past year, the amount of earned income will be low and the connections to income supports may be intermittent, creating a 31 percent probability that the household will be among the most vulnerable renters.

Renters enrolled in public benefits programs have an increased likelihood of being among the most vulnerable renters, with additional risks associated with receiving cash aid or having an extremely low income.

Enrollment in Medicaid (Medi-Cal in California) is associated with a 12 percent probability. This increases to 19 percent for Supplemental Security Income (SSI) recipients, 20 percent for food stamp recipients, and 29 percent for recipients of cash assistance.

Households with a total annual income under \$20,000 have a 46 percent probability of being among the most vulnerable renters.

Probability based on Demographics, Household Structure and Housing Condition

Demographic attributes, household structure and housing condition are linked to the probability of being among the most vulnerable renters, as shown in *Figure 21*.

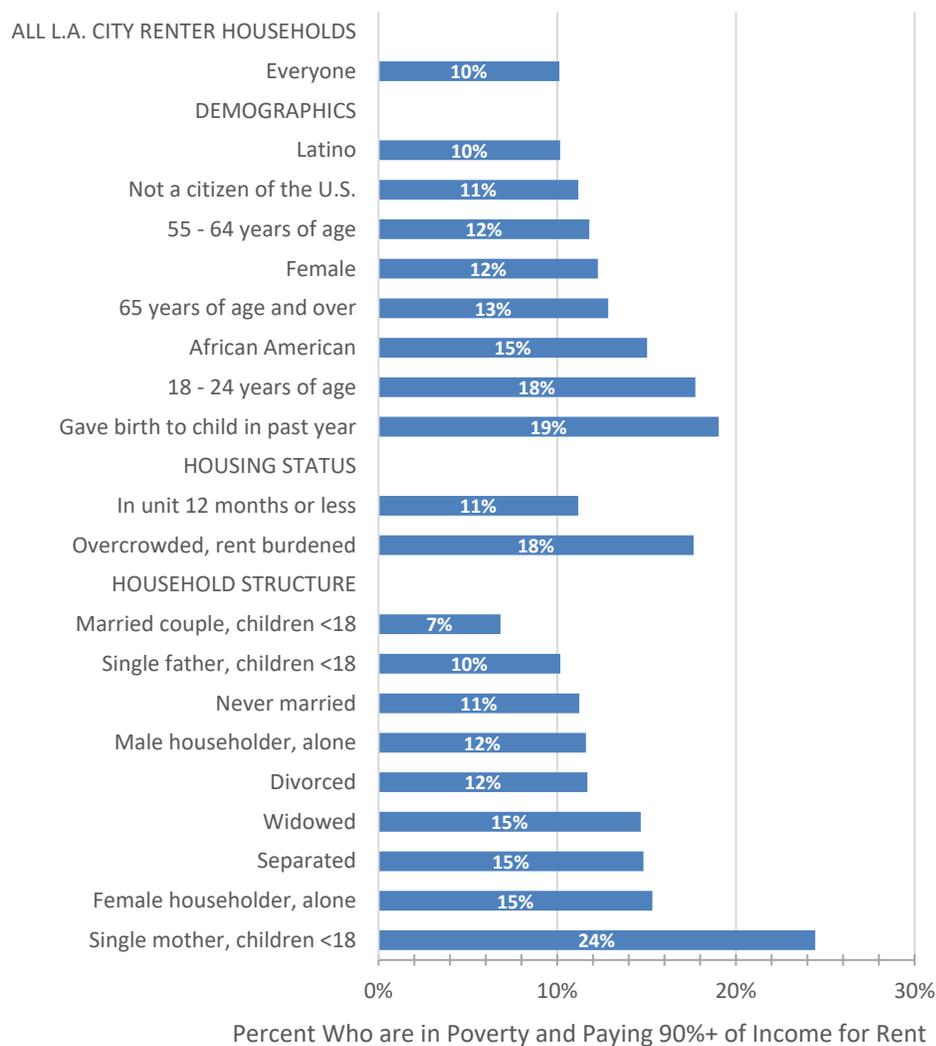
Latino households have the same rate of vulnerability as the overall renter population – 10 percent. This increases to 12 percent if the householder is 55 to 64 years old or female, and 13 percent for those 65 years of age or older.

If the householder is African American, there is a 15 percent probability of being among the most vulnerable renters. This increases to 18 percent if the householder is a young adult, and 19 percent if the householder has given birth in the past year.

If the household has been in their unit for one year or less, there is an 11 percent probability of being among the most vulnerable renters. If they are both overcrowded and rent burdened the probability increases to 18 percent.

A married couple with children under 18 years of age has a seven percent probability of being among the most vulnerable renters. Single fathers with

Figure 21: Probability of being in Poverty and Paying 90%+ of Income for Rent Based on Demographics, Household Structure and Housing Condition



Data source: U.S. Census Bureau Public Use Microdata Sample 2017-2021.

children have a 10 percent probability, but the probability shoots up to 24 percent for single mothers with children.

An adult male living alone has a 12 percent probability of being among the most vulnerable renters, but an adult female living alone has a 15 percent probability.

Householders who are widowed or separated have a 15 percent probability of being among the most vulnerable renters.

Findings

- Highly vulnerable renters who are in poverty and pay 90 percent or more of their income from rent differ from other renters based on: age – they are more likely to be younger, household structure –

they are more likely to live alone, employment status – they are more likely to be unemployed, income – they are more likely to have annual incomes below \$20,000, and they are more likely to receive public benefits.

- If the head of household does not have a high school diploma, there is a 14 percent probability of being among the most vulnerable renters.
- If the entire household has limited English ability there is a 15 percent probability that they will be among the most vulnerable renters.
- The presence of a disability makes the household more vulnerable, with a 21 percent probability of being among the most vulnerable renters if the head of household has a self-care difficulty.
- The probability of being among the most vulnerable renters is 14 percent if the householder is laid off from work and 20 percent if the householder did not work in the past week. Unemployment increases the probability to 27 percent and having no workers in the household increases it to 28 percent.
- Enrollment in Medi-Cal is associated with a 12 percent probability. This increases to 19 percent for Supplemental Security Income (SSI) recipients, 20 percent for food stamp recipients, and 29 percent for recipients of cash assistance.
- Households with a total annual income under \$20,000 have a 46 percent probability of being among the most vulnerable renters.
- If the householder is African American, there is a 15 percent probability of being among the most vulnerable renters. This increases to 18 percent if the householder is a young adult, and 19 percent if the householder has given birth in the past year.
- An adult male living alone has a 12 percent probability of being among the most vulnerable renters, but an adult female living alone has a 15 percent probability.
- Single fathers with children have a 10 percent probability of being among the most vulnerable renters, but the probability shoots up to 24 percent for single mothers with children.



5. Rent Savings for RSO Tenants

*Photo credit:
Economic Roundtable*

Citywide Difference between RSO and Non-RSO Renters

Citywide, the rent for non-RSO units has been an average of 25 percent higher than for RSO units from 1990 through 2022, as shown in *Figure 22*.

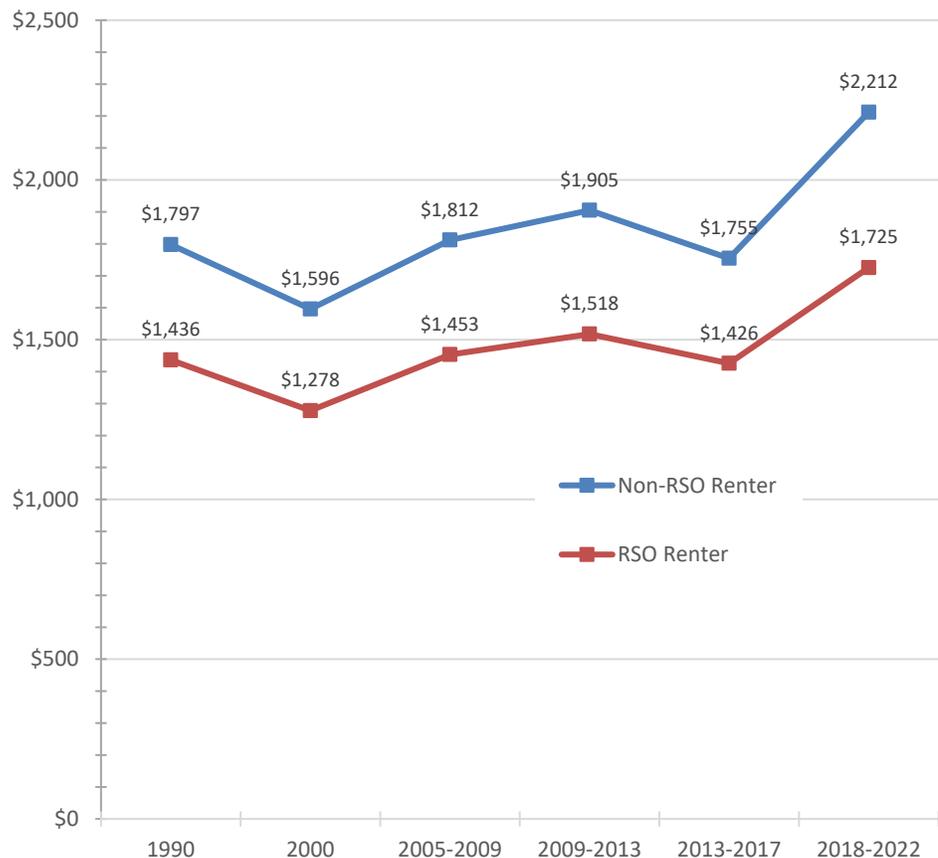
The gap was smallest in 2013 to 2017, at 23 percent, and largest in 2018 to 2022, at 28 percent. This is based on comparing all RSO units with all non-RSO units without accounting for differences in the locations and sizes of RSO and non-RSO units.

The rent differential between the two inventories of rental housing differs based on the size and location of rental units.

Size of RSO and Non-RSO Units

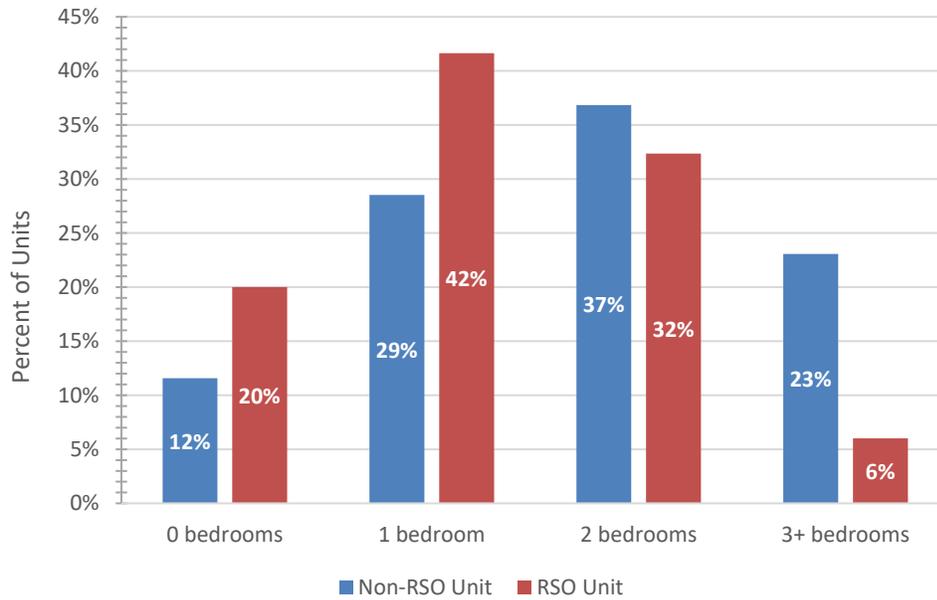
Non-RSO units in the City of Los Angeles have an average of 2.1 bedrooms, whereas RSO units have an average of 1.5 bedrooms, as shown in *Figure 23*. A larger share of the RSO inventory is made up of studio and one-bedroom apartments, whereas a larger share of the non-RSO inventory is made up of apartments with two or more bedrooms.

Figure 22: Average Monthly Gross Rent for RSO and Non-RSO Units in 2022 Dollars



Data source: U.S. Census Bureau Public Use Microdata Samples. Each data point represents the average of the five years of survey data that are compiled in each release of Public Use Microdata Sample records. All rent amounts have been adjusted to 2022 dollars.

Figure 23: Number of Bedrooms in RSO and Non-RSO Units

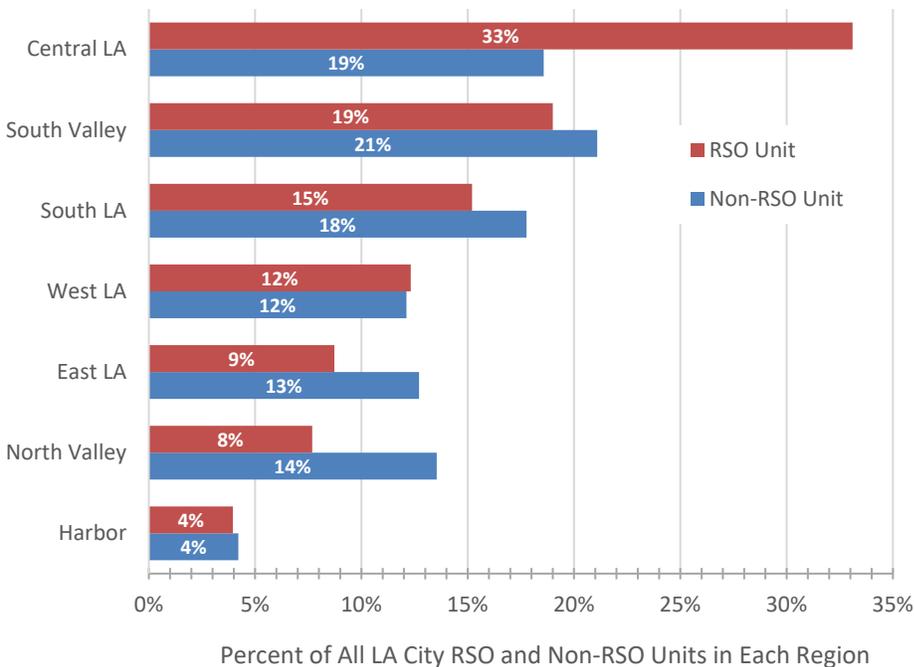


Data source: U.S. Census Bureau Public Use Microdata Sample 2018-2022.

Geographic Distribution of RSO and Non-RSO Units

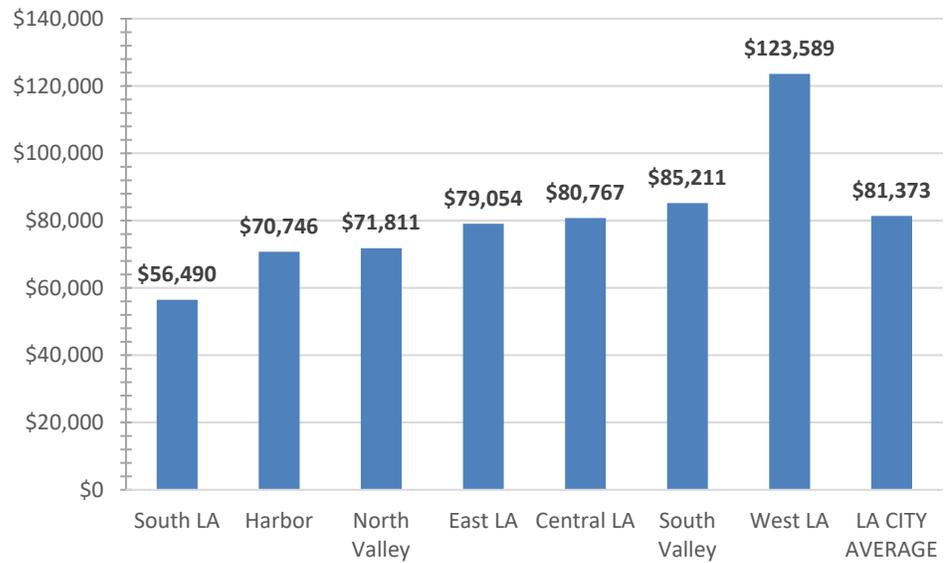
The largest share of RSO units is in Central Los Angeles, whereas the largest share of non-RSO units is in the South San Fernando Valley, as shown in *Figure 24*.

Figure 24: Percent of Los Angeles' Total RSO and Non-RSO Rental Inventories in Each Planning District of the City



Data source: U.S. Census Bureau Public Use Microdata Sample 2018-2022.

Figure 25: Average Household Income of Renters by Planning District in 2022 Dollars



Data source: U.S. Census Bureau Public Use Microdata Sample 2018-2022.

There are much larger shares of the non-RSO inventory than of the RSO inventory in East Los Angeles and the Northern San Fernando Valley.

Within the Central Los Angeles district, RSO units make up 66 percent of the rental housing inventory and non-RSO units make up 34 percent. In contrast, within the North San Fernando Valley district, RSO units make up only 38 percent of the rental inventory, but non-RSO units make up 62 percent.

These differences are important because the average income of renters is different in different districts of the City. The rental market reflects these differences in the amount of rent that tenants can afford to pay.

Average Income of Renter Households in Different Districts of Los Angeles

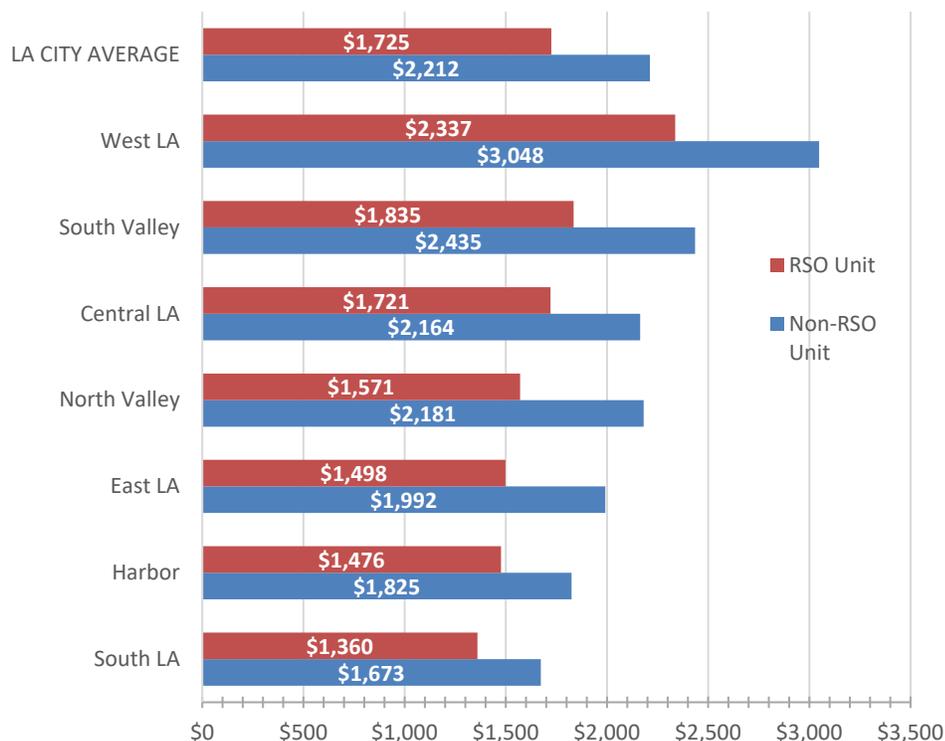
The average household income for all Los Angeles renters in 2022 was \$81,373, as shown in *Figure 25*.

Household incomes in East Los Angeles, Central Los Angeles and the Southern San Fernando Valley came within a few thousand dollars of the City average. However, incomes in South Los Angeles were 31 percent below the City average and incomes in West Los Angeles were 52 percent greater than the City average.

Rent for RSO and Non-RSO Units in Different Districts of Los Angeles

Over the five-year period of 2018 to 2022, the average gross rent for RSO units, when adjusted to 2022 dollars, was \$1,723, and the average for non-RSO units was \$2,027, as shown in *Figure 26*.

Figure 26: Gross Monthly Rent in 2022 Dollars for RSO and Non-RSO Units by Planning District



Data source: U.S. Census Bureau Public Use Microdata Sample 2018-2022, average of all five years.

Rents in Central Los Angeles are very close to the City average for both RSO and non-RSO units. However, rents in South Los Angeles for RSO and non-RSO units are 21 and 24 percent, respectively, less than the City average. Rents in West Los Angeles for RSO and non-RSO units are 36 and 38 percent, respectively, higher than the City average.

Controlling for Differences Affecting RSO and Non-RSO Rents

There are differences in the size of RSO and non-RSO units, the shares of the RSO and non-RSO rental inventories located in different districts of the City, the income levels of renters in different districts of the City, and the average rent for RSO and non-RSO units in different districts of the City.

It is feasible to control for the size of units in estimating the difference in rent for RSO and non-RSO units. However, it is not feasible to control for geographic differences without the risk of arbitrariness in including some communities and excluding other communities.

When considering comparisons between rents of RSO and non-RSO units it is critical to understand that multiple factors come into play, apart from whether or not the RSO is applicable. These factors include differences in location, amenities, and building size.

Rent Savings for Tenants in RSO Units

Savings Based on Comparable Number of Bedrooms

Rent for RSO and non-RSO rental units can be compared based on two size criteria - either number of bedrooms or total number of rooms.

Savings for RSO renters compared to non-RSO renters based on the number of bedrooms are shown in *Figure 27*.

Savings are greatest for renters of studio apartments that do not have a bedroom, where there is a 31 percent rent differential for RSO renters.

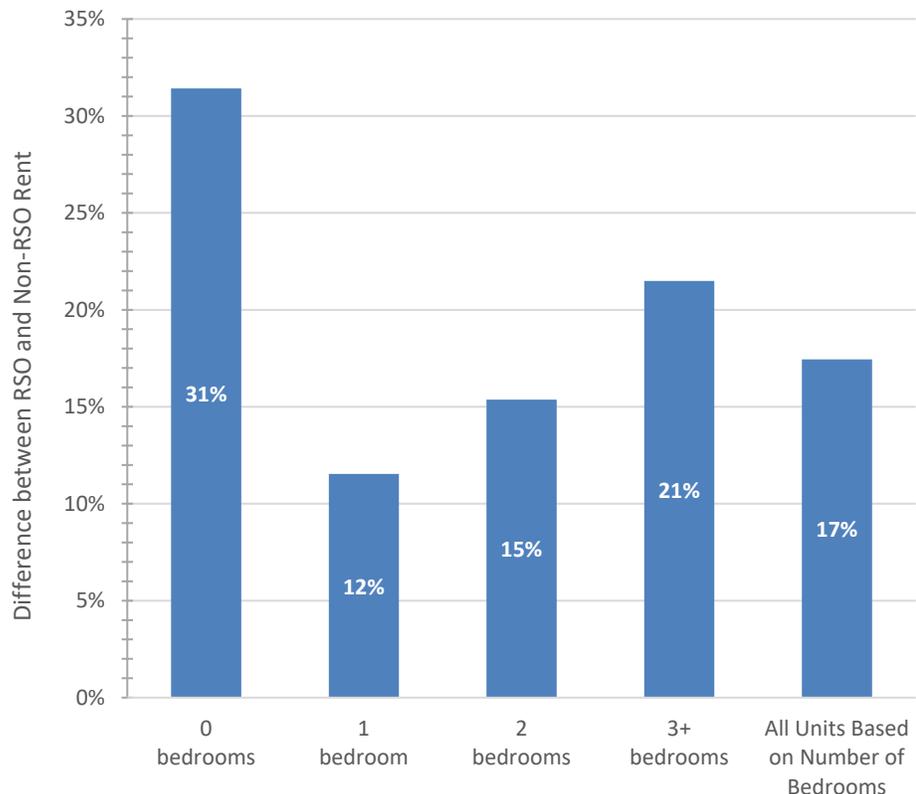
Savings are smallest for renters of one-bedroom apartments, where there is a 12 percent rent differential for RSO renters.

Savings increase to 15 percent for two-bedroom apartments and 21 percent for apartments with three or more units.

Apartments with one or two bedrooms make up 70 percent of the City's rental housing inventory and are the core of the rental market.

The average difference in rent for all RSO and non-RSO units based on number of bedrooms, weighted by the share of the City's rental inventory made up of units of each size, is 17 percent.

Figure 27: Savings for RSO Renters Compared to Non-RSO Renters Based on Number of Bedrooms in Unit



Data source: U.S. Census Bureau Public Use Microdata Sample 2018-2022, average of all five years.

Savings Based on Total Number of Rooms

Savings for RSO renters compared to non-RSO renters based on the total number of rooms in rental units are shown in *Figure 28*. This information comes from the American Community survey and includes bedrooms, kitchens, living rooms, dining rooms, family rooms, and offices. It excludes bathrooms, porches, balconies, foyers, halls, and unfinished basements.

Savings are greatest for renters of studio apartments that do not have a bedroom, where there is a 33 percent rent differential for RSO renters based on the metric of total rooms.

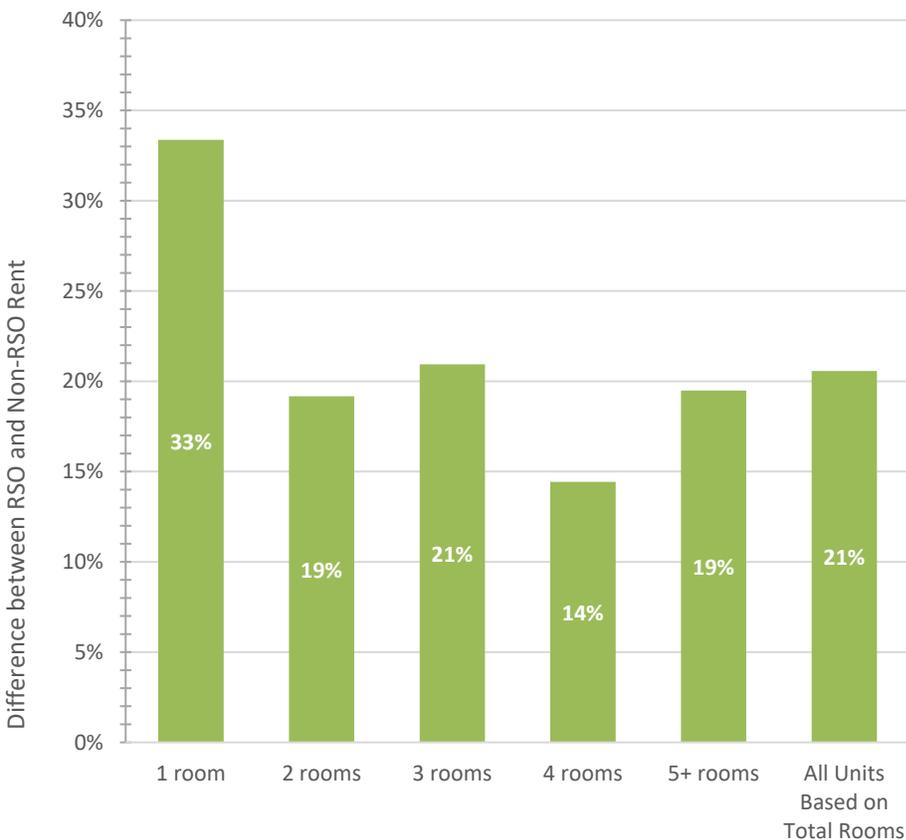
Savings are similar for renters of units with two, three and five or more rooms, with a 19 to 21 percent rent differential for RSO renters.

Savings are smallest for renters of four-room units, where there is an average rent differential of 14 percent for RSO renters.

Apartments with three or four rooms make up 52 percent of the City's rental housing inventory and are the core of the rental market.

The average difference in rent for all RSO and non-RSO units based on total number of rooms, weighted by the share of the City's rental inventory made up of units of each size, is 21 percent.

Figure 28: Savings for RSO Renters Compared to Non-RSO Renters Based on Total Number of Rooms in Unit



Data source: U.S. Census Bureau Public Use Microdata Sample 2018-2022, average of all five years.

Average Savings for RSO Renters

Savings for RSO renters based on number of bedrooms and on total number rooms have equal credibility because each captures relevant information about the amount of livable space within a dwelling unit.

We use the average of these two metrics, 17 percent savings based on number of bedrooms and 21 percent based on total number of rooms, to estimate the overall average rent savings for RSO renters. This means that the average rent paid by RSO renters is 19 percent less than the rent paid by non-RSO renters for units of comparable size.

Findings

- Citywide, the average rent for non-RSO units has been an average of 25 percent higher than for RSO units from 1990 through 2022. This is based on comparing all RSO units with all non-RSO units without accounting for where units are located or their size.
- Non-RSO units in the City of Los Angeles have an average of 2.1 bedrooms, whereas RSO units have an average of 1.5 bedrooms. Non-RSO units are typically bigger. This difference needs to be taken into consideration in estimating the rent savings for RSO units.
- There are differences in the size of RSO and non-RSO units, the shares of the RSO and non-RSO rental inventories located in different districts of the City, the income levels of renters in different districts of the City, and the average rent for RSO and non-RSO units in different districts of the City.
- It is feasible to control for the size of units in estimating the difference in rent for RSO and non-RSO units. However, it is not feasible to control for geographic differences.
- The rent differential between RSO and non-RSO units is the average of multiple different rental markets within the City.
- Based on comparing the rent for RSO and non-RSO units using both number of bedrooms and total number of rooms as benchmarks, the average rent paid by RSO renters is 19 percent less than the rent paid by non-RSO renters for units of comparable size.



6. Rent Increases and Homelessness

*Photo credit:
Economic Roundtable*

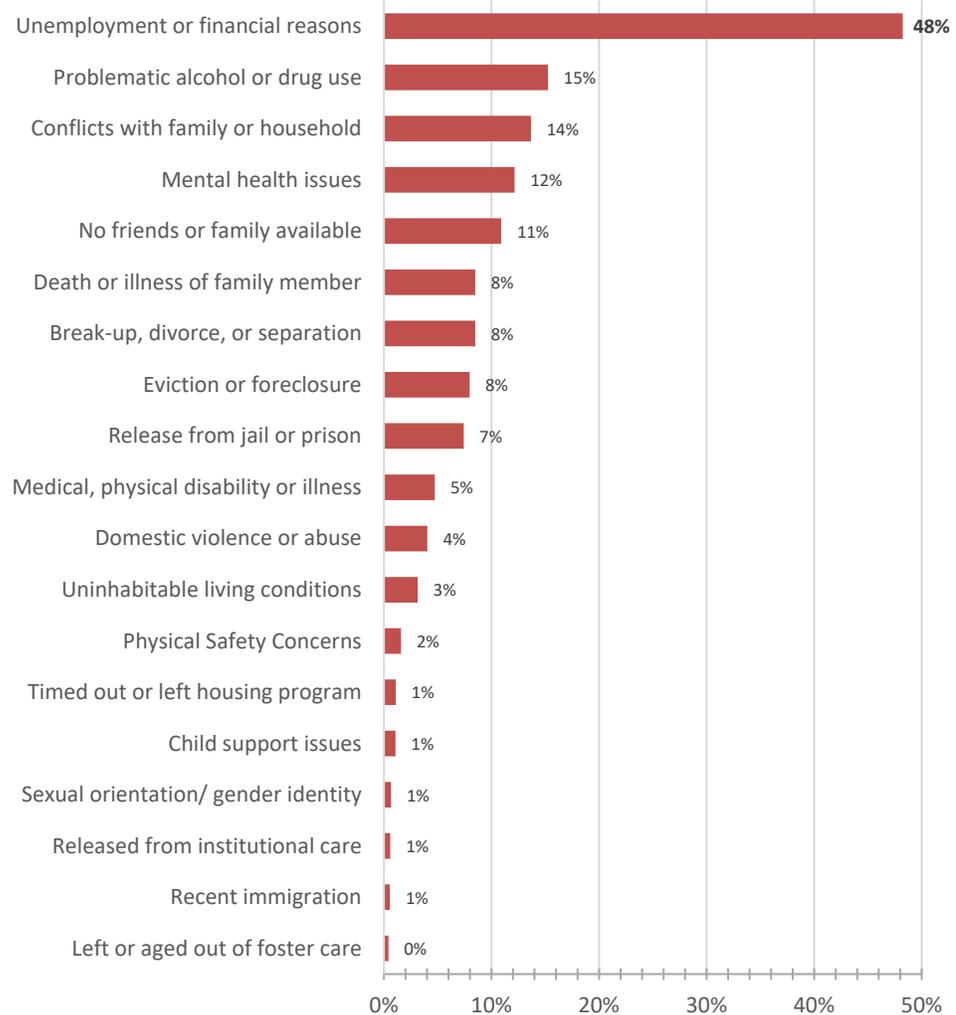
Homelessness is an Income Problem

There is a direct connection between insufficient money to pay rent and homelessness. Over half of all Los Angeles renter households that are in poverty spend over 90 percent of their household income for rent, as was shown earlier in *Figure 29*. For many low-income renters, homelessness is a continuing threat.

A report by the United States General Accounting Office found a “statistically significant relationship between changes in household median rents and changes in rates of homelessness.”¹⁶ Looking at the United States as a whole, the report found that, “a \$100 increase in median rental price was associated with about a nine percent increase in the estimated homelessness rate.”¹⁷

The most frequent explanation that homeless adults in Los Angeles give for their lack of housing is unemployment and lack of money, which caused

Figure 29: Reasons Cited by Unsheltered Homeless Adults for Loss of Housing, 2023



Source: LAHSA 2023 demographic surveys of unsheltered adults. Respondents identified an average of two reasons, so total responses exceed 100 percent.

them to be unable to pay their rent. This overriding explanation was given by half of half of homeless adults living on Los Angeles street in 2023, as shown in *Figure 29*.¹⁸

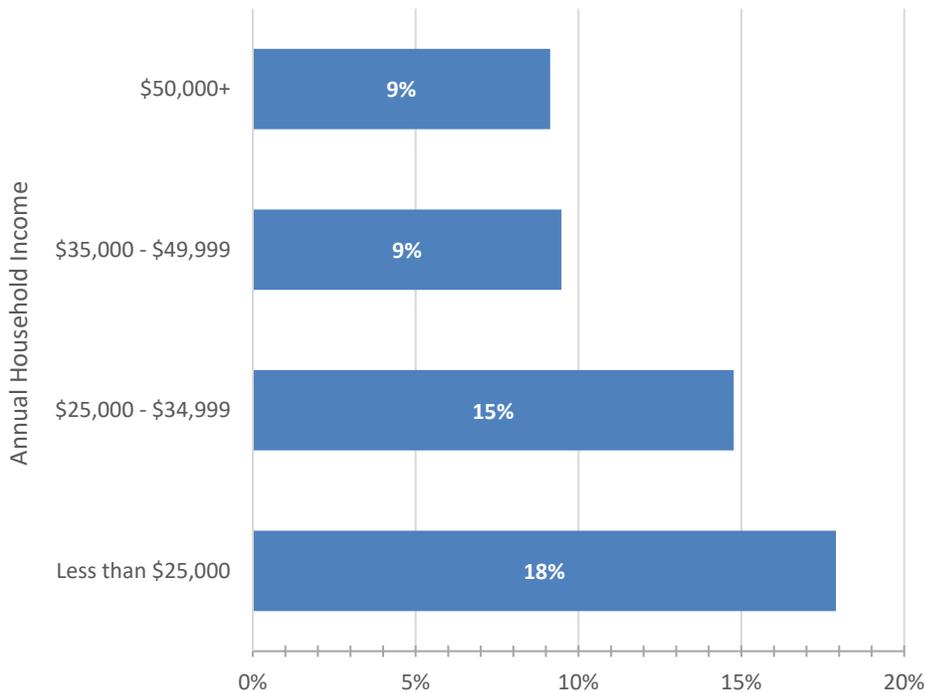
When rent increases, low-wage workers are less likely to have enough income or savings to continue paying their rent, and therefore they are more likely to experience evictions, which impose even more strain on their often fragile finances, health, and access to opportunity.

Homelessness caused by financial shortfalls emerges largely from jobs at the thin edge of the labor market. The center of low-wage employment is in restaurants, retail stores, restaurants and bars, clerical jobs, childcare, and large nonprofit institutions such as universities. These are the largest employers of low-wage workers, who often are precariously housed, even in a growing economy.

There is a direct connection between loss of income and loss of shelter, but these losses do not appear to occur simultaneously. Disconnection from work is a degenerative dynamic – less work, less earnings, less stable living conditions, and further disconnection from work.¹⁹

Lower income and greater housing insecurity are interlocking hazards. Lower-income households are more likely to face eviction than higher-income households. Housing insecurity is widespread among low-income renters.

Figure 30: Income levels of Renters Who Say it is Extremely Likely that they will be Evicted in the Next Two Months



Data source: U.S. Census Bureau Household Pulse Survey, Weeks 1-64, Los Angeles and Orange Counties.

One-quarter of renters in the Los Angeles region have household incomes under \$25,000. Eighteen percent of these households say that it is extremely likely that they will be evicted in the next two months, as shown in *Figure 30*. In addition, 15 percent of households with incomes between \$25,000 to \$35,000 report the same pessimistic expectation.²⁰

People are likely to fend off homelessness as long as possible by foregoing other expenses, relinquishing assets and going into debt in order to remain housed. However, without money to pay for rent or a supportive social network, it is likely that individuals will be evicted and lack a place of their own to sleep.

Rent costs that exceed what tenants can pay is a primary cause of homelessness. The ability of a household to pay rent and retain shelter can break down if income decreases or rent increases.

Overview of GAO Study

There is strong evidence to support the conclusion reached in the GAO study, that increases in rent lead to increases in homelessness. However, the GAO's specific empirical estimates are constrained by significant data and statistical limitations.

Increases in income inequality lead to increases in homelessness because they simultaneously drive up the cost of housing *and* the percent of low-income renters who cannot afford that housing. There is a high rate of homelessness in Los Angeles primarily because of this interaction between the housing market and the labor market—namely, the high cost of housing and the high rate of working poverty.

Evictions act as a mechanism connecting these two problems, as the high cost of housing leads to greater evictions, which then lead to an increase in the likelihood that the evicted individuals will fall into homelessness.

Deep Dive into the GAO Study

In 2020, the U.S. Government Accountability Office conducted a study of how the U.S. Department of Housing and Urban Development (HUD) estimates the size of the homeless population in Continuums of Care for homeless services across the United States. They used those estimates to study how the growth of the homeless population is associated with local demographic, economic, and housing characteristics, as well as local funding for housing support and homeless services.²¹

The overriding conclusion of the GAO report is strongly supported by a large body of evidence—namely, that the cost of housing is the primary reason why some cities, like Los Angeles, have higher rates of homelessness than other cities. This finding is so well documented that a recently published, well-researched book is titled *Homelessness Is a Housing Problem*.²²

Importantly, however, we reach this conclusion by considering the GAO report within the context of this larger literature because the report itself has three significant limitations.

First, to understand what the GAO is investigating, it is important to point out that HUD defines homelessness based on the lack of a permanent structure, resulting in point-in-time counts that focus on individuals living in shelters, on the street, or in temporary or mobile structures such as vehicles or tents. This is a limited definition. It does not include individuals who are living temporarily with family or friends—in a permanent structure—because they do not have a home of their own.

If we consider homelessness to be the lack of a home of one's own, the GAO analysis does not give us much insight into the growth of that group as a whole. We can better understand this analysis by viewing it as an investigation of *severe* homelessness—the type experienced by individuals who have *neither* their own home *nor* anyone else's home to rely on.

Second, the GAO's statistical methodology is limiting in its ability to draw strong conclusions because it is not identifying the *causes* or *drivers* or *determinants* of homelessness. Rather, it is only measuring *correlates* of homelessness. In modern econometrics, this is a critical distinction because *correlation is not causation*. False conclusions can be drawn by noticing two trends occurring in parallel and incorrectly assuming that one is responsible for the other. For instance, it is possible that a growth in homelessness somehow leads to growth in rents or that an omitted third factor is the driving force behind both trends. For this reason, we will present stronger econometric studies that support the GAO report's findings.

Third, the GAO's statistical methodology does not consider the possibility of long-term effects. The regression equation estimates the effect of a variety of factors measured in a given year on homelessness counted in the following January. Thus, these factors have only one to twelve months to impact homelessness. If it takes more time for these factors to change homelessness in a significant way, it is unlikely to be captured by this measurement approach. As noted below, we have good reason to believe that many housing and labor dynamics take many months, if not years, to play out fully, making it important to not ignore long-term effects.

For example, the panorama of homelessness on Los Angeles streets has emerged over many years. The typical (median) length of the current episode of homelessness for unsheltered individuals is 1,096 days. The average length, skewed upwards by individuals for whom homelessness has become a life course, is 1,931 days.²³ Before these three- and five-year stints, respectively, of homelessness, these individuals had some form of shelter, may have had previous stints of homelessness, and many had some form of employment. A series of displacements and institutional failures preceded their life of persistent homelessness in unsheltered places.

With those limitations in mind, there are three important sets of findings in the GAO report:

1. A \$100 increase in median rent is associated with a nine percent increase in homelessness, on average, across the continuums of care for homeless services for which reliable data are available.
2. The analysis finds no significant relationship between homelessness and the following factors, which are often hypothesized as drivers of housing insecurity: median wages, poverty rates, or unemployment rates.
3. The analysis is unable to measure the effect of mental health or evictions on homelessness; thus, it cannot compare these effects to the effect of median rent, nor can it say the extent to which these factors interact with the cost of housing.

There is credible research that is relevant to each of these three sets of findings.

Median Rent

A large body of evidence, documented in the book *Homelessness Is a Housing Problem*, supports the conclusion that unaffordable rents are one of the primary drivers of homelessness.

A recent study of the relationship between inequality and homelessness titled, “*A Rising Tide Drowns Unstable Boats: How Inequality Creates Homelessness*,” also finds that median rent is a statistically significant predictor of growth in homelessness across communities. It uses a more rigorous econometric methodology than was used by the GAO to show that the mechanism underlying this correlation is not the rising value of homes *per se*, but rather the percent of rent-burdened low-income renters living in the city.²⁴ Essentially, fast home price growth does not necessarily drive up homelessness as long as everyone’s incomes are rising proportionally.

The exact numbers reported by the GAO study are not accurate for every U.S. region. A \$100 increase in median rent is very different in more expensive markets versus less expensive markets. The statistical approach would have more relevant to Los Angeles if the GAO reported the association between a given *percentage* increase in median rent and homelessness, as percentages can be scaled appropriately to each city.²⁵

Median Wage, Poverty, and Unemployment

The GAO’s inability to find a significant effect of wages, poverty, or unemployment on homelessness likely reflects their statistical approach, rather than a lack of relationship between these variables in the real world.

First, they include both the poverty rate and the proportion of SNAP recipients in the same equation. The SNAP variable *is* a significant predictor of growth in homelessness, indicating that material hardship is associated with lack of shelter. The poverty variable is likely being overshadowed statistically by this other measure of material hardship, and

therefore it is impossible to suggest that poverty is unrelated to homelessness from this equation.²⁶

Second, previous research by the Economic Roundtable demonstrates that unemployment does not have an immediate effect on homelessness, but it does have a significant effect in the long run.²⁷ When people lose their jobs, they dip into savings, ask family and friends for help, file for unemployment insurance, and use any other means possible to continue paying their rent.

These forms of assistance take time to exhaust. Only after people have been unemployed for many months do they typically run the risk of losing their home. Thus, the Economic Roundtable has shown, it is possible to forecast homelessness quite accurately using local unemployment rates—but the forecast must take into account a lag of multiple years. Because the GAO’s equation is only focused on effects within a year or less, it misses this important dynamic.

Third, each of these variables in isolation is unlikely to identify the complex interactions between the housing market and the labor market that result in homelessness. Only when they are measured in relation to the cost of housing does their importance become clear. The study of the relationship between inequality and homelessness mentioned earlier provides more insight into this relationship with a more rigorous econometric model that attempts to identify *causes*, rather than simply correlates, and it concludes that what matters in the labor market is *income inequality*.²⁸

Because income inequality (like rent) can be driven by homelessness or a third omitted factor, this model identifies causation by using a measure of local inequality that changes based on national trends—and therefore is unlikely to be driven by other local factors like homelessness. The resulting effect is a true measure of the effect of changes in inequality on changes in homelessness, and it is significantly positive.

Low wages and poverty *do* matter—but *how* they matter is when they exist in the same local market as high income-earners who drive up the cost of housing, leaving a larger proportion of low-income renters in an unaffordable position. Unfortunately, these same statistics reveal that Los Angeles has relatively high local income inequality—and therefore, high homelessness—compared to the rest of the country.

Finally, as the GAO acknowledges, the median wage does not capture the experience of the workers most likely to fall into homelessness. Recent research from the Economic Roundtable has demonstrated that many homeless individuals are working at some point throughout the year, but they tend to have very low incomes and unreliable jobs with inconsistent work schedules.²⁹ As a result, they cannot assure landlords that they will earn a steady paycheck to cover rent every single month.

These renters earn much lower wages than the median wage—and even when they do earn slightly higher wages, they do not earn them regularly. Thus, while the labor market is a critical factor in a city’s homelessness, the median wage is not the ideal indicator of this relationship. In Los Angeles

County, for example, the rate of workers living below the poverty line is higher than in any other county in California.³⁰ This indicator, far more than the median wage, helps to explain the area's high rate of homelessness.

Mental Health and Evictions

The impacts of mental health and evictions on homelessness elude the GAO, largely due to data constraints. Looking at the literature, however, we can say more than the GAO found about their impact on homelessness.

The study, *Homelessness Is a Housing Problem*, employs data on rates of mental illness and finds that they are very poorly correlated with rates of homelessness. This does not imply that the homeless population does not suffer from high rates of mental illness, nor that homelessness itself has no effect on mental health. Indeed, just as low and inconsistent wages make a person more vulnerable to losing their home, so too does mental illness—and the experience of homelessness, in turn, is seriously traumatic, affecting mental health in a variety of negative ways.

Los Angeles does not have a high rate of homelessness because it has a higher prevalence of mental illness than other cities. Thus, if we want to understand how Los Angeles wound up on a different trajectory than other cities, attributing it to mental illness is less productive than attributing it to the high cost of housing.

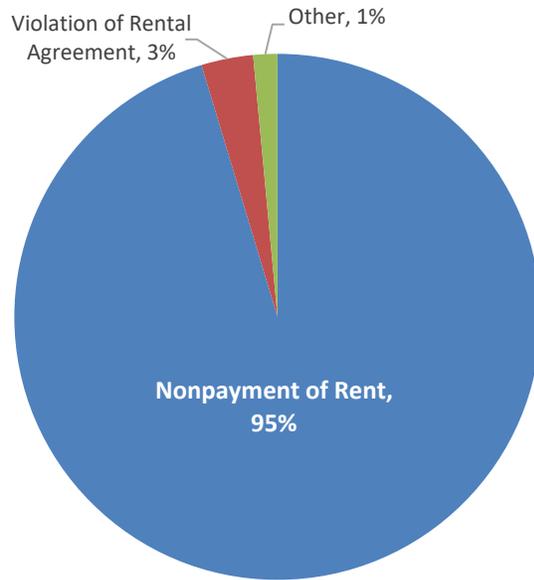
Had those same vulnerable Angelenos with mental health vulnerability lived in a more affordable city, they may still have suffered from mental illness, but they were more likely to do so with a roof over their heads. If it maintains a sufficient stock of affordable housing, a city need not penalize psychologically vulnerable individuals with the double injury of losing their shelter.

At the time of the GAO study, little evidence existed to demonstrate a conclusive empirical link between evictions and homelessness. Since then, new research in a paper titled, “*Eviction and Poverty in American Cities*,” has shown that an eviction increases the probability of experiencing homelessness by 300 percent.³¹ This is not simply a correlate.

Using a similar methodology as the paper mentioned earlier about the link between inequality and homelessness, this analysis measures a plausibly *causal* effect. An increase in evictions is indeed a driver of an increase in homelessness. This is consistent with the evidence compiled above, which shows that an increased cost of housing leads to an increased rate of homelessness.

The connection between lack of income and loss of housing is shown in *Figure 31*. From February 2023 to February 2024, in the City of Los Angeles, 95 percent of eviction filings were caused by “nonpayment of rent.” Thus, when the cost of housing increases and tenants cannot afford it, their likelihood of eviction increases—and therefore, their likelihood of experiencing homelessness rises too.

Figure 31: Causes of Evictions

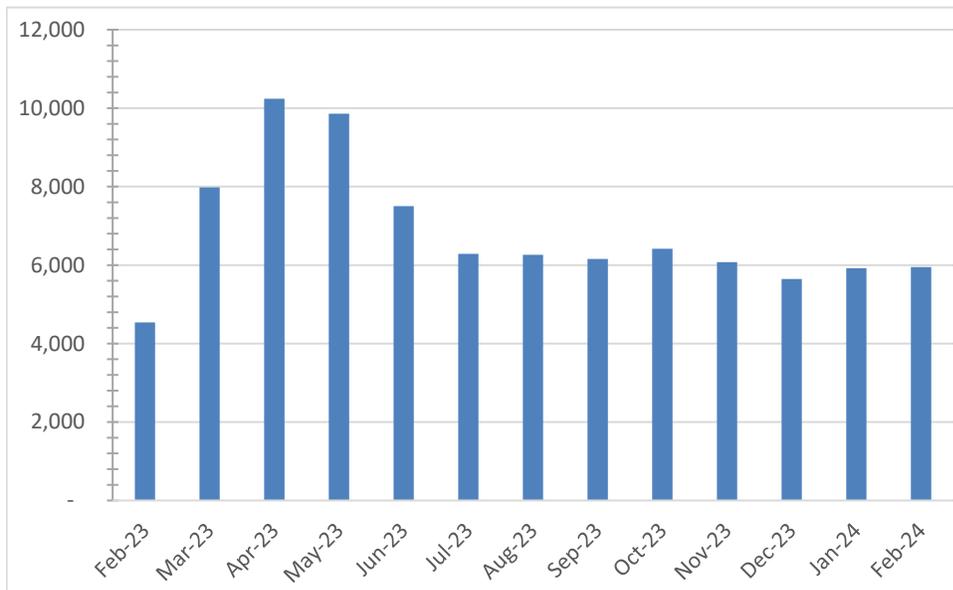


Data source: City of Los Angeles Housing Department, Eviction Notice Workbook.

It is also important to note in *Figure 31* that very few evictions are caused by criminal behavior, disorderly conduct, or any other problematic alleged violations by the tenant. The primary driver of evictions is the rising cost of housing—and thus, dampening this rise should be a top priority in policies to reduce the rate of evictions.

During the pandemic, the eviction moratorium reduced the rate of evictions to record lows. As a result, it is not surprising to find that

Figure 32: Eviction Notices Filed in City of Los Angeles, February 2023 to February 2024



Data source: City of Los Angeles Housing Department, Eviction Notice Workbook.

homelessness did not increase as much as anticipated initially, given the high unemployment at the beginning of the Covid pandemic. Recent research by the Economic Roundtable showed how this policy and other rental assistance and fiscal stimulus programs were successful in preventing the rise of homelessness from being as severe as it otherwise would have been otherwise.³²

Unfortunately, as these policies ended, the eviction rate soared in early 2023 and remained elevated into early 2024, as shown in *Figure 32*. Thus, it is also not surprising that the latest Homeless Count in 2023 reported a much sharper increase in homelessness, bringing it close to the initial forecast released by the Economic Roundtable before those policies were put into place.³³

Findings

- The most frequent explanation that homeless adults in Los Angeles give for their lack of housing is unemployment and lack of money.
- There is a direct connection between loss of income and loss of shelter, but these losses do not appear to occur simultaneously. Disconnection from work is a degenerative dynamic – less work, less earnings, less stable living conditions, and further disconnection from work.
- One-quarter of renters in the Los Angeles region have household incomes under \$25,000. Eighteen percent of these households say that it is extremely likely that they will be evicted in the next two months.
- Rent costs that exceed what tenants can pay is a primary cause of homelessness.
- Increases in income inequality lead to increases in homelessness because they simultaneously drive up the cost of housing and the percent of low-income renters who cannot afford that housing.
- There is a high rate of homelessness in Los Angeles primarily because of this interaction between the housing market and the labor market—namely, the high cost of housing and the high rate of working poverty.
- Los Angeles has relatively high local income inequality—and therefore, high homelessness—compared to the rest of the country.
- An increase in evictions is a driver of an increase in homelessness.
- The primary driver of evictions is the rising cost of housing.
- The eviction moratorium, rental assistance and fiscal stimulus programs were successful in preventing the rise of homelessness from being as severe as it would have been otherwise.



7. Financial Stress of RSO Landlords by Building Size

*Photo credit:
Economic Roundtable*

Scale of RSO Ownership

Rent-stabilized units are owned in investment and management settings that range from small landlords for whom rental income is augmented by a day job to corporations with large real estate portfolios that are managed by full-time professional staff. It is important to understand how the scale of ownership affects the financial outcomes of RSO landlords.

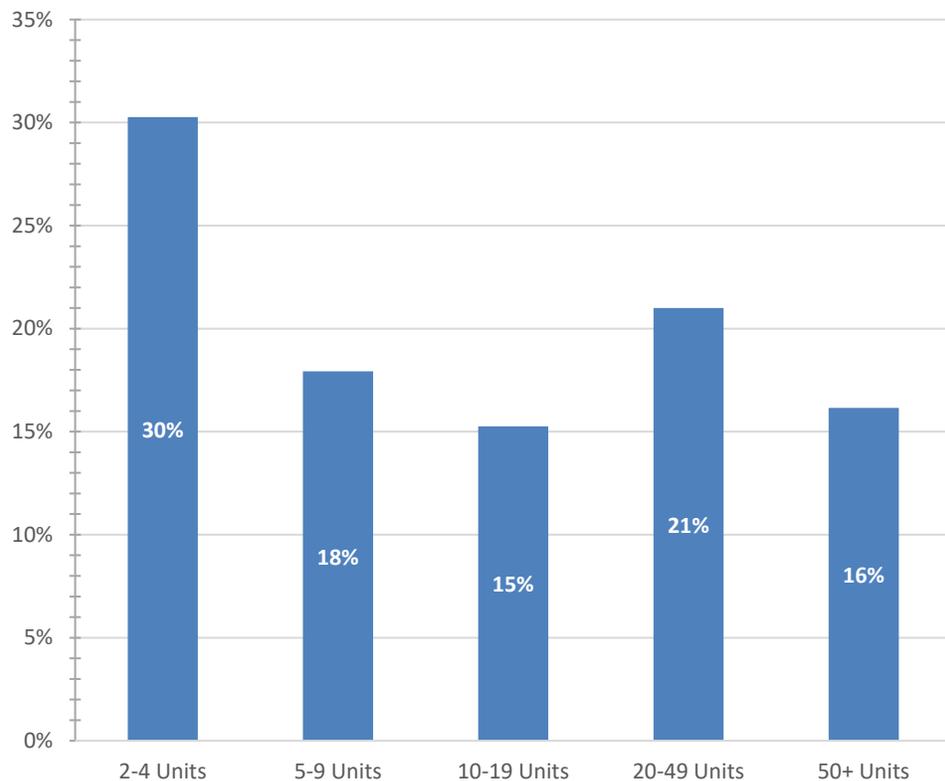
Thirty percent of RSO units are on parcels with two to four units, as shown in *Figure 33*.³⁴ Owners of these properties commonly called mom-and-pop landlords.

The inventory of RSO units in the other four larger size categories is almost evenly distributed, as shown in *Figure 33*. With condominiums excluded, the typical (median) RSO unit is on a property with 17 units. These fall within the category of properties with 10 to 19 units, which account for 15 percent of RSO units.

The second largest size category is properties with 20 to 49 units, which accounts for 21 percent of all RSO units.

Sixteen percent of RSO units are on the largest properties, with 50 or more units.

Figure 33: Distribution of RSO Units by Number of Units on Parcel



Data source: City of Los Angeles Housing Department RSO Rent Registry. City of Los Angeles Housing Department. 2024. Dataset A: RSO Inventory; Los Angeles County Assessor. 2023. SBF Abstract (DS04). Condominium units excluded.

RSO Unit Size based on Building Size

The typical unit on small, or mom-and-pop, RSO properties has more bedrooms than any other ownership category as well as the overall average unit size for the RSO inventory, as can be seen in *Figure 34*.

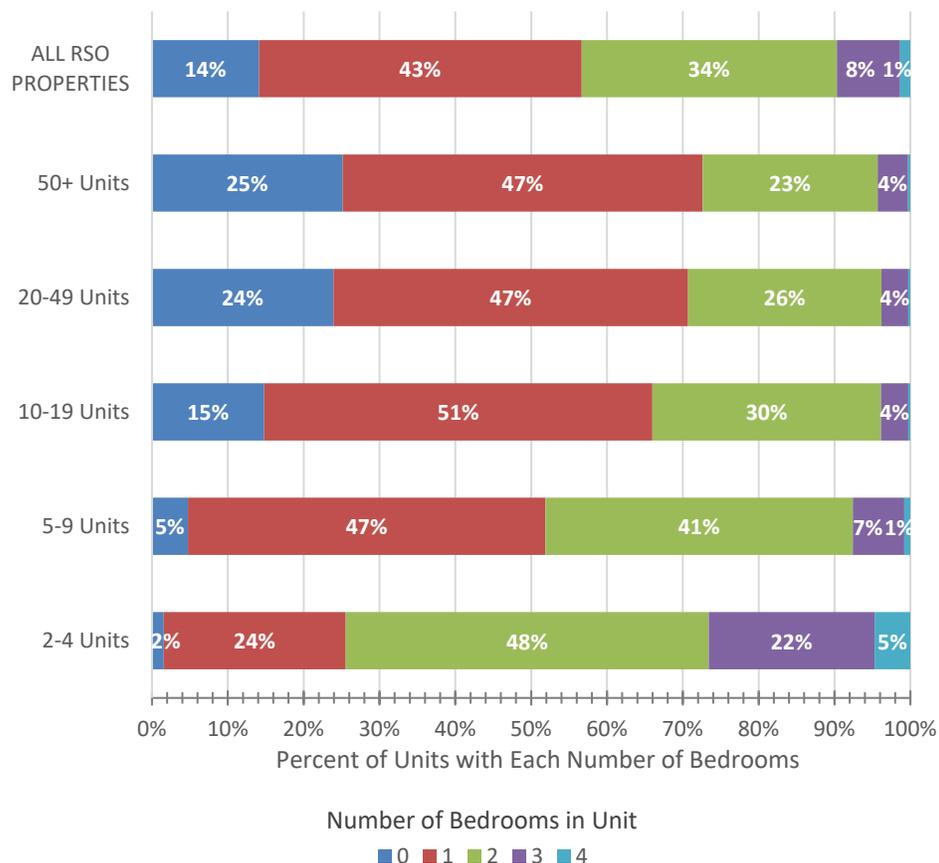
The average number of bedrooms in different RSO building size categories decreases progressively from an average of 2.04 bedrooms in buildings with 2 to 4 units, 1.52 in buildings with 5 to 9 units, 1.23 in buildings with 10 to 19 units, 1.10 in buildings with 20 to 49 units, and 1.07 bedrooms in buildings with 50 or more units.

The overall RSO housing inventory has an average of 1.4 bedrooms per unit.

The fact that mom-and-pop landlords provide units with an average of 46 percent more bedroom space than the overall average for the RSO inventory needs to be taken into account in comparing the rent received for units in different ownership categories.

The larger units typically owned by small landlords have more rental value because they can accommodate larger households.

Figure 34: Number of Bedrooms per RSO Unit by Number of Units on Parcel



Data source: City of Los Angeles Housing Department RSO Rent Registry. Condominium units excluded.

RSO Rents based on Building Size and Unit Size

The average rent in 2023 for all RSO units was \$1,633 per month, as shown in *Figure 35*. Broken out by the number of bedrooms in units, this comes to an average of \$1,211 per bedroom.

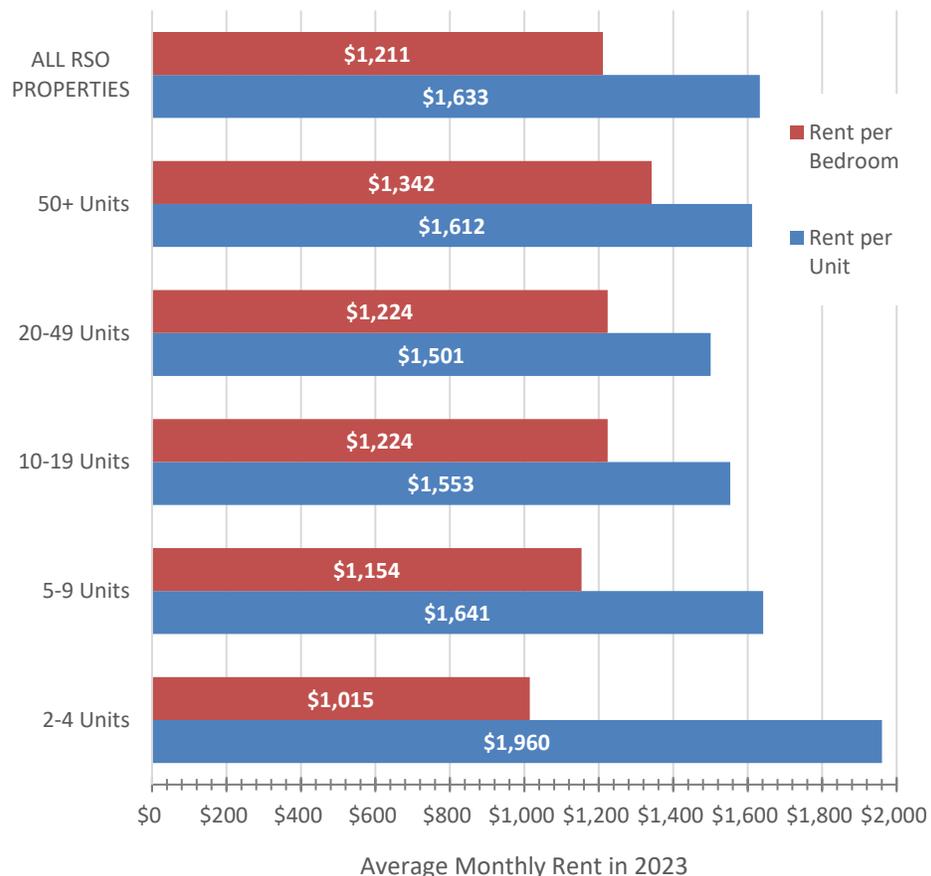
Rent per *unit* as well as per *bedroom* is similar across ownership categories, except for small landlords with two to four units.

Rent per *unit* is within plus or minus six percent of the overall average for the RSO inventory, except for small landlords with two to four units. The average rent for these units is 20 percent higher than for the total RSO inventory.

The amount of rent per *bedroom* provides an even-handed comparison across ownership categories, given the larger average size of units owned by small RSO landlords. Rent per bedroom is within plus or minus three percent of the overall average for the RSO inventory except for small landlords.

The average rent per *bedroom* for units owned by landlords with two to four units is 16 percent lower than the overall average: \$1,105 compared to \$1,211 per *bedroom*.

Figure 35: RSO Rent per Unit and per Bedroom by Building Size



Data source: City of Los Angeles Housing Department RSO Rent Registry. Condominium units excluded.

Length of Occupancy

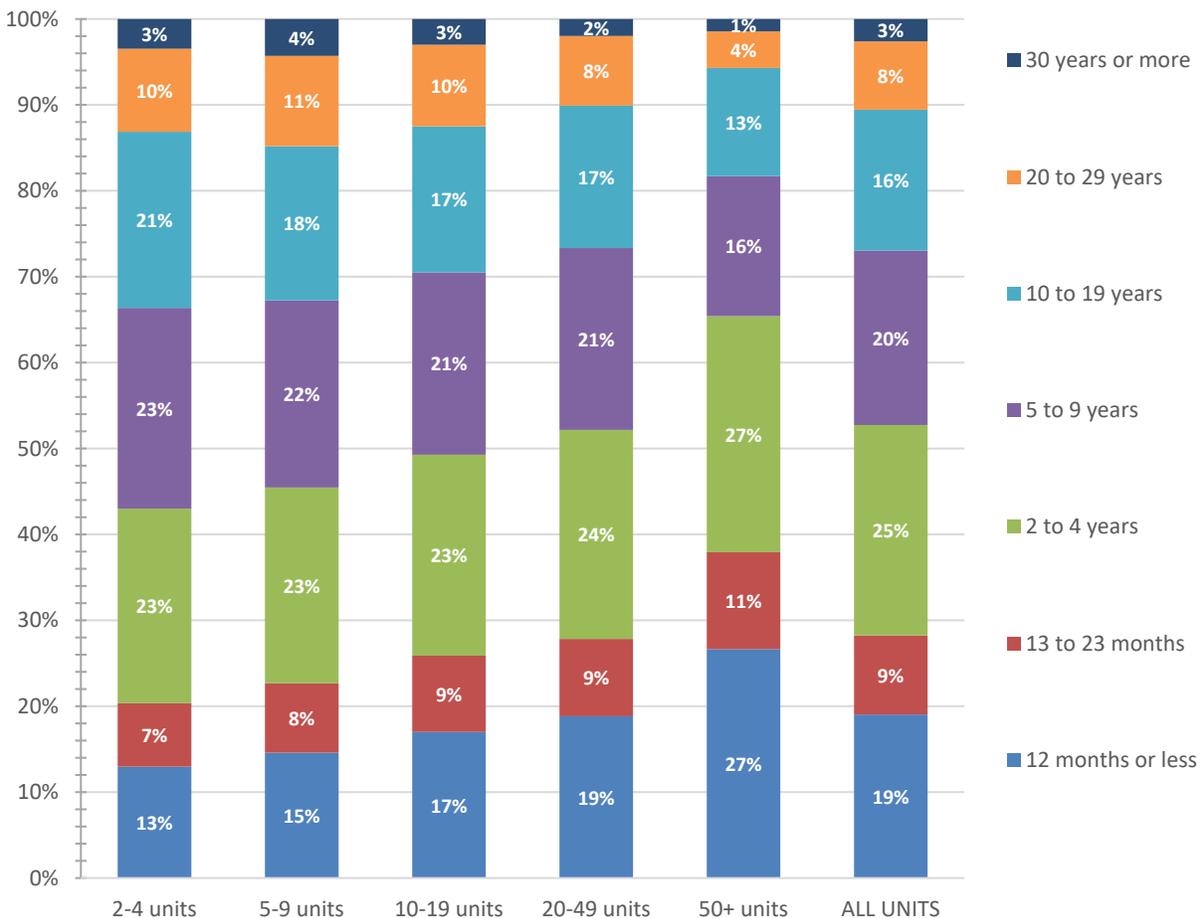
The length of time that RSO tenants have been in their units appears to vary inversely with ownership size, as shown in *Figure 36*.

Tenant turnover reduces landlords' revenue and profit. First, because vacant units do not bring in rent. Second, because landlords usually have expenses for refurbishing units and marketing them for new tenants.

Fifty-seven percent of tenants in units owned by small landlords are reported by the Census Bureau to have been in their units for five or more years.³⁵ This compares to only 47 percent of tenants in all RSO units reaching the five-year mark.

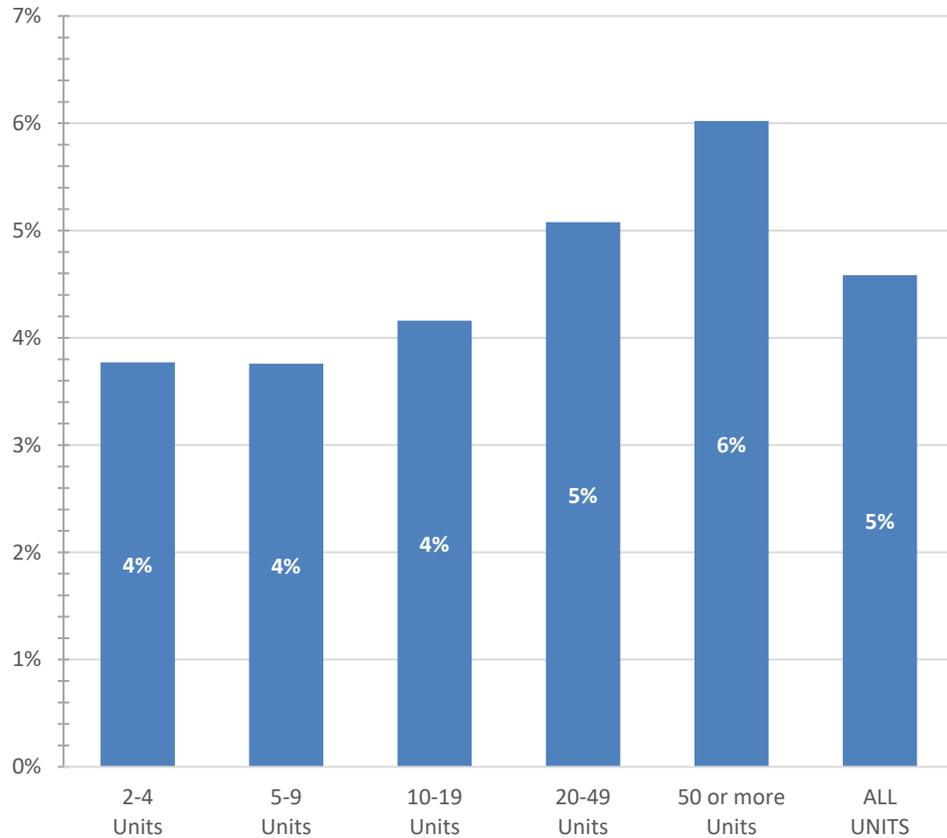
Duration of occupancy decreases progressively as building size increases. Fifty-seven percent of tenants in RSO buildings with four or less units have occupied them for five or more years; 55 percent of tenants in buildings with five to nine units, 51 percent of tenants in buildings with 10 to 19 units; 48 percent of tenants in buildings with 20 to 49 units; and only 35 percent of tenants in buildings with 50 or more units.

Figure 36: Length of Time RSO Renters Have Occupied their Units by Building Size



Data source: U.S. Census Bureau Public Use Microdata Sample 2018-2022, average of all five years.

Figure 37: Percent of Unoccupied RSO Units Available for Rent by Building Size



Data source: U.S. Census Bureau Public Use Microdata Sample 2018-2022, average of all five years.

The person-to-person relationship between tenants in small buildings and their mom-and-pop landlords appears to make tenants more inclined to stay where they are.

Vacancy Rate

Vacancy Rates Reported by Census Bureau

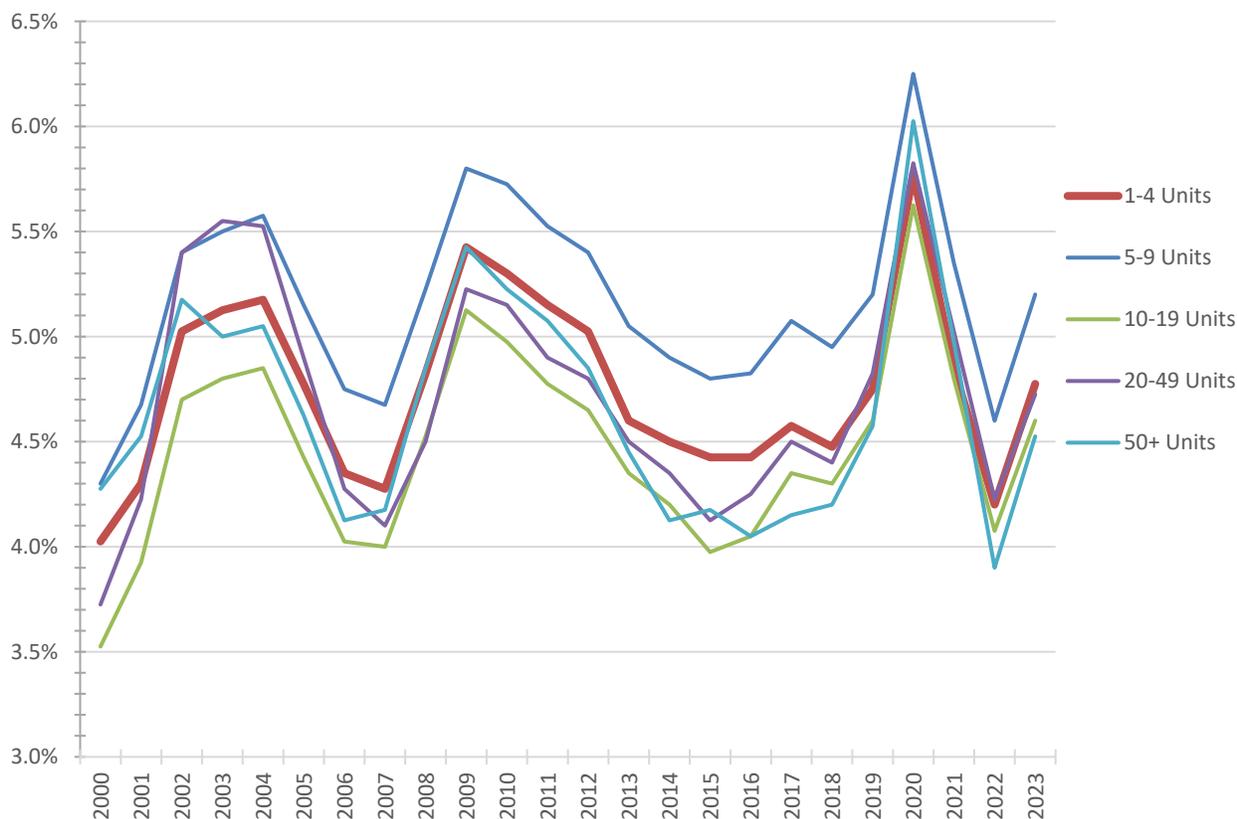
Vacancy rates are the result of how often tenants leave their units and how long it takes to bring in new renters to replace them. The average vacancy rate reported by the Census Bureau for all Los Angeles RSO units from 2018 to 2022 was five percent, as shown in *Figure 37*.

Vacancy rates appear to increase as RSO ownership size increases, ramping up from four percent for buildings with two to four units to six percent for buildings with 50 or more units.

Vacancy Rates Reported by CoStar

CoStar collects and aggregates information about the real estate market based on commercial listings and calls to property owners. Their data is likely to

Figure 38: Average Annual Vacancy Rate in RSO Buildings by Size, CoStar Data



Data source: CoStar Group data for RSO properties in the City of Los Angeles. Building size categories set by CoStar.

under-represent mom-and-pop landlords and over-represent the middle and upper tiers of building sizes in the real estate market. Their information is likely to be most accurate for larger landlords, but it also provides a second frame of reference for comparing the vacancy rates for different sizes of apartment buildings.

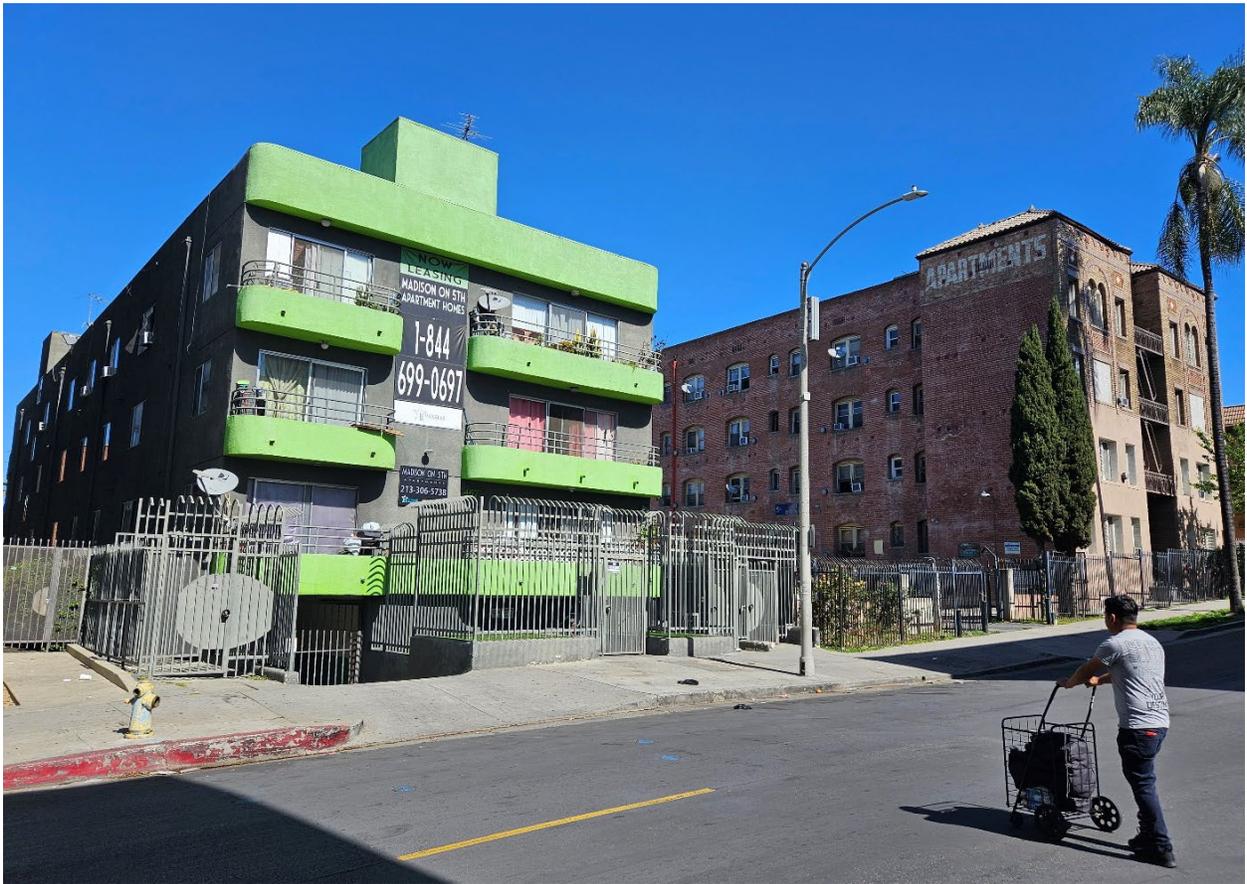
From 2020 to 2023, CoStar data shows that vacancy rates for small buildings with one to four units were very similar to rates for all other ownership sizes, except buildings with five to nine units, which had fractionally higher vacancy rates. This can be seen in *Figure 38*.

Findings

- Small landlords with two to four units account for the plurality of the RSO housing inventory, 30 percent.
- The typical (median) RSO unit is in a building with 17 units.
- The units owned by small landlords with one to four units typically have more bedrooms than all other size classes of ownership. They

provide an average of 46 percent more bedroom space than the overall average for the RSO inventory.

- Seventy-five percent of units in buildings with two to four units have two or more bedrooms, compared to 34 percent of units in buildings with five or more units.
- The average rent for units owned by small landlords is higher than the average rent for any other building size group and 20 percent higher than for the overall RSO inventory.
- When rents are compared on the basis of rent per bedroom, small landlords receive 16 percent less rent per bedroom than the overall average for RSO units.
- Fifty-seven percent of tenants in units owned by small landlords are reported by the Census Bureau to have been in their units for five or more years. This compares to only 47 percent of tenants in all RSO units reaching the five-year mark, and is longer occupancy than any other ownership group. Less tenant turnover reduces lost revenue from empty units. However, it also reduces the frequency with which rents can be vacancy decontrolled and re-rented at market rates.
- Based on vacancy data from the Census Bureau that encompasses the entire RSO inventory, vacancy rates increase with ownership size, and small landlords have the lowest vacancy rate. The person-to-person relationship between tenants in small buildings and their mom-and-pop landlords appears to make tenants more inclined to stay where they are.
- Vacancy rate data from CoStar shows small landlords to have vacancy rates that closely match, or lower than, other ownership groups.
- RSO landlords have less tenant turnover than non-RSO landlords, which reduces lost rent when units are vacant as well as costs to refurbish units for new tenants.
- Operating expenses may or may not be higher per unit for smaller buildings, but this may be offset by self-management, which would reduce cash outlays for managing small RSO buildings. No empirical data about these possible differences in operating costs is available.
- Smaller RSO landlords appear to receive higher rent per unit, although lower rent per bedroom, and have lower vacancy rates than larger RSO landlords. There is not clear evidence that they have greater financial stress than larger landlords.



8. Short-Term and Long-Term Impact of the Covid Pandemic on Landlords

*Photo credit:
Economic Roundtable*

Overview

Landlords experienced a sharp increase in non-payment of rent, which they addressed by granting more rent extensions, charging less rent fees, deferring maintenance, and listing their properties for sale. This assessment is based on a series of surveys conducted during the Covid pandemic.

Smaller landlords were more likely to experience non-payment of rent, and larger landlords were more flexible in managing this problem, for instance, by granting rental extensions or forgiving late rent fees. Landlords were least likely to offer accommodations to renters of color for the same level of non-payment of rent.³⁶ Rental assistance programs were significantly helpful to tenants, but they did not reach as many tenants as administrators often hoped due to strong resistance from landlords.³⁷

In Los Angeles and Orange Counties, the U.S. Census Bureau's Pulse Survey shows that rental non-payment has been declining from 2020 to the end of 2023. Meanwhile, CoStar data show that multi-family vacancy rates rose dramatically at the start of the pandemic but fell soon thereafter.

Today, there is a large gap in vacancy rates between RSO properties and non-RSO properties, with RSO properties returning to their pre-pandemic historical average and non-RSO vacancy rates remaining elevated. Thus, it appears that RSO properties have returned to their previous revenue-generating capability.

Short-Term Impact of Pandemic on Landlord Finances

During the Covid pandemic, several surveys asked landlords to report how their tenants had been impacted by financial distress, how those losses had affected the financial viability of their investments, how they had changed their property management strategies to cope with the lessened cash flows, and what role emergency assistance from the government might have played. Here, we summarize these findings, especially as they illuminate the experiences of Los Angeles and vulnerable communities most likely to benefit from the Rent Stabilization Ordinance.

From February to April 2021, a team of researchers—from the Bloomberg Harvard City Leadership Initiative, the Joint Center for Housing Studies of Harvard University, and the Housing Initiative at the University of Pennsylvania—surveyed 2,930 residential landlords across 10 U.S. cities, including Los Angeles.³⁸ From their findings, we identify the following conclusions as most important for understanding the experience of RSO landlords in LA:

1. In Los Angeles, 12 percent of landlords received less than 90 percent of rent charged in 2019 before the pandemic. In 2020, that rate increased to 45 percent of landlords. This non-payment was more prevalent than in Akron, Indianapolis, Minneapolis, San Jose, and Racine, and it was less prevalent than in Albany, Philadelphia, Rochester, and Trenton.

Thus, in this sample, Los Angeles was roughly in the middle of the pack.

2. In Los Angeles, two percent of landlords received less than 50 percent of rent charged in 2019 before the pandemic. In 2020, that rate increased to 11 percent of landlords. Similarly, to the 90 percent metric, this more severe level of non-payment was more prevalent than in Akron, Indianapolis, Minneapolis, San Jose, and Racine, and it was less prevalent than in Albany, Philadelphia, Rochester, and Trenton.
3. Smaller landlords (1-5 units owned) experienced more non-payment of rent from their tenants—both *before* and *during* the pandemic.
4. Mid-sized landlords (6-19 units owned) experienced the greatest *increase* in non-payment of rent from their tenants *during* the pandemic.
5. From 2019 to 2020, landlords increased their use of the following strategies to address the non-payment of rent: rental concessions, forgiving back rent, deferring maintenance, and listing properties for sale. Specifically, in Los Angeles the changes from before the pandemic in 2019 to during the pandemic in 2020 included:
 - In 2019, 9.5 percent of landlords granted rent extensions. This rate increased to 59.5 percent in 2020.
 - In 2019, 26.5 percent of landlords charged fees for late rent. This rate decreased to 4.5 percent in 2020.
 - In 2019, 6.5 percent of landlords deferred maintenance. The rate increased to 35.0 percent in 2020.
 - In 2019, 1.0 percent of landlords listed their properties for sale. The rate increased to 11.5 percent in 2020.
6. Large landlords (20 or more units owned) had the “most adaptability in managing” and coping with non-payment of rent.
7. Non-payment of rent was most prevalent among renters of color, and these renters were also the least likely to experience positive responses from landlords, such as rental concessions or forgiveness of back rent. This negative experience with landlords was not simply due to the non-payment of rent. Renters of color were significantly less likely to receive forbearance from landlords *even if they had the same level of non-payment of rent* as European American renters.
8. Nationally, the proportion of landlords filing evictions against tenants did not change from 2019 to 2020 (15 percent of landlords in both years), despite eviction moratoria being instituted in 2020. The eviction moratorium was slightly more successful in Los Angeles, where the rate

of landlords initiating evictions declined from 8.5 percent in 2019 to 6.5 percent in 2020.

To address these negative experiences, federal, state, and local governments enacted a series of emergency assistance programs. From August to October 2020, a team of researchers—from the Housing Initiative at the University of Pennsylvania, the NYU Furman Center, and the National Low Income Housing Coalition—surveyed program administrators who were distributing emergency rental assistance across 40 states.³⁹ They found wide variation in program design, tenant eligibility, and landlord responsiveness.

- **Program design:** The programs delegated control of implementation to a wide variety of institutions across the country. In 48 percent of cases, nonprofit organizations reviewed and selected the applicants. In 21 percent, city, county, or state housing departments played this role. In 12 percent of cases, including Los Angeles, multiple institutions worked together to review and select the applicants.⁴⁰
- **Tenant eligibility:** There was no consensus regarding the level of income that should make a tenant eligible for emergency rental assistance. In 25 percent of programs, the maximum eligible income was set at or below 60 percent of area median income (AMI). In 57 percent of programs, the maximum eligible income was set between 80 and 100 percent of AMI. In the remaining 18 percent of programs, the maximum eligible income was set between 120 and 150 percent of AMI. Additional eligibility criteria included an income loss specifically due to the Covid pandemic (85 percent), no other housing subsidies (37 percent), legal U.S. residency (21 percent), “insufficient savings to cover rent” (20 percent), “was current on rent before the onset of Covid-19” (18 percent), and participation in other low-income housing programs (7 percent).
- **Los Angeles design:** The Emergency Rental Assistance Program in Los Angeles covered up to fifteen months of rental arrears.⁴¹ The eligibility criteria were:
 - Residence in the City of Los Angeles, regardless of immigration status.
 - One or more individuals within the household have experienced a loss of employment, reduction in household income, or incurred significant costs due to COVID-19 between April 2020 and March 2021.
 - Have unpaid rent due to their current landlord for any month between April 1, 2020, through March 2021.
 - Household income is at or below 80 percent of the area median income (AMI).
- **Los Angeles outcomes:** Rental assistance was approved for approximately 127,000 City of Los Angeles households, which received approximately \$1.8 billion in rental assistance.⁴²

- **Landlord responsiveness:** Programs also instituted requirements on landlords in 98 percent of cases. The most common requirement was “a commitment not to evict the participating tenant” (78 percent), followed by “forgiveness of rent in arrears” (28 percent), “a current rental license” (13 percent), “being registered to a local rent registry” (5 percent), and “a commitment to freeze rent” (3 percent). Faced with these requirements, however, many landlords chose not to participate. Nearly half of programs indicated that this lack of landlord participation was a significant problem.

The lack of landlord participation is concerning because the evidence is clear that these programs bestowed significant benefits on tenants in need. In Philadelphia, where one of the most in-depth studies was conducted, researchers found that emergency rental assistance resulted not only in a reduction in rent arrears but also a reduction in debt and anxiety.⁴³

Rental Non-Payment During and After the Pandemic

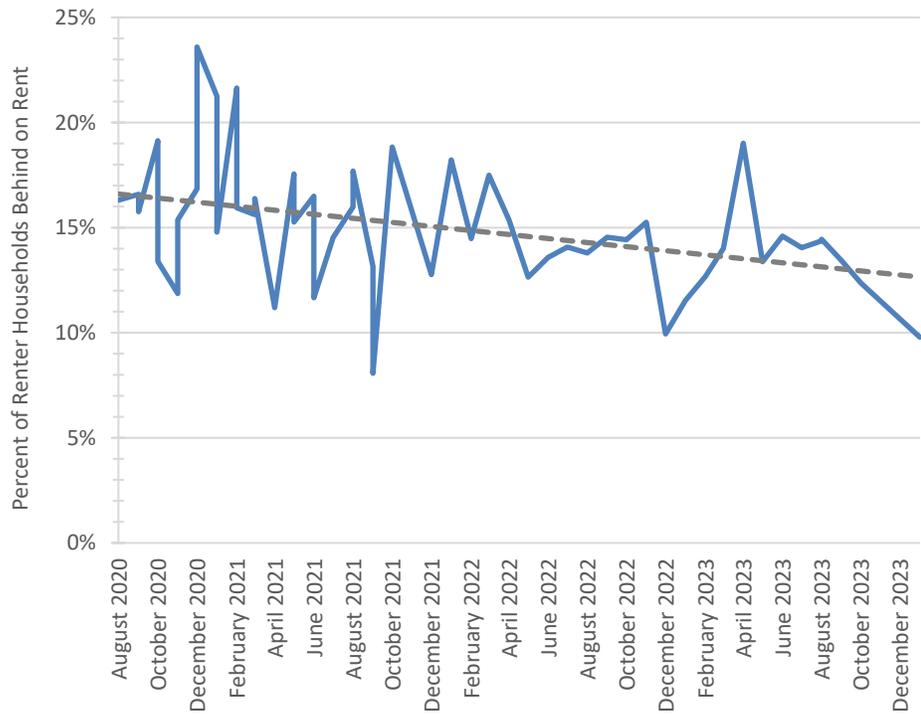
In Los Angeles and Orange Counties, non-payment of rent was most pervasive in December 2020, nine months into the Covid pandemic. The government had begun reporting this metric in August via the Pulse Survey administered by the U.S. Census Bureau. The survey typically took approximately two weeks to complete, allowing us to see how rental non-payment changed month-by-month.

The percent of renter households that were behind on rent, which peaked at 24 percent in the December 9 to 21 period of 2020, is shown in *Figure 39*. Since that time, it has been trending downward. Its latest reading, 10 percent in January 2024, is near the lowest point since the Pulse Survey began.

Unfortunately, we cannot observe the same metric before the pandemic, but we can conclude that the high distress of the early pandemic months is clearly over—and has been receding for quite some time. It did not persist near its highest point for long, falling as low as 11 percent only four months after the peak.

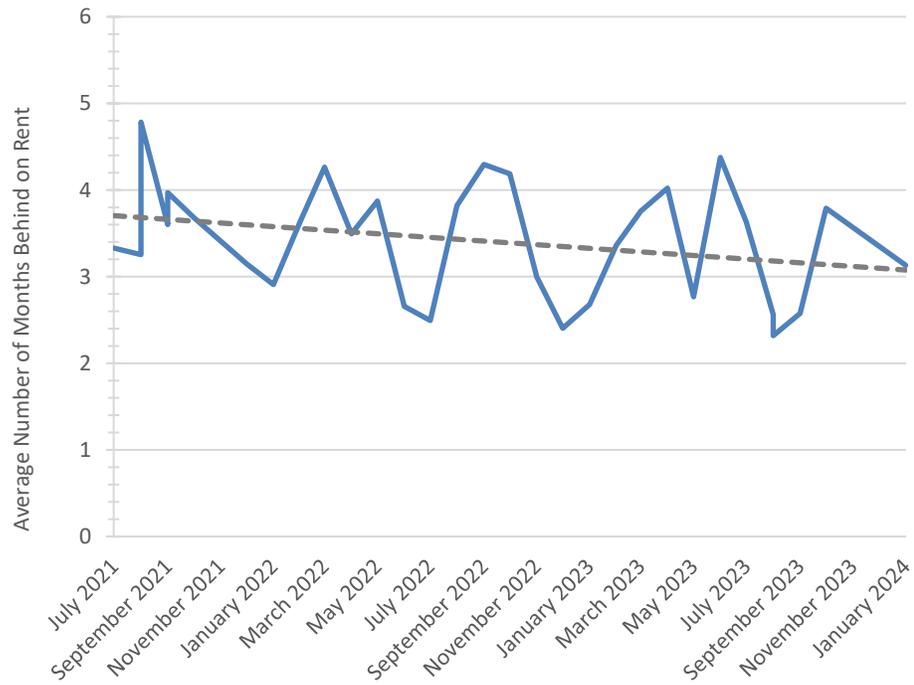
The pervasiveness of non-payment only tells part of the story. Some households caught up on back rent quickly, and others persisted long after the initial missed payment. Thus, it is also important to consider the severity of non-payment, measured in *Figure 40* as the average number of months behind on rent for the renters who have missed at least one payment. This metric too has been declining since the early months of the Pulse Survey.

Figure 39: Percent of Renter Households in Los Angeles and Orange Counties That Are Behind on Rent, 2020-2024



Source: U.S. Census Bureau.

Figure 40: Average Number of Months Behind on Rent for Households in Los Angeles and Orange Counties, 2020-2024



Source: U.S. Census Bureau.

Among renters not caught up on rent, the amount of unpaid rent peaked as early as August 2021, with 4.8 months unpaid, essentially indicating that the average delinquent tenant in Los Angeles and Orange Counties stopped paying rent as soon as the pandemic began and remained behind until that point. From then on, many tenants started catching up on back rent, likely due to the infusion of cash from federal, state, and local stimulus and emergency rental assistance programs. The latest estimate, 3.1 months unpaid, is still elevated relative to several low points during the four years of the survey, suggesting that the remaining delinquent households are still experiencing some distress.

Another data source, the Survey of Household Economics and Decisionmaking (SHED) conducted by the Federal Reserve Board, reveals details about the composition of these households who are behind on rent.

Generally, households behind on rent during the pandemic (i.e. in 2021) had similar characteristics to households behind on rent before the pandemic (i.e. in 2019). Namely, they had similar “education, age, parental education, and disability status,” and they “received unemployment income and applied for rental assistance at similar rates and owed similar amounts of back rent,” according to an analysis from Federal Reserve researchers.⁴⁴

However, the researchers found that most households that were behind on rent in 2021 *became* behind on rent during the pandemic. In other words, it was a new phenomenon, not a continuation of financial distress that preceded the pandemic. African American and Latino households had a greater likelihood of falling behind on rent during this time, compared to European American households, due to the lower average incomes and other economic vulnerabilities experienced by these households of color.

Long-Term Impact of Pandemic on Vacancy Rates

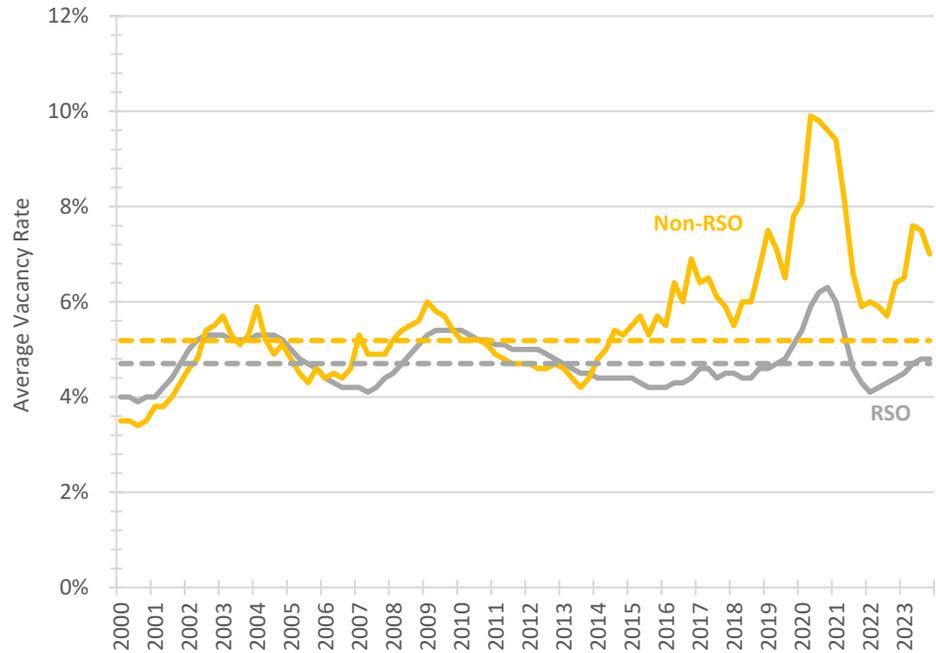
As non-payment occurrences decline, landlord returns depend less on tenant creditworthiness and more on occupancy. So long as landlords can collect rent, what matters most for revenue generation is how many units are filled with tenants. Historically, RSO and non-RSO properties have performed similarly in filling units, as shown in the vacancy rates in *Figure 41*.

From 2000 to 2013, the average vacancy rates in both types of multi-family properties fluctuated in sync, according to data from CoStar. Beginning in 2014, they diverged, with RSO vacancy rates remaining at or below their historical average and non-RSO vacancy rates climbing upward from 4 percent to a peak of 10 percent in 2020.

At this pandemic peak, RSO vacancy rates increased too, but not nearly as much as the non-RSO rate: only six percent. This is consistent with industry and news reports at the time indicating that many Americans were moving—to larger homes, to join family members or significant others, from cities to suburbs—to adapt to the pandemic and the work-from-home shift.

For both property types, vacancy rates decreased precipitously in 2021 and 2022, as the economy rebounded and the demand for housing grew rapidly.

Figure 41: Average Vacancy Rates for Multi-family Properties, 2000-2023



Source: CoStar.

However, the gap between RSO and non-RSO vacancy rates has persisted to today, with the latest estimate in the fourth quarter of 2023 showing 5 percent vacancy in RSO properties and 7 percent vacancy in non-RSO properties.

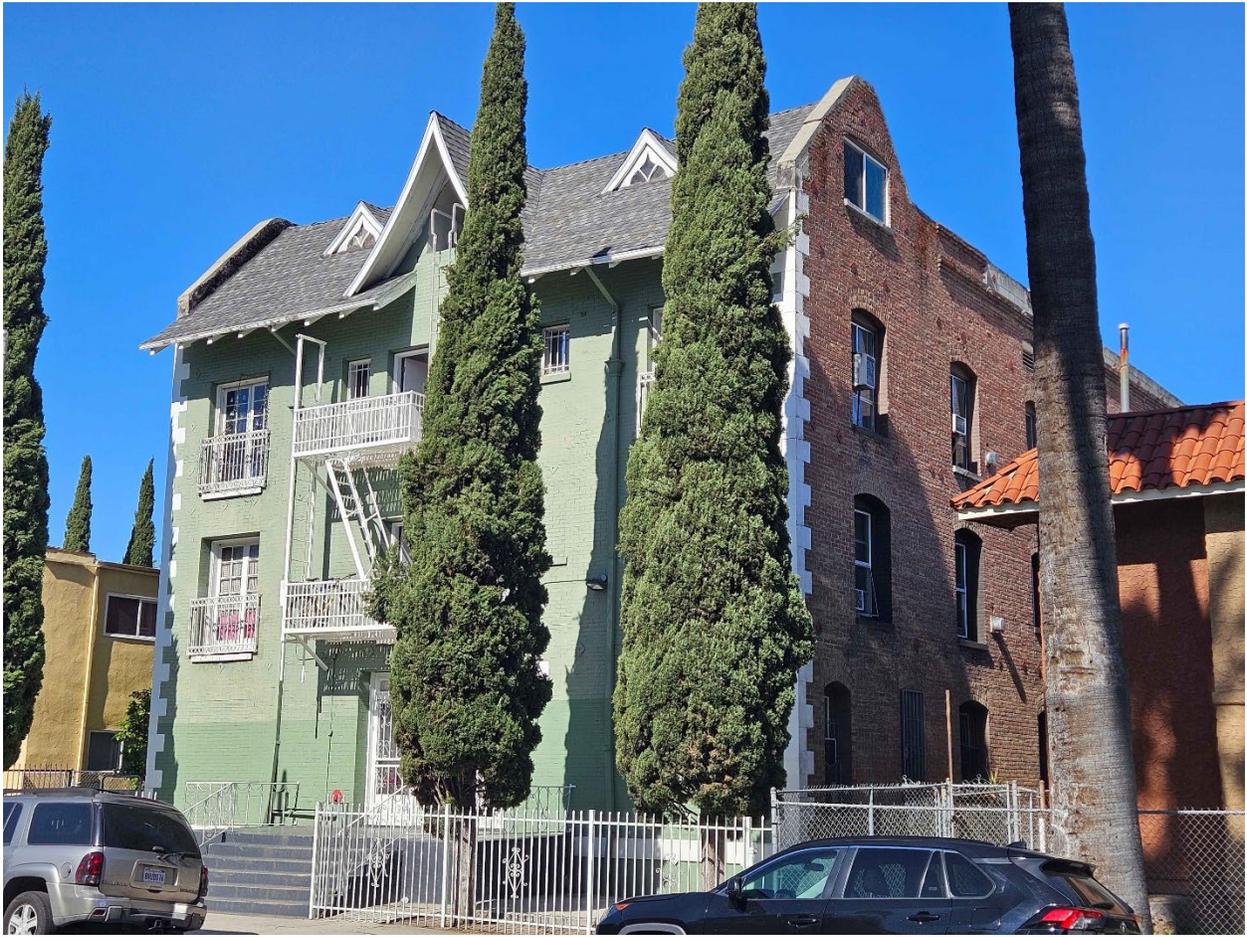
Comparing these solid lines to the dotted lines in *Figure 18*, we can see how these current vacancy rates compare to their pre-pandemic historical averages. RSO properties have returned to this historical average of five percent, while the non-RSO vacancy rate of seven percent is approximately two percentage points above its historical average.

Two conclusions emerge from this analysis: First, since 2014, RSO properties have been far more successful in filling the average unit than non-RSO properties. This low turnover is likely due to the value that tenants find in rent-restricted units as rents and property values have risen in recent years. Thus, despite earning lower rents for comparable units, on average, RSO landlords receive the compensating benefit of lower turnover costs, more stable revenue, and proportionally more revenue-generating units.

The second conclusion is that the pandemic has had a more lasting negative effect on occupancy in non-RSO properties, where vacancy rates remain elevated. In contrast, the average RSO landlord is experiencing a similar level of vacancies as their historical average, indicating little remaining negative impact on immediate revenue generation from the pandemic.

Findings

- Landlords experienced a sharp increase in non-payment of rent during the Covid pandemic, which they addressed by granting more rent extensions, charging less rent fees, deferring maintenance, and listing their properties for sale.
- Smaller landlords were more likely to experience non-payment of rent, and larger landlords were more flexible in managing this problem, for instance, by granting rental extensions or forgiving late rent fees.
- Landlords nationwide were least likely to offer accommodations to renters of color for the same level of non-payment of rent.
- Rental assistance programs throughout the U.S. were significantly helpful to tenants, but they did not reach as many tenants as administrators often hoped due to strong resistance from landlords. However, in the City of Los Angeles, rental assistance was paid directly to tenants whose landlords declined to participate.
- In Los Angeles and Orange Counties, rental non-payment has been declining from 2020 to the end of 2023.
- Approximately 13 percent of renter households in Los Angeles and Orange Counties are estimated to currently be behind on rent, with an average of 3.1 months unpaid, based on the Census Bureau's household surveys.
- Since 2014, RSO properties have been far more successful in filling the average unit than non-RSO properties. This low turnover is likely due to the value that tenants find in rent-restricted units as rents and property values have risen in recent years.
- Despite earning lower rents for comparable units, on average, RSO landlords receive the compensating benefit of lower turnover costs, more stable revenue, and proportionally more revenue-generating units.
- The pandemic has had a more lasting negative effect on occupancy in non-RSO properties, where vacancy rates remain elevated.



9. Market-Rate Rents, Restricted Rents, and Inflation

*Photo credit:
Economic Roundtable*

Overview

Rent-stabilized (RSO) multi-family properties in Los Angeles offer units for approximately \$900 less per month than non-RSO multi-family properties, based on data from CoStar.⁴⁵ From 2015 to 2024, however, asking rents grew faster for RSO properties (24.1 percent, compared to 15.6 percent for non-RSO properties), likely reflecting strong demand for protection against high rent hikes in an increasingly expensive market, as reflected in low vacancy rates.

This rental growth is approximately the same rate as the inflation of all other (non-housing) goods and services over this period. However, using data from Zillow, we find that all residential properties—both single-family and multi-family—across the Los Angeles metropolitan area experienced an increase in rent that exceeded total inflation nationally and in Los Angeles.

This analysis of the real estate market relies on commercial data reported by property owners. Elsewhere in this report, self-reported data collected by the Census Bureau from renters is also presented. The Census Bureau is likely to obtain more complete information from low-income renters, but with the possible drawback of imprecision in the knowledge and memories of renters. The commercial data presented in this section are likely to be more accurate, but with the potential drawback of over-representing the middle and upper tiers of the real estate market. With both types of data, the trends that are shown are at least as important as the absolute numbers.

Estimates of Average Rent Growth

Rental data collection is imperfect. Unlike the transaction price for purchasing a home, the price of renting a housing unit is not reported to most local governments. Instead, private data collectors attempt to survey a representative sample of the population of rented units in two ways: (1) by creating a website that landlords can use as a marketplace to advertise vacant units and input the prices for tenants to see and (2) by contacting landlords and inquiring about the rental prices.

The first approach is generally used by Zillow, which then reports the average listed rent per unit by metropolitan area on their publicly available data site.⁴⁶ The two approaches together are used by CoStar, which owns several rental listing websites used by landlords and provides data access to academic researchers at the building level, neighborhood level, and city level.

Neither company claims to measure average rental prices with perfect precision—and in fact, because they survey different but overlapping populations, they both provide useful estimates. We therefore use both sets of estimates here to understand the variety of trajectories along which different rental housing units have evolved in recent years.

According to these datasets, the average effective asking rent per unit in Los Angeles was estimated to be between \$1,803 and \$1,913 in the first quarter of

2015, as shown in *Figure 42*. By the fourth quarter of 2023, these estimates had increased to the \$2,151 to \$2,879 range.

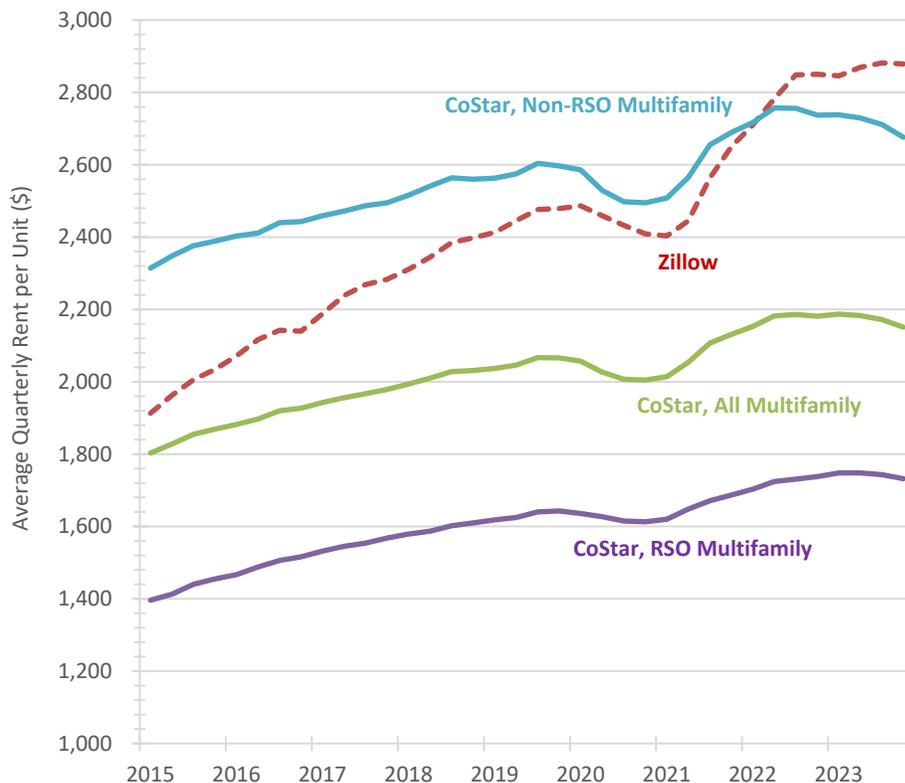
The Zillow estimates were higher, possibly because they used a larger sample of all municipalities in the metropolitan area, while CoStar reported only rents for units located within the City of Los Angeles. The Zillow sample also includes both single-family and multi-family properties, while CoStar focuses on multi-family properties.⁴⁷

It appears that either single-family properties or properties located in the surrounding municipalities drove rental estimates higher than solely multi-family rents within the City of Los Angeles.

Because CoStar allows researchers to filter buildings by age, it is possible to compare properties built before 1978, which are covered by the rent stabilization ordinance (RSO), versus properties built after 1978, which are generally not rent-stabilized.⁴⁸ Not surprisingly, the non-RSO multi-family properties are significantly more expensive, with an average rent per unit growing from \$2,314 to \$2,676 over these nine years, compared to growth from \$1,396 to \$1,732 for RSO properties.

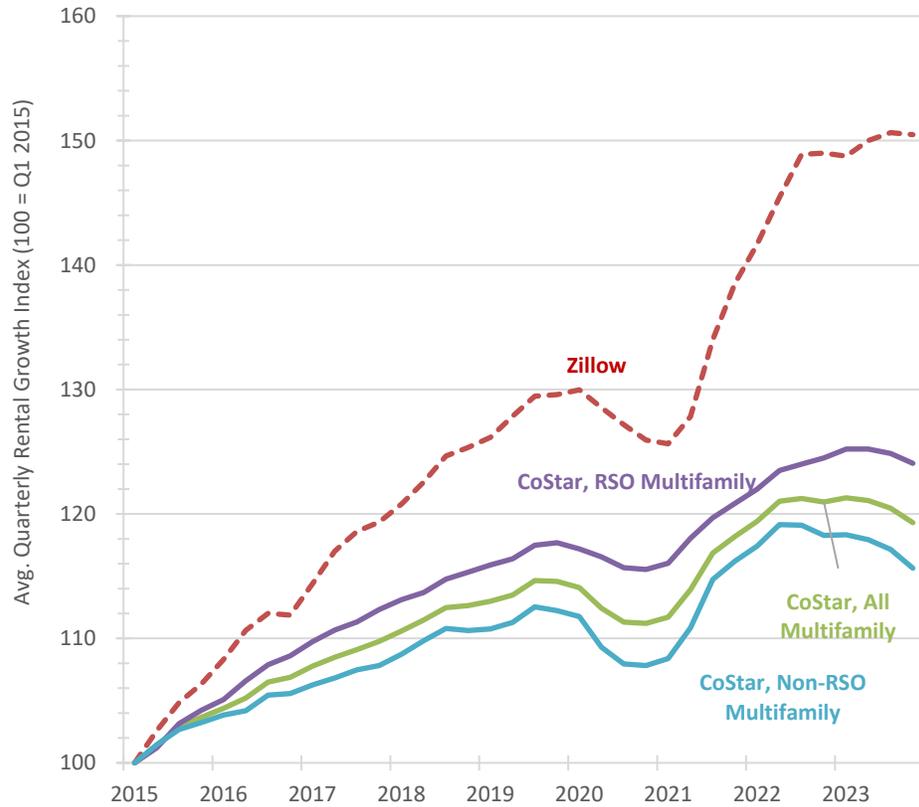
Because these estimates all begin at different starting points in 2015, it is useful to compare growth rates in addition to rental price levels. *Figure 43* indexes all

Figure 42: Estimates of Average Quarterly Rent per Unit in Los Angeles by Building Age, 2015-2023



Source: CoStar; Zillow.

Figure 43: Estimates of Average Quarterly Rent Growth by Building Age, 2015-2023



Source: CoStar; Zillow.

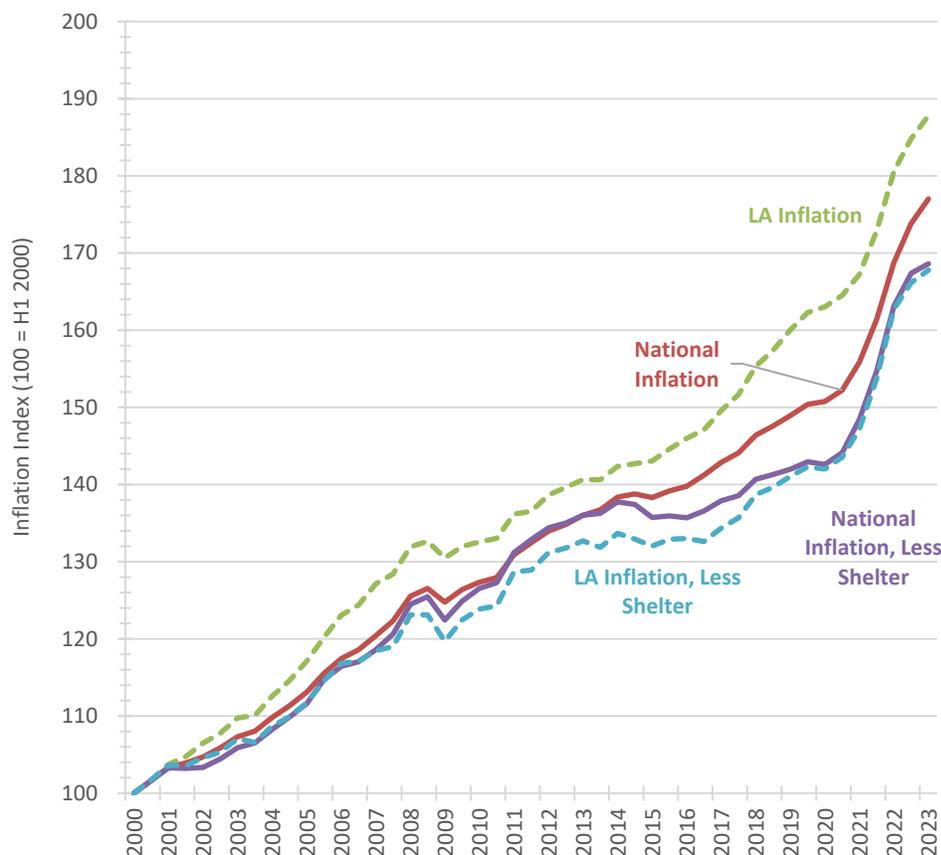
four estimates to 100 in the first quarter of 2015 and then shows how they appreciated thereafter. Based on these different indexes, the average effective asking rent in Los Angeles grew from 19.3 to 50.5 percent from 2015 to 2023.

This indicates an annual growth rate between 2.0 percent and 4.6 percent, with the former estimate more focused on multi-family properties within the City and the latter estimate more broadly capturing regional trends for both single-family and multi-family properties.

Breaking down the dataset by building age again allows a comparison of RSO multi-family properties versus non-RSO multi-family properties. The older, RSO properties exhibited rent growth of 24.1 percent, or an annual growth rate of 2.4 percent. The newer, non-RSO properties exhibited rent growth of 15.6 percent, or an annual growth rate of 1.6 percent.

Although the older properties began at a significantly lower level of rental prices, they caught up somewhat to the newer properties over time. Although rent stabilization is intended to achieve slower, rather than faster, rent growth, it is important to remember that it only applies to tenants who are renewing their leases. These growth rates indicate that the turnover of old-to-new tenants is high enough for landlords to increase the average rents they earn at a rate similar to the market rate for non-RSO properties.

Figure 44: National vs. Los Angeles Inflation, 2000-2023



Source: U.S. Bureau of Economic Analysis.

Consumer Price Inflation

Across the United States, the national CPI-U, the Consumer Price Index for All Urban Consumers, increased by 81.9 percent from January 2000 to November 2023, or an average annual growth rate of 2.5 percent, as shown in *Figure 44*. In Los Angeles, the CPI-U increased more—by 92.6 percent over these 24 years, or an average annual growth rate of 2.8 percent. Thus, it became relatively more expensive to live in Los Angeles than in the rest of the country during this period.

This relatively faster inflation in Los Angeles is due entirely to housing costs. From the first half of 2000 to the first half of 2023, when the disaggregated data are available, non-shelter inflation—the CPI-U without housing costs—increased by 68.6 percent nationally and 67.8 percent in LA, as shown in *Figure 45*. Thus, in all goods other than housing, Los Angeles actually became slightly more affordable than the rest of the country.

Subtracting the non-shelter inflation from the overall inflation reveals the contribution of housing costs to this increasing cost of living. Housing added 0.3 percentage points to the annual national inflation rate and 0.6 percentage points to the annual LA inflation rate, accounting for 12 percent of inflation nationally and 21 percent of inflation in Los Angeles.

This difference includes both owner-occupied and rental housing, which are combined in the government’s shelter inflation calculation.⁴⁹ The next section disaggregates these components to focus specifically on rental housing.

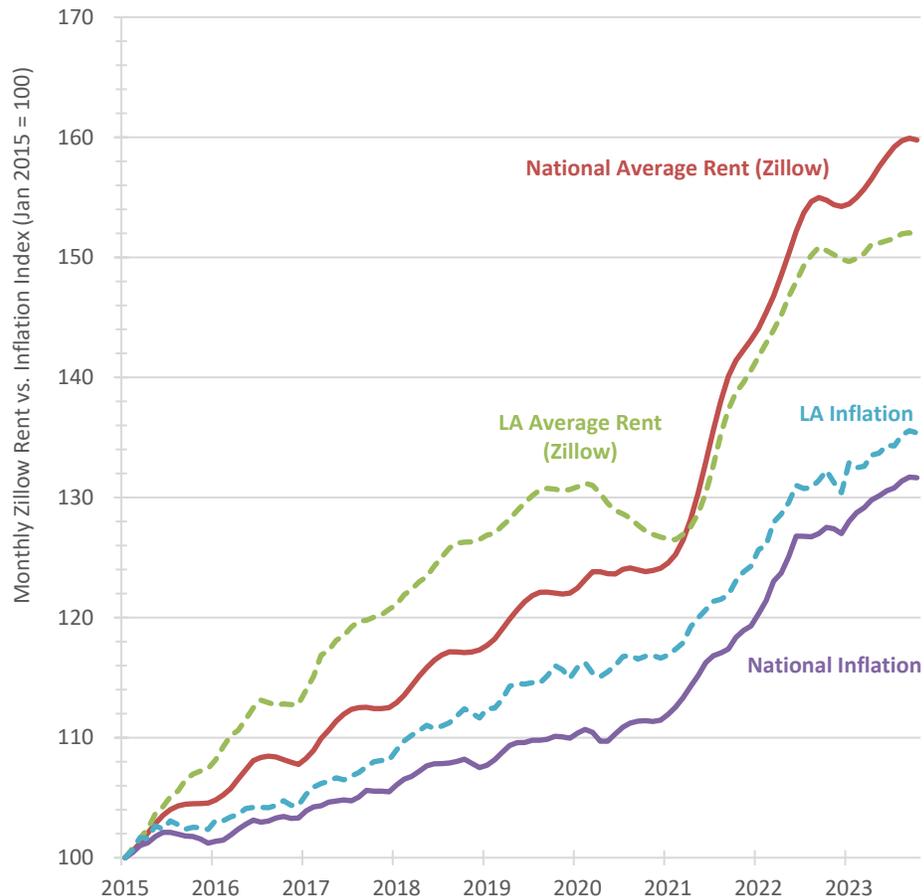
Rent Growth vs. Inflation

By most metrics, rent growth exceeded inflation in recent years. However, the extent of this divergence depends significantly upon the chosen estimates. The largest gap appears by comparing Zillow rents to overall CPI-U, as shown in *Figure 45*. By this comparison, from 2015 to 2023, national average listed rent increased 59.8 percent, while inflation only increased 31.6 percent.

Focusing more locally on Los Angeles, average listed rent increased 51.7 percent, while inflation increased 35.6 percent. Thus, despite unusually high inflation in 2021 and 2022, rents still outpaced overall consumer prices. In fact, as indicated above and shown in the graph, rents were a large driver of this unusually high inflation.

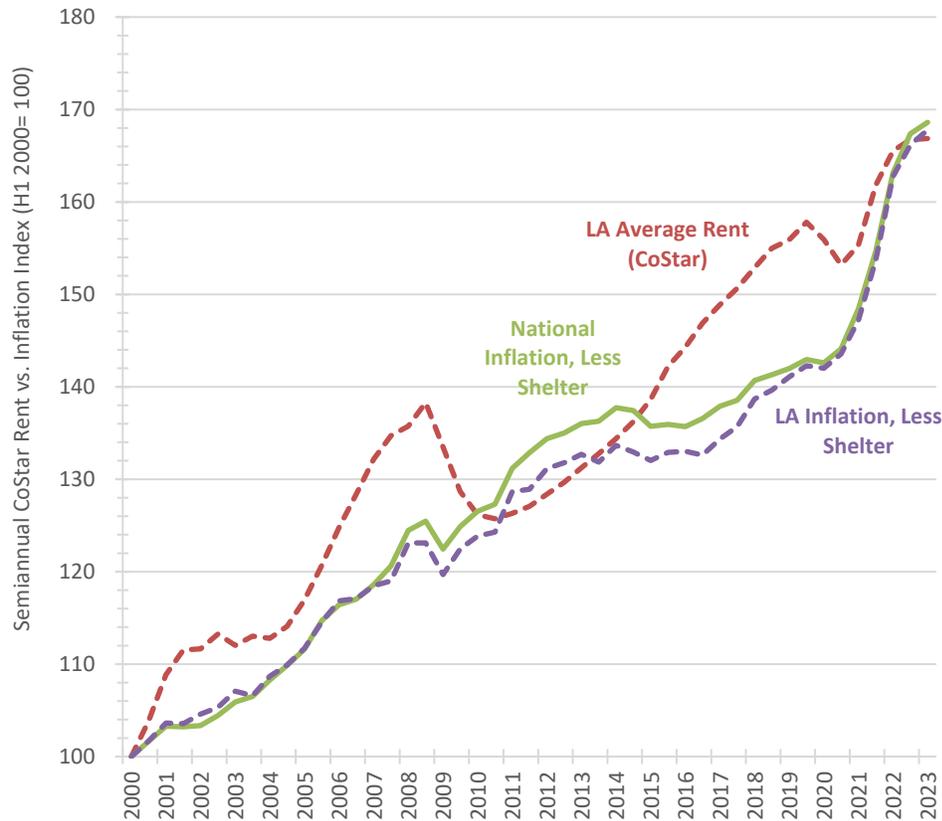
It is noteworthy that the gap is larger for the rest of the United States than for Los Angeles. Despite the City’s reputation as an expensive housing market,

Figure 45: Monthly Zillow Rent Growth vs. Inflation, 2015-2023



Source: U.S. Bureau of Economic Analysis; Zillow.

Figure 46: Semiannual CoStar Rent Growth vs. Non-Shelter Inflation, 2000-2023



Source: CoStar; U.S. Bureau of Economic Analysis.

rents grew faster in smaller housing markets during the Covid pandemic, as shown by the sudden acceleration in the red line around early 2021, while Los Angeles rents actually decreased significantly in the early months of the pandemic, erasing the outsized gains they had made relative to the rest of the country.

This gap disappears by comparing CoStar rents to non-shelter CPI-U, as shown in Figure 46. By this comparison, the average effective asking rent per unit in Los Angeles increased by 66.9 percent, while inflation increased 68.6 percent nationally and 67.8 percent locally in Los Angeles. This benchmark offers a more direct comparison of housing costs versus other consumer prices, rather than double-counting housing on both sides of the comparison given its large role in overall CPI-U. However, as indicated above, the CoStar estimates only focus on multi-family properties sampled by this data provider.

Different tenants therefore had different experiences. Some tenants, represented by the Zillow index measuring all rental housing across the metropolitan area, experienced rent growth that far exceeded inflation, both locally and nationally. Other tenants, represented by the CoStar index focusing more narrowly on multi-family rental housing in the City of Los Angeles, experienced rent growth that was slightly less than the inflation of all other goods.⁵⁰

Findings

- From 2000 to 2023, the Los Angeles region had a higher rate of inflation than the rest of the United States. This was due entirely to housing costs. For all goods other than housing, the Los Angeles region actually became slightly more affordable than the rest of the country.
- From 2000 to 2023, housing added 0.3 percentage points to the annual national inflation rate and 0.6 percentage points to the annual Los Angeles inflation rate, accounting for 12 percent of inflation nationally and 21 percent of inflation in Los Angeles.
- From 2015 to 2024, average effective asking rents grew faster for RSO properties than for non-RSO properties (24.1 percent, compared to 15.6 percent), likely reflecting strong demand for protection against high rent hikes in an increasingly expensive market, as reflected in low vacancy rates.
- Los Angeles rents decreased significantly in the early months of the pandemic, erasing the outsized gains they had made relative to the rest of the country. From 2020 to 2023, rents grew more slowly in Los Angeles than in the rest of the United States.



10. The Context for Rent Regulation

*Photo credit:
Economic Roundtable*

Overview

Under the Rent Stabilization Ordinance (RSO), evictions are only permitted for specified just causes. In regard to allowable rent increases, the RSO has two prongs. Increases in the rents of sitting tenants are regulated. However, at the commencement of a new tenancy, rents can be reset at market levels (vacancy decontrol). As well as being included in the RSO, vacancy decontrol is mandated by state law (the Costa-Hawkins Act) that preempts local regulation.⁵¹ Consequently, because the rate of turnover in tenancies is substantial, market rents are a central determinant of allowable rent levels.

The RSO is applicable to residential rental units constructed before October 1, 1978, with the exception of single-family dwellings (but not condominium units), specified types of non-profit, non-market rentals, and other specified classes containing a small number of units.⁵² Of the 1,122,326 rental units in the City, 650,832 are subject to the RSO.⁵³ The number of properties under the RSO is skewed towards smaller rental properties (*Table 1*). Seventy-one percent of *properties* under the RSO have two to four units. However, 70 percent of the *units* are on properties with more than four units.

Table 1: Properties and Units by Number of RSO Units on Property

Building Size	Percent of RSO Properties	Percent of RSO Units
2-4 Units	71%	30%
5-9 Units	17%	18%
10-19 Units	7%	15%
20-49 Units	4%	21%
50 or more Units	1%	16%

Source: City of Los Angeles Housing Department. 2024. Report Dashboard for RSO. Excludes condominium units.

Apart from the RSO, a state law that was adopted in 2022 places a cap on allowable rent increases in units that are more than 15 years old and are not covered by local rent control legislation.⁵⁴ In Los Angeles about 220,201 rental units that were constructed after October 1978, but are more than 15 years old, are in this category.⁵⁵

Identification and interpretation of rents, rent increases, and rental income of units covered by the RSO requires consideration of widely diverse factors.

A freeze on allowable annual rent increases of sitting tenants was in effect from May 2020 through January 2024. Effective February 1, 2024, a four percent rent increase was authorized for all RSO units. During the freeze, generally, no increases could be imposed on sitting tenants, who occupied about half of all units.⁵⁶ On the other hand, for the other half that became vacant during the freeze, substantial rent increases could be obtained. The rents of units with vacancy turnovers have averaged 30 to 50 percent above their level in 2020.⁵⁷

In the decade prior to the freeze (2010 to 2020), the increases in market rents that could be obtained upon vacancies were well above the increases in the

CPI. Also, as a consequence of the three percent floor on allowable annual increases for sitting tenants during a period when the CPI was increasing at a lower rate, increases in allowable rent levels for sitting tenants exceeded the rate of increase in the CPI. Consequently, from 2010 to 2020, the average of rents of units covered by the RSO increased from \$1,097 to \$1,477, a 34.6 percent increase, compared to the rate of increase in the CPI of 23.3 percent.⁵⁸

On the other hand, apart from the prohibition on increases of the rents of sitting tenants, on some units, either no rents or only a portion of allowable rents were received from 2020 to 2023, as a consequence of the moratorium on evictions for non-payment of rent. In regard to apartment operating costs, insurance costs, which amounted to only about two percent of rental income in 2020, have increased by roughly one hundred percent in the past four years.

The following discussion elaborates on these details and provides various perspectives on the current situation regarding apartment rentals. It includes discussions of: 1) increases in rent of units covered by the RSO, 2) increases in apartment operating costs, 3) standards for allowable rent increases under the 33 other local rent stabilization ordinances that are in effect in California, 4) whether or not the additional allowable annual rent increases of one percent each for master-metered gas and electricity should be continued, and 5) issues related to the selection of an annual general adjustment standard.

The History of Rent Increase Standards under the RSO

In October 1978, rents were rolled back to their level on June 1, 1978 and a moratorium was placed on rent increases.⁵⁹ In April 1979, the RSO was adopted.⁶⁰ Under that law, annual rent increases of seven percent were authorized. During that period, annual increases in the CPI exceeded seven percent (CPI increases: 1978 – 7.4 percent, 1979 – 10.7 percent, 1980 – 15.8 percent, 1981 – 9.8 percent). In 1980, the RSO was amended to allow additional annual rent increases of one percent each for master-metered gas and electric utilities.⁶¹

Starting in 1982, the rate of increase in the CPI declined (CPI increases: 1982 – 5.9 percent, 1983– 1.8 percent, 1984 – 4.5 percent, 1985 – 4.6 percent). In 1985, the annual rent increase standard in the RSO was amended. Annual allowable increases for sitting tenants were tied to the percentage increase in the CPI with a floor of three percent and a ceiling of eight percent.⁶²

In May 2020, in response to pandemic conditions, the annual rent increase allowance was suspended.⁶³ In January 2024, the Council authorized a rent increase of four percent for the period from February 1 through June 30, 2024, with additional allowances of one percent each for master-metered gas and/or electricity.⁶⁴

Turnover of Tenants under the RSO

Vacancy decontrol plays a central role in determining allowable rent increases. A substantial portion of tenants are recent movers, who commenced their tenancies at market rent levels. As of May 2020, when the freeze on increases of the rents of sitting tenants was adopted, 40 percent of the tenants had moved into their units since January 1, 2017. From January 2020 through January 2023, 40.5 percent of all units turned over (*Table 2*).

Table 2: Percent of Occupied RSO Units by Move-In Year

Move-In Year	Percent of Occupied Units
2020 – Jan. 2023	40.5%
2015-2019	22.8%
2010-2014	16.9%
2000-2009	11.8%
1990-1999	6.5%
Before 1990	1.4%

Source: Economic Roundtable team analysis; City of Los Angeles Housing Department Rent Registry 2024.

Overall, turnover rates from 2020 through January 2023 did not vary substantially by the size of the building. In single unit properties and buildings with over 50 units, the turnover rates were higher. In one or two unit properties, 49.8 percent of tenants moved in since 2020. In buildings with 50 or more units 44 percent of tenants moved in since 2020 (*Table 3*).

The RSO generally applies to parcels with two or more units, which make up 99.9 percent of all RSO units. The rare exceptions are single residential units attached to commercial units.

Table 3: Percent of Occupied RSO Units by Move-In Year and Building Size

Move-In Year	1-2 Units	3-4 Units	5-9 Units	10-19 Units	20-49 Units	50+ Units	Total
2020 - Jan 2023	49.8%	39.1%	38.1%	38.5%	38.6%	44.4%	40.5%
2015-2019	25.2%	26.1%	22.6%	21.7%	21.9%	22.6%	22.8%
2010-2014	13.6%	16.7%	17.1%	17.6%	18.6%	15.4%	16.9%
2000-2009	7.9%	12.0%	13.3%	13.2%	12.4%	9.9%	11.8%
1990-1999	2.8%	4.9%	7.1%	7.3%	7.3%	6.2%	6.5%
Before 1990	0.7%	1.4%	1.9%	1.7%	1.2%	1.5%	1.4%
Total	100%	100%	100%	100%	100%	100%	100%

Source: Economic Roundtable team analysis; City of Los Angeles Housing Department Rent Registry 2024.

Increases in Rents of Units Subject to the RSO

Increases in rents of units covered by the RSO are an outcome of the combination of increases in market rents obtained upon turnover and the annual allowable rent increases for sitting tenants.

Increases in Market Rents in Buildings Subject to the RSO

As a consequence of vacancy decontrol, average rent levels of RSO units have increased at rates substantially exceeding the rate of increase in the CPI. From 2005 to 2022, the average of rents paid by tenants who within the past year had moved into apartment units constructed before 1979 increased by \$948, an 88.5 percent increase compared to an increase in the CPI of 54 percent during this period.

The average rents of tenants who moved into units under the RSO within the past 12 months, the increases in those average rents and the annual increases in the CPI from 2006 through 2022, are shown in *Table 4*. The starting year for this trend analysis is 2005 because it is the first year with annual data from the American Community Survey. The most recent year is 2022.

Table 4: Increases in Market Rents that Could Be Charged to Incoming Tenants in Units Covered by the RSO Compared with CPI Increases

Year	Average Market Rent for New Move-ins	Percent Increase in Average Market Rent	Percent Increase in the Consumer Price Index
2005	\$1,071	-	-
2006	\$1,155	7.8%	4.3%
2007	\$1,222	5.8%	3.3%
2008	\$1,291	5.6%	3.5%
2009	\$1,278	-1.0%	-0.8%
2010	\$1,285	0.5%	1.2%
2011	\$1,283	-0.2%	2.7%
2012	\$1,264	-1.5%	2.0%
2013	\$1,339	5.9%	1.1%
2014	\$1,440	7.5%	1.3%
2015	\$1,600	11.1%	0.9%
2016	\$1,571	-1.8%	1.9%
2017	\$1,691	7.6%	2.8%
2018	\$1,716	1.5%	3.8%
2019	\$1,774	3.4%	3.1%
2020	\$1,738	-2.0%	1.6%
2021	\$1,909	9.8%	3.8%
2022	\$2,019	5.8%	7.2%

Year Ranges	Percent Increase in Average Market Rent	Percent Increase in the Consumer Price Index
2005-2013	25.0%	18.5%
2013-2017	26.3%	7%
2017-2020	2.8%	8.7%
2020-2022	16.2%	11.6%
2005-2022	88.5%	54%

Source: U.S. Census Bureau, American Community Survey, Public Use Microdata Sample for the City of Los Angeles; U.S. Bureau of Labor Statistics, Consumer Price Index for All Urban Consumers for Los Angeles and Orange Counties.

A substantial portion of this difference is attributable to a surge in rents from 2013 to 2017, when average market rents increased by \$352, a 26 percent increase compared to a seven percent increase in the CPI. Trends in market rents have been cyclical. In the three prior years, 2009 through 2012, market rents declined by 1.2 percent, while the CPI increased by six percent; in contrast from 2005 through 2008, market rents increased by 20.5 percent compared to an 11.5 percent increase in the CPI.

Overall Increases in Rents in the Los Angeles Area

The CPI Rent Index for the Los Angeles Standard Metropolitan Statistical Area takes into account regulated and unregulated rents. During substantial portions of the period from 2005 through 2023, the rate of increase in the CPI Rent Index was well above the rate of increase in the CPI All-Items Index. From 2005 to 2023, the CPI Rent Index for the Los Angeles area increased by 89 percent compared to an increase of 59.4 percent in the CPI All-Items Index, and an increase of 49 percent in the CPI All-Items Less Shelter Index.

Allowable Annual Rent Increases under the RSO before 2020 Compared with the Increase in the CPI

In the ten-year period before the rent freeze (from 2010 to 2020), the annual allowable rent increases totaled 35.6 percent compared to a 23 percent increase in the CPI. In the five-year period before the rent freeze (from 2015 to 2020), the annual allowable rent increases totaled 17 percent, compared with a 12.5 percent increase in the CPI.⁶⁵ These results were the outcome of the combination of the floor of three percent on annual allowable general adjustments during a decade that included five years of annual increases under 1.6 percent in the CPI (*Table 5*).

Table 5: Allowable Annual Increases under the RSO Compared with CPI Increases (Vacancy Decontrol Increases Not Included)

Year	Allowable Annual Increase	CPI Increase *	Annual Allowable Rent Increase Exceeded CPI Increase by More than 1%	CPI Increase Exceeded Annual Allowable Rent Increase by More than 1%
<i>Difference between Allowable Rent Increase and CPI Increase</i>				
2005	3%			
2006	4%	4.45%		
2007	5%	4.79%		
2008	3%	2.97%		
2009	4%	4.14%		
2010	3%	-0.62%	3.62%	
2011	3%	1.17%	1.83%	
2012	3%	2.24%		

2013	3%	2.10%	
2014	3%	1.55%	1.55%
2015	3%	1.19%	1.81%
2016	3%	0.80%	2.2%
2017	3%	1.78%	1.22%
2018	3%	2.43%	
2019	4%	3.75%	
2020	0%	3.19%	3.19%
2021	0%	2.14%	2.14%
2022	0%	2.60%	2.60%
2023	0%	7.42%	7.42%
2024	4%	4.28%	

Source: Economic Roundtable team analysis; U.S. Bureau of Labor Statistics, Consumer Price Index for All Urban Consumers for Los Angeles and Orange Counties. Note: * In accordance with the RSO, the increase in the CPI is calculated by the Los Angeles Housing Department based on the 12-month average ending in the prior September.

Average RSO Rents

Average Rents and Increases in Rents of RSO Units since 2017

A comparison is made between 2017, 2020, and 2023 rent levels in *Table 8*. The base year is 2017, because detailed data about rents levels beginning with 2017 through the present can be obtained from the City’s Rent Registration database.

During the freeze on annual general adjustments, while the rents of one portion of units were frozen, substantial rent increases were realized for a substantial portion of all units – the units that turned over.

From 2020 to January 2023, although the rents of sitting tenants could not be increased, average rents of units covered by the RSO increased by \$127 as a consequence of vacancy decontrol. This was an increase of 8.5 percent compared with a 15.4 percent increase in the CPI.⁶⁶

Taking into account the period from 2017 to January 2023, the average rent of units under the RSO increased by \$295, from an average of \$1,280 to \$1,575, an increase of 23 percent, compared to a 25.5 percent increase in the CPI during this period.⁶⁷

This increase was bifurcated in the sense that in 40.5 percent of the units that had no change in tenants from 2020 to January 2023, no rent increase was permitted. In contrast, in 2023, the average rent levels of new tenants who moved in during 2020 was eighteen percent above the 2020 average for units covered by the RSO. By January 2023, the average rent level of \$2,112 for new tenants was 50 percent above the 2020 average of \$1,477.

Overall, as *Table 6* indicates, move-in year is a central determinant of the current rent for RSO units.

Table 6: Percent of Occupied RSO Units by Move-In Year

Move-In Year	Percent of Units	Average Rent in Jan. 2023
1995-1999	5.2%	\$1,154
2000-2004	5.4%	\$1,186
2005-2009	6.4%	\$1,316
2010-2014	18.1%	\$1,350
2015	4.2%	\$1,451
2016	4.4%	\$1,497
2017	4.3%	\$1,583
2018	5.1%	\$1,629
2019	6.4%	\$1,689
2020	9.8%	\$1,742
2021	13.9%	\$1,838
2022	12%	\$2,028
Jan. to Feb.2023	1.7%	\$2,112

Source: Roundtable analysis; U.S. Bureau of Labor Statistics, Consumer Price Index for All Urban Consumers for Los Angeles and Orange Counties; City of Los Angeles Housing Department Rent Registry 2024.

Average RSO Rent Levels by Size of Building and Move-In Year

Average RSO rent levels were significantly higher for properties with two to four units. Compared to an overall RSO average rent of \$1,609, the average rent for properties with two to four units was \$2,357 and for properties with five to nine units was \$1,952. Some of the differences may be attributable to differences in the characteristics of units on smaller properties (*Table 7*). These differences are discussed in *Chapter 7* of this report.

Table 7: Average RSO Rent in January 2023 by Building Size and Move-In Year

Move-In Year	2-4 Units	5-9 Units	10-19 Units	20-49 Units	50+ Units	All Units	Number of Units
All Years	\$2,357	\$1,952	\$1,651	\$1,560	\$1,500	\$1,609	450,268
1970-1979	\$1,551	\$1,240	\$1,155	\$1,103	\$1,149	\$1,314	2,036
1980-1989	\$1,618	\$1,345	\$1,177	\$1,159	\$1,186	\$1,261	4,117
1990-1999	\$1,584	\$1,396	\$1,209	\$1,150	\$1,126	\$1,218	27,415
2000-2009	\$1,759	\$1,483	\$1,293	\$1,223	\$1,195	\$1,284	52,910
2010-2014	\$1,926	\$1,633	\$1,405	\$1,316	\$1,271	\$1,331	82,652
2015-2019	\$2,291	\$1,889	\$1,628	\$1,545	\$1,491	\$1,532	133,173
2020 – Jan 2023	\$2,624	\$2,350	\$2,014	\$1,886	\$1,778	\$1,852	147,481

Source: Economic Roundtable team analysis; City of Los Angeles Housing Department Rent Registry 2024.

Average RSO Rent Levels by Planning District

Average RSO rent levels vary substantially among the different districts of the City. As of 2023, the range was between \$1,361 and \$2,218.

The rates of increase in average rents between 2017 and 2023 in different planning districts varied between 22 and 29 percent, and from 2020 to 2023, following the onset of Covid, rent increases ranged from 9 to 14 percent (*Table 8*).

Table 8: RSO Units Average Rent Levels 2017 to 2023 by Planning District

Planning District	Mean Rent						Percent Increase		
	2017	2018	2019	2020	2021	2022	January 2023	2017-2023	2020-2023
West Los Angeles	\$1,784	\$1,904	\$1,972	\$2,077	\$2,074	\$2,122	\$2,218	24%	7%
Central Los Angeles	\$1,249	\$1,323	\$1,375	\$1,430	\$1,475	\$1,491	\$1,540	23%	8%
N. San Fernando Valley	\$1,143	\$1,220	\$1,234	\$1,300	\$1,330	\$1,362	\$1,391	22%	7%
S. San Fernando Valley	\$1,256	\$1,349	\$1,381	\$1,454	\$1,484	\$1,526	\$1,573	25%	8%
South Los Angeles	\$1,088	\$1,185	\$1,194	\$1,255	\$1,297	\$1,359	\$1,407	29%	12%
Harbor	\$1,109	\$1,144	\$1,140	\$1,191	\$1,246	\$1,340	\$1,361	23%	14%
East Los Angeles	\$1,164	\$1,236	\$1,269	\$1,338	\$1,389	\$1,446	\$1,496	29%	12%
Citywide	\$1,285	\$1,369	\$1,409	\$1,477	\$1,509	\$1,554	\$1,604	25%	9%

Source: City of Los Angeles Housing Department Rent Registry

Findings

- Increases in the rents of units covered by the RSO are the outcome of the combination of increases in market rents obtained upon the commencement of a tenancy and the annual allowable rent increases during tenancy.
- Annual general adjustments of rents were not permitted from May 2020 through January 2024. However, substantial rent increases, averaging 30 to 50 percent above the 2020 level, could be obtained from units with a turnover in tenants.
- Because the rate of turnover in tenancies is substantial, about 50 percent within a four-year period, market rents are a central determinant of allowable rent levels and increases in rent under the RSO.
- In the decade before the freeze on annual general adjustments, from 2010 to 2020, the annual allowable rent increases totaled 35.6 percent compared to a 20.9 percent increase in the CPI. In the five-year period from 2015 to 2020, the annual allowable rent increases totaled 17 percent, compared with a 12.5 percent increase in the CPI.
- Overall, in the context of Los Angeles’ substantial increases in market rents, move-in year has been a central determinant of the current allowable rent of RSO units.



11. Operating Expenses and Other Costs for Low-Income Housing

*Photo credit:
Economic Roundtable*

Overview

The largest expenses for most Los Angeles landlords are capital expenditures, followed by vacancy, salaries and personnel, taxes, and contract services, based on data from the National Apartment Association.

Investor cash flows range from 34 percent to 62 percent of total revenue collected; however, these data do not identify how much of these cash flows remain for the landlords (i.e., the equity investors) after paying debt service.

The fastest growing expense from 2010 to 2022 for low-income (rent-restricted) properties has been property insurance, though it still comprises a small portion of total operating costs, based on data from Novogradac, an accounting and consulting firm that specializes in affordable housing and surveys low-income housing landlords across the country annually to estimate the average operating expenses per unit. While these properties may be distinct from the RSO inventory, they are a useful proxy to understand operating expenses, for which little other data are available to researchers.

From 2010 to 2022, the growth of operating costs for low-income housing exceeded both inflation and the growth of rents. Most of the divergence occurred during the Covid pandemic.

Revenue and Costs for a Typical Los Angeles Apartment

Before studying how operating expenses, capital expenditures, and other relevant costs have changed over time, it is useful to understand their role in a typical apartment investment, compared to the revenue that landlords collect.

The National Apartment Association (NAA) collects data on apartment revenues and expenses in Los Angeles, broken down into several categories, and reports the averages across four apartment types.

First, they distinguish low-rise, garden-style apartments from mid- and high-rise apartments.

Second, they distinguish apartments where utilities are broken down individually by sub-meters (“individual-metered”) from “master-metered” systems where utilities are measured only for the building as a whole.

This two-by-two matrix creates four cost breakdowns that are reported for 2021, the latest year of available data; this is shown in *Figures 47, 48, 49, and 50*.

Generally, the NAA is likely to collect data from market-rate properties. Therefore, the average rental revenue should be higher than we would find at rent-stabilized properties. However, these data points can still be useful to understand what new tenants can face when landlords reset the rent for a new lease. These breakdowns first report “potential gross rent,” indicating how much the landlords *could* receive if there were no vacancies, no trouble collecting rent, and no need to offer concessions to lure tenants.

This potential revenue is higher for mid- and hi-rise apartments (in *Figures 48 and 50*), compared to garden-style apartments (in *Figures 47 and 49*), probably because the taller buildings are located in denser neighborhoods where demand is higher. Previous research has shown that building height itself does not necessitate higher rents; in fact, taller buildings often can charge less because the development cost can be spread out over more units.⁶⁸ Any correlation between building height and rents is typically due to (a) the value of the neighborhood, (b) differences in building quality, and (c) financial constraints that make some building types easier to buy and sell than others.⁶⁹

From this potential gross rent, we deduct all the losses and expenses that the landlords pay before earning their equity cash flows. Across these four types of apartments, the largest costs are vacancy losses (which will be analyzed separately later in the report), salaries and personnel, taxes, contract services, and capital expenditures. For most apartment types, capital expenditures dominate.

In total, landlords lose the following amount of their potential revenue to these losses and expenses:

- 69 percent for individual-metered garden apartments
- 55 percent for individual-metered mid- and hi-rise apartments
- 38 percent for master-metered garden apartments
- 49 percent for master-metered mid- and hi-rise apartments

Thus, investor cash flows represent 31 percent, 45 percent, 62 percent, and 51 percent of potential gross rent, respectively.

Alternatively, we can compare the investor cash flows to the actual total revenue collected (often referred to as “effective gross income”), which would be more standard for a typical corporate finance analysis: 34 percent, 50 percent, 62 percent, and 55 percent, respectively.

Though it is not common to use the term “profit” in real estate in the same way as financial accountants do in preparing corporate income statements, these percentages are a reasonable measure of the “profitability” of these investments before considering the financing costs.

Importantly, these data do not allow us to identify how these cash flows are divided between debt and equity investors. Most investors, especially recent buyers, have large mortgage payments that can swallow much, if not all, of these cash flows.

However, for equity investors who have owned their properties for a long time, paid off their loans, and are now free-and-clear of debt, this analysis indicates that the average apartment unit in Los Angeles appears to be highly profitable when allowed to charge market-rate rents.

Even in these best-case scenarios, though, this analysis does not indicate whether these cash flows are sufficient to compensate investors for the risks they are taking or to motivate developers to create new housing.

Figure 47: Individual-Metered Garden Apartments

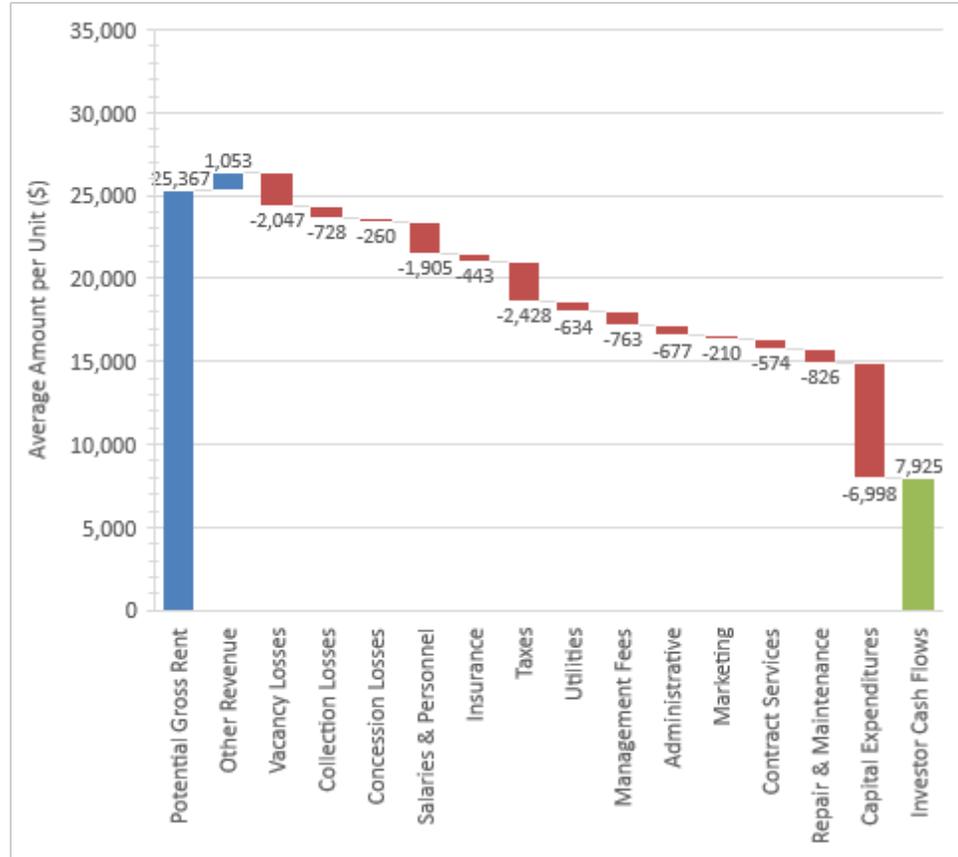


Figure 48: Individual-Metered Mid- and Hi-Rise Apartments

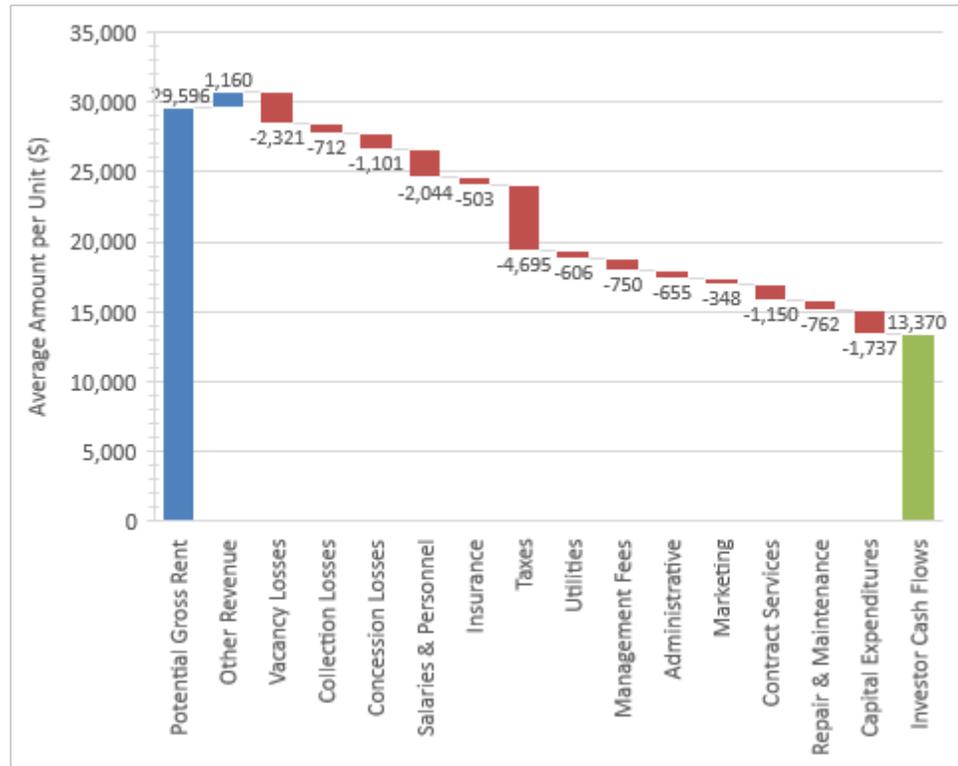


Figure 49: Master-Metered Garden Apartments

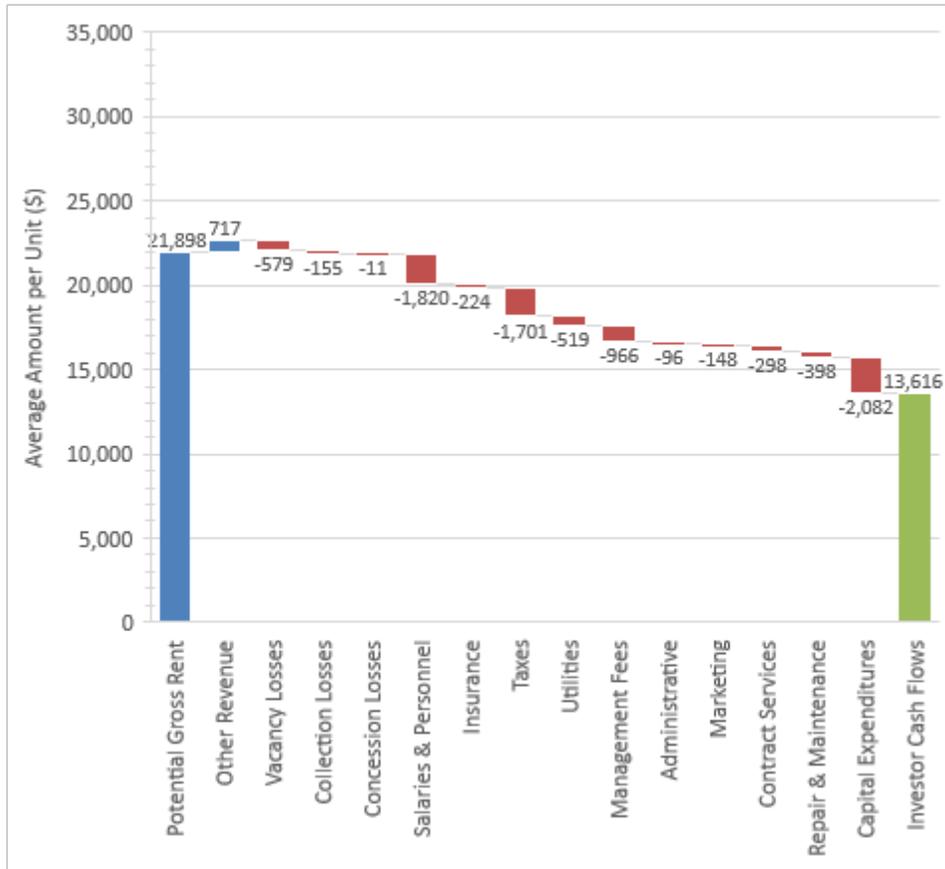
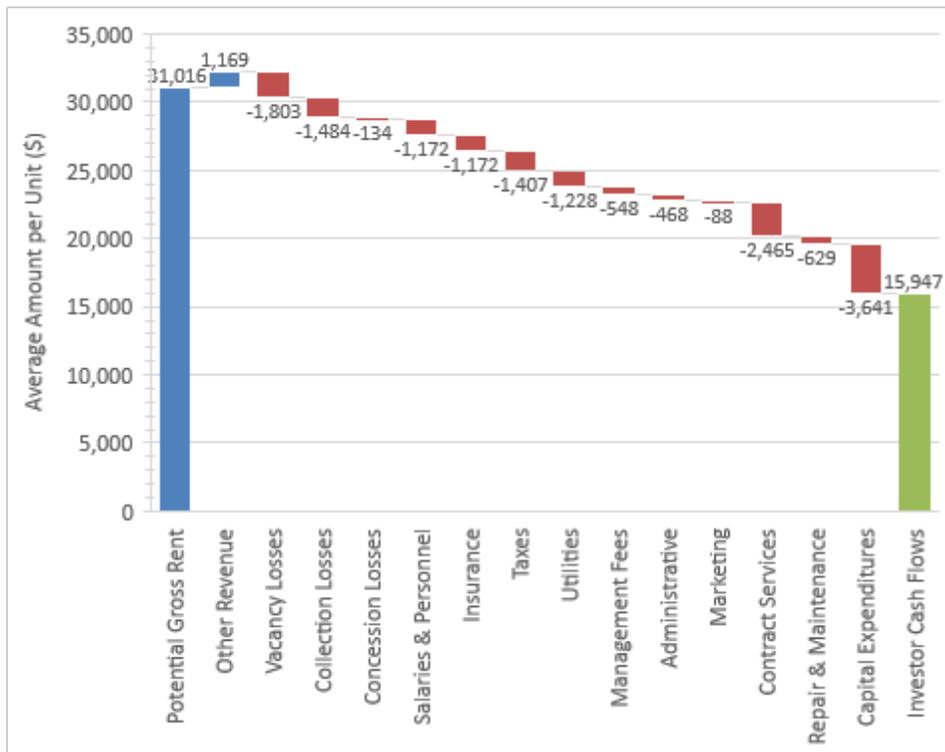


Figure 50: Master-Metered Mid- and Hi-Rise Apartments



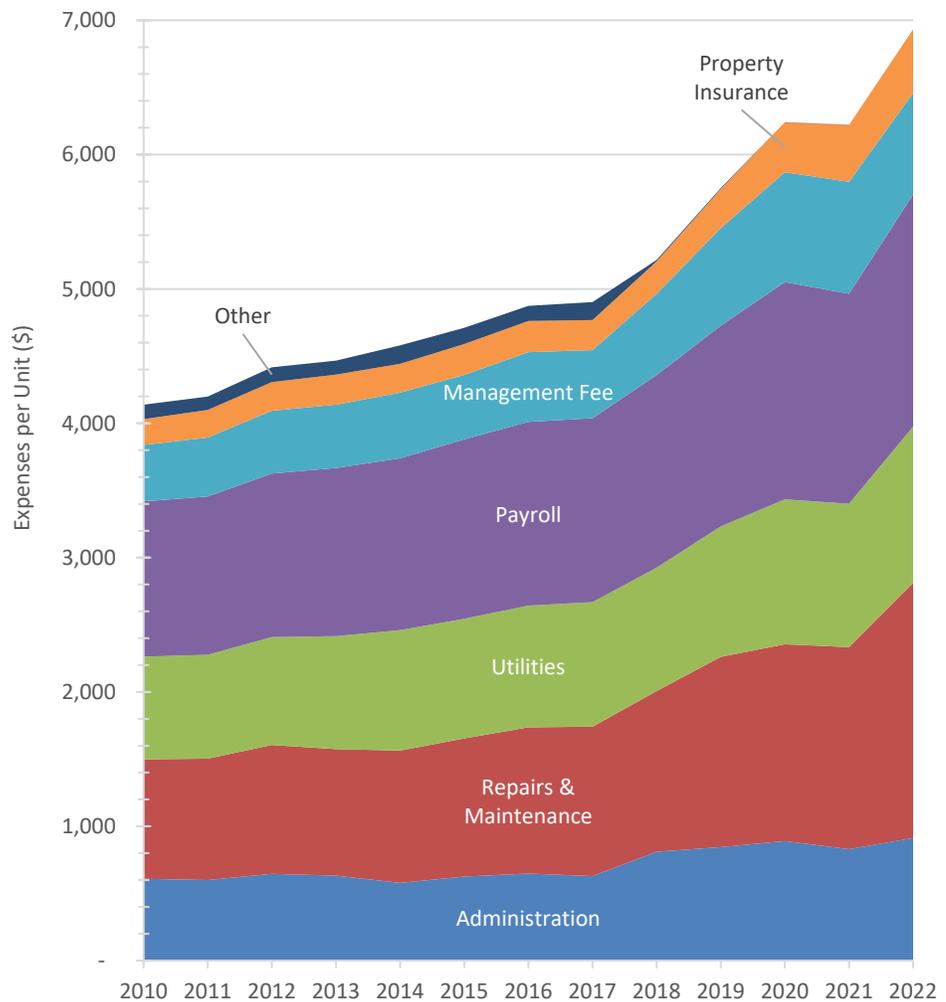
Operating Expense Growth over Time

Putting aside capital expenditures where less data are available, it is possible to break down changes in different operating expenses over time, particularly for rent-restricted housing units. This data comes from Novogradac.

These properties are funded by the Low-Income Housing Tax Credit (LIHTC), and therefore they were built after 1986. So, in Los Angeles, they are different from rent-stabilized properties. However, as rent-restricted properties, they have many similarities and can serve as a useful proxy to understand how the cost of operating low-income housing has changed over time.

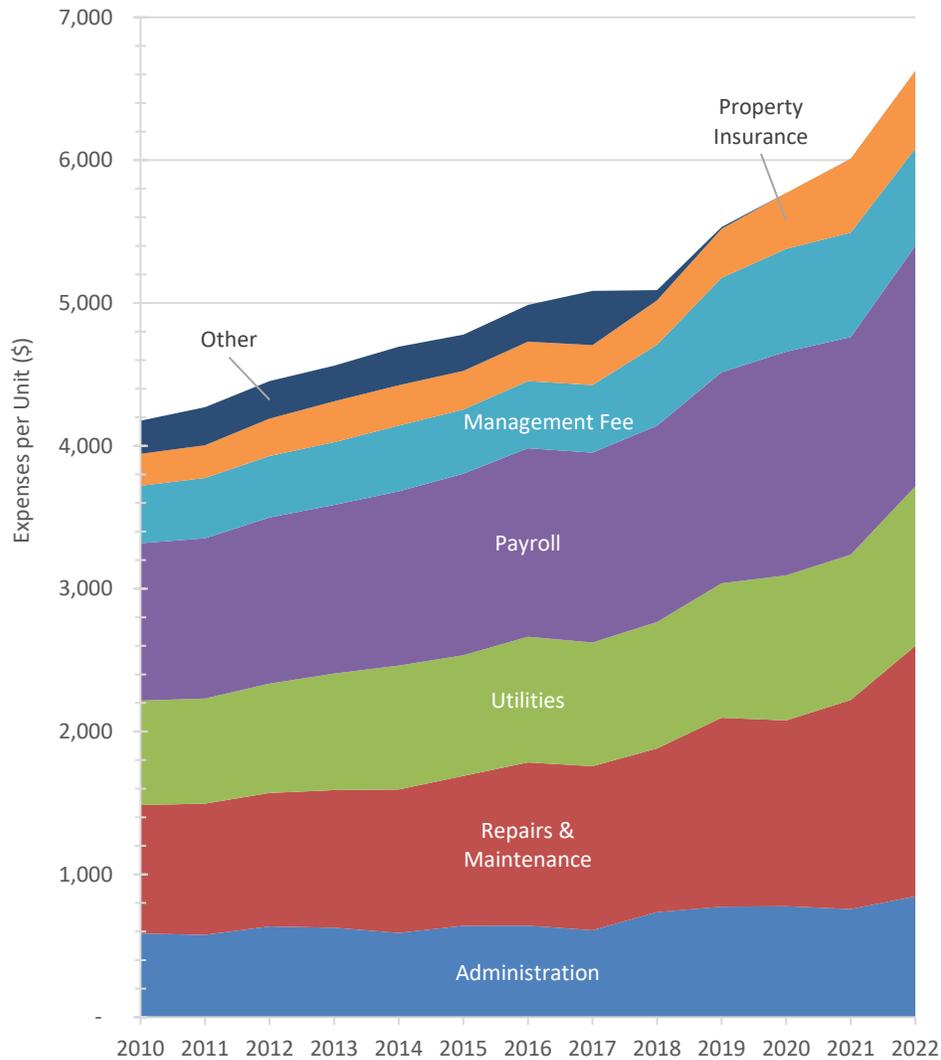
Novogradac reports a slightly different (but somewhat overlapping) set of categories than the NAA, as shown in *Figures 51 and 52*. These breakdowns contain more geographies than simply Los Angeles, partly because Novogradac's sample size in Los Angeles is small.

Figure 51: Average Expenses per Low-Income Housing Unit in the Western United States, 2010-2022



Source: Novogradac.

Figure 52: Average Expenses per Low-Income Housing Unit in Large Metropolitan Areas, 2010-2022



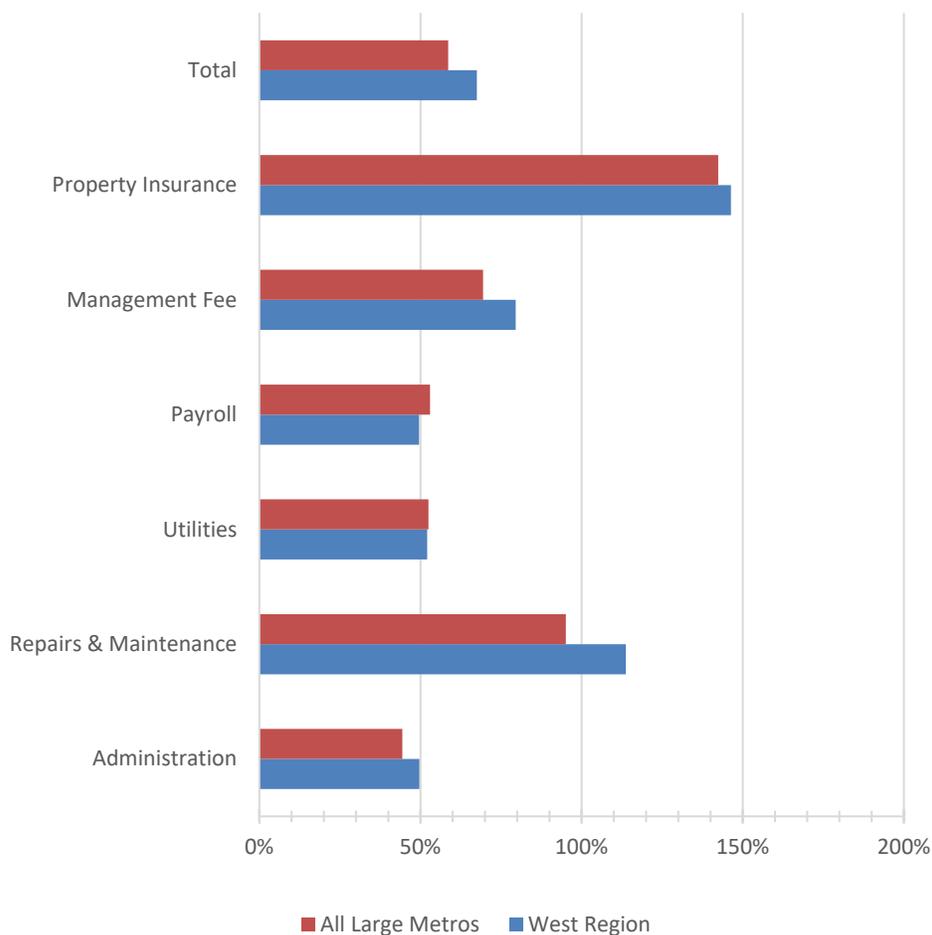
Source: Novogradac.

To ensure that we are not choosing a wider geography that is inaccurate for understanding Los Angeles specifically, we show two different geographic definitions and compare them to bolster the robustness of our conclusions. The average operating expenses per unit across the Western region of the United States are reported in *Figure 51*, and the average operating expenses per unit across all large metropolitan areas in the U.S. are reported in *Figure 52*. As the graphs show, they tell nearly identical stories.

According to both graphs, the largest operating expenses were payroll and repairs and maintenance, with utilities coming in third, administration fourth, and management fee fifth.

These graphs probably understate the cost of repairs and maintenance because they only measure operating expenses, not capital expenditures, which are also a form of physical property improvement. Property insurance was a much smaller cost.

Figure 53: Total Growth in Average Expenses per Low-Income Housing Unit, 2010-2022



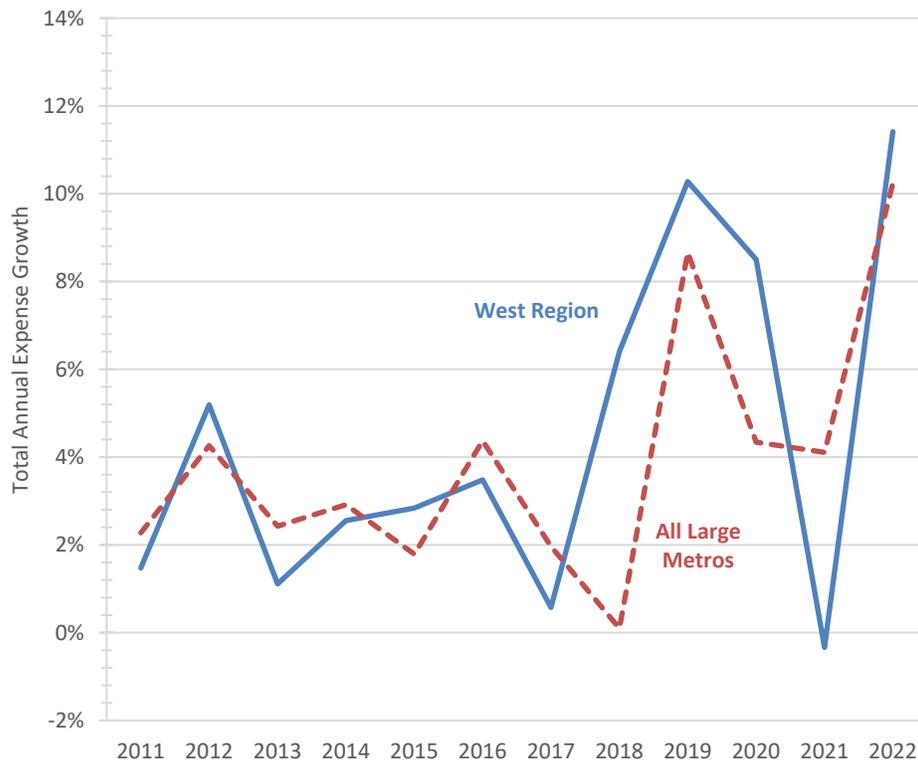
These costs have increased nearly every year from 2010 to 2022, with a brief lull in the West during the pandemic from 2020 to 2021. The sharpest cost growth occurred during the two periods 2017 to 2020 and 2021 to 2022.

The proportions of these categories are changing over time. As *Figure 53* shows, despite being the smallest category, property insurance costs are growing the fastest. This is consistent with a growing series of reports in the industry and the media about rising premiums and deductibles, as well as declining coverage, as insurance companies try to anticipate future losses from climate change, natural disasters, rising property costs, and other uncertainties in increasingly volatile markets.

If this trend continues, insurance will become a much larger contributor to the cost of operating residential properties. For the moment, however, it remains small for the average unit compared to other cost categories (4.6 percent to 8.6 percent in the low-income properties sampled by Novogradac).

From 2010 to 2022, property insurance costs increased over 140 percent, at an average annual growth rate of eight percent. In comparison, the next fastest growing category was repairs and maintenance, which grew 95 percent across all large metropolitan areas and 114 percent throughout the West region, for

Figure 54: Annual Growth in Average Expenses per Low-Income Housing Unit, 2010-2022



Source: Novogradac.

average annual growth rates of six percent and seven percent, respectively. The other categories of operating expenses grew three percent to five percent annually, on average.

From 2010 to 2018, the overall annual growth rate of operating expenses fluctuated within a small band, approximately two percent to four percent in most years, as shown in *Figure 54*. There was very little volatility, despite small fluctuations.

In 2019, cost growth accelerated to nine percent across all large metropolitan areas and 10 percent in the West region. Then, at the beginning of the pandemic in 2020, these two figures diverged. Operating expenses grew four percent across all large metropolitan areas, possibly due to declining housing demand and out-migration as some residents moved to smaller, more affordable areas. However, the West region overall continued to experience high expense growth of 10 percent that year.

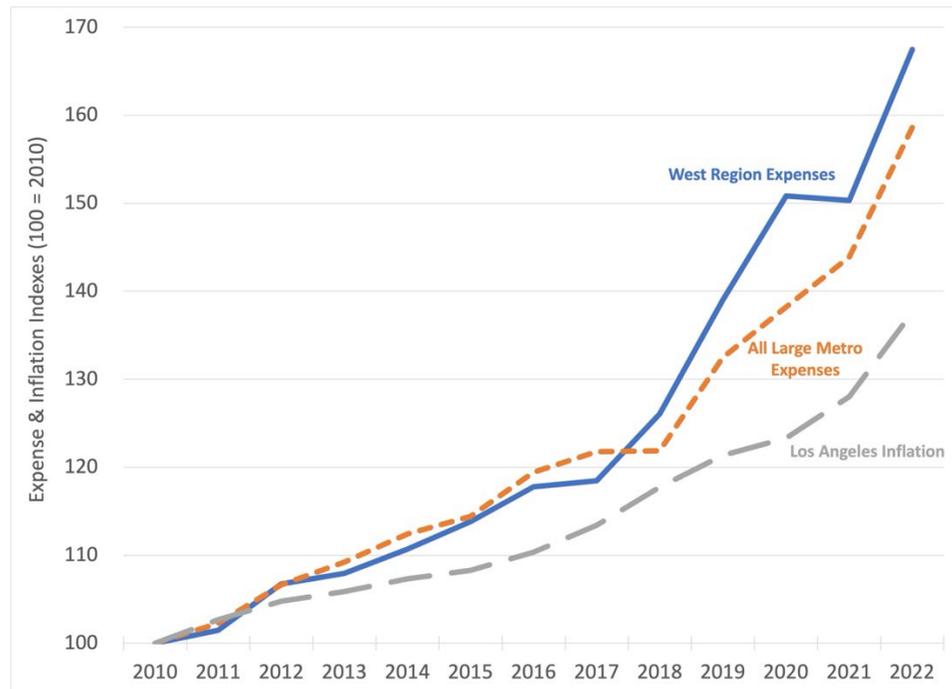
In 2021, operating expense continued to grow four percent across all large metropolitan areas, but it fell to zero percent in the West. Finally, in 2022, operating expense growth soared to new heights in both measures: 10 percent across all large metropolitan areas and 11 percent in the West.

Though inflation was high during this period, operating expense growth was higher, consistent with reports in the industry and the media indicating a shortage of construction materials and labor as well as an increase in

renovations, all of which would push up the costs of repairs, maintenance, and payroll.

Operating expenses that outpaced inflation has been the rule, rather than the exception, over these 12 years, as shown in *Figure 55*. From 2010 to 2022, operating expenses grew 59 percent across all large metropolitan areas and 67 percent in the West region, compared to inflation in Los Angeles of only 38 percent, as measured by the local CPI-U index. Operating expenses began outpacing inflation as early as 2012 and have remained ahead ever since, with the gap growing especially from 2019 onward. In fact, most of the gap preexisted the late pandemic surge.

Figure 55: Average Expense Growth per Low-Income Housing Unit vs. Inflation, 2010-2022

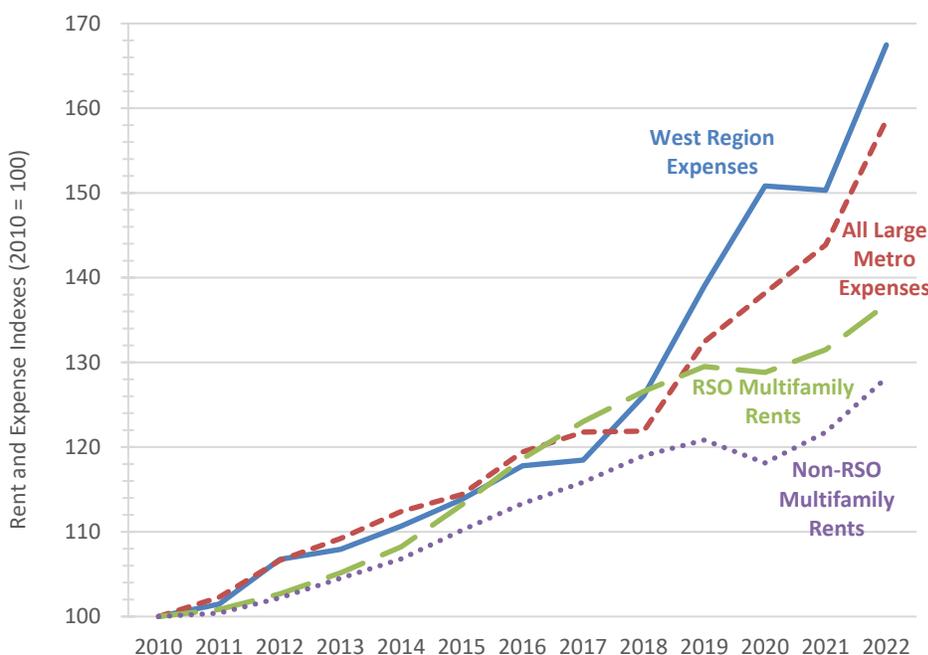


Source: Novogradac.

To understand how the financial margins of the average landlord have changed, especially in the wake of the pandemic, it is helpful to compare these operating expenses to the rents that landlords are earning in revenue. *Figure 56* compares the CoStar rents described earlier to the LIHTC operating expenses, all indexed to 100 in 2010 and showing total growth up to 2022.

Not only did operating expenses outpace rents, but by some measures, they grew twice as fast. Whereas operating expenses grew 59 percent across all large metropolitan areas and 67 percent in the West region, multi-family rents in Los Angeles grew only 28 percent for non-RSO properties and 37 percent for RSO properties.

Figure 56: Average Expense Growth per Low-Income Housing Unit vs. Rents, 2010-2022



It is likely that profit margins shrank during this time, with most of the erosion occurring during the pandemic. Until 2019, RSO rents mostly kept pace with operating expenses. The divergence is clear and persistent thereafter.

Findings

- The largest expenses and losses for most Los Angeles landlords are capital expenditures, followed by vacancy, salaries and personnel, taxes, and contract services.
- The fastest growing expense from 2010 to 2022 for rent-stabilized properties has been property insurance, though it still comprises a small portion of total operating costs (4.6 percent to 8.6 percent in the low-income properties sampled by Novogradac).
- Operating expenses outpaced inflation in the Western region of the United States from 2010 to 2022, increasing 67 percent compared to 38 percent increase in the Consumer Price Index.
- Until 2019, increases in RSO rents mostly kept pace with increases in operating expenses, but have lagged inflation since the onset of the Covid pandemic.
- For equity investors who have owned their properties for a long time, paid off their loans, and are now free-and-clear of debt, the average apartment unit in Los Angeles appears to be highly profitable.



12. Increases in Apartment Operating Costs

*Photo credit:
Economic Roundtable*

Overview

In the course of engaging in the rental housing business, apartment owners have to cover operating expenses and mortgage payments. (An important distinction is that mortgage payments are not an operating expense.) In the U.S., apartment operating expenses are typically in the range of 30 percent to 50 percent of rental income. In Los Angeles, operating expenses have averaged about 35 percent of rental income. Assuming an average monthly rent of \$1,600 (the average for all units is \$1,609), and an average operating expense ratio of 35 percent, monthly operating costs per rental unit average \$560.

Systematic sources on apartment operating costs are very limited, based on data provided by managers of large properties to national reporting services and services reporting expenses for non-profit rentals supported with tax incentive programs. In this analysis, projections of the amounts of operating expenses and the increases in those costs relative to overall apartment rents are based on a combination 1) the data from national sources that include reports on metropolitan averages of apartment operating costs for modest samples, 2) operating cost projections in financial statements contained in offering memoranda accompanying listings of apartment properties offered for sale, 3) public records of property tax amounts, and 4) city and industry data on utility costs.

In half of the 100 financial statements in the offering memoranda in apartments sales listings in 2022, 2023 and 2024 that were reviewed for the purpose of this study, the total of operating expenses as a share of gross scheduled income was in the range of 30 to 39 percent. In a quarter of the listings, the ratio was between 40 and 45 percent. In dollar terms, in a quarter of the buildings the amount was between \$400 and \$499 per unit per month, and in half of the buildings operating expenses ranged from \$500 to \$599 per unit per month.

In the income and operating expenses reports of the Institute of Real Estate Management for 2017 and 2019 covering different categories of larger buildings, including all ages of buildings, the ratio of overall operating expenses to gross scheduled income ranged from 26 percent to 30 percent. In the class of buildings that had rents comparable to the average in Los Angeles, the average dollar amount was \$525 per unit per month. In the National Apartment Association income and expense report for 2021, the ratios averaged 38 percent. However, in its sample, the average rents were far above the average for Los Angeles. These samples do not segregate newer and older buildings.

In addition to operating costs, apartment owners incur replacement (capital improvement) costs. In the financial statements in offering memoranda, typically about two percent of the rental income is projected for reserves.

The balance of rental income net of operating expenses - **net operating income** - is an average of 65 percent of total income. This is the return on the

investment in the property, which is available to cover debt service and provide cash flow.

The foregoing sources do not provide the basis for projecting exact averages of operating expenses, but they do provide the basis for reasonable projections of the scale of the various apartment operating expenses relative to rental income and the amounts of increases in those expenses in proportion to rental income. In any case, whatever estimates or averages are provided, they are within the context that operating expense ratios vary between properties and sometimes vary substantially. Operating expense ratios are most likely to diverge widely among small properties, while being more uniform among larger properties.

Overall Summary of Operating Costs

1) In buildings with five or more units, the average property tax is \$147 per unit per month, in buildings with four or less units the average is \$192. The amount of property tax per unit per month is mainly dependent when the property was purchased and varies by large amounts from the average.

Property taxes are equal to 1.2 percent of the assessed value, which is usually determined by the purchase price adjusted upwards by two percent per year since the purchase year. Average purchase prices per rental unit have nearly doubled in the past ten years, which in turn were nearly triple the average of ten years earlier.

2) Utility costs have been increasing at rates well in excess of the percentage increase in the CPI. However, because their overall weight relative to overall rental income is 10 percent or less, the impact of increases in utility costs relative to rental income is very modest. In about 80 percent of all units, gas and electricity are separately metered and paid by the tenant, apart from the rent. Those costs are addressed in *Chapter 16* of this report.

3) Insurance costs, which in past years only amounted to about two to three percent of rental income, \$30 to \$45 per month per rental unit, have skyrocketed over the past few years, roughly doubling to \$60 to \$90.

4) Management and maintenance costs vary greatly among properties. In cases in which the owner performs all or part of management functions and all or part of maintenance functions, out of pocket expenditures are lower. Offsite management fees are typically in the range of four percent of rental income. Overall management and maintenance expenses are typically in the range of 10 to 15 percent of rental income.

The table below summarizes the income and operating expense projections in a sample of apartment offering memoranda. Reporting in the memoranda varied between statements of actual amounts and projections.

Table 9: Average Income and Operating Expense Projections in Los Angeles Apartment Listing Offering Memoranda (OM) Buildings Subject to the RSO

Expense	Avg. Per Unit/Mo	Explanation
Scheduled Gross Income	\$1,556	
3% Vacancy Allowance	\$47	Standard projection in OM – 2% or 3%
Effective Gross Income	\$1,509	
OPERATING EXPENSES		
Property Taxes	\$250	In the OM, property tax levels were imputed based on reassessments that would arise from a sale at the asking price
On Site Manager		Combined average of on-site & offsite management \$30 higher on properties with on-site manager
Offsite Management Fee	\$62	Standard projection in OM 4%
Insurance	\$ 40	
Utilities	\$ 70	Properties with separately metered gas & electricity
Refuse Collection	\$27	
Repair and Maintenance	\$42	Standard Projection in OM \$500/yr. unit
Landscaping	\$10	
Operating Reserves	\$31	Standard projection in OM – 2%
Other		Other categories commonly listed include internet, pest control, city fees
Total Operating Expenses	\$542	
Net Operating Income	\$967	

Source: Economic Roundtable team analysis.

Table 10: Overall Operating Expense Increases 2020 to 2024

Operating Expense	Cost per Unit per Month 2021-2023	Percent Increase 2020-2024	Increase per Unit per Month
Property Taxes	\$146	9%*	\$13.00
Insurance	\$40	100%	\$40.00
Management	\$64	17.6%	\$11.00
Repair & Maintenance, Outside Services, Misc.	\$167	25%	\$42.00
Utility Services			
Water	\$35		\$2.50
Sewer	\$30		\$1.80
Solid Waste	\$30		\$5.00
Public Fees Not Included on Property Tax Bill			
SCEP	\$0		\$2.83
RSO Rent Registration	\$1.61		\$0
Business License	\$1.50		\$0
Total			\$118

Source: Economic Roundtable team analysis. *Increase in property tax rate is for properties that have not sold.

Overall Outcome in Terms of Cost Increases

The foregoing projection of overall operating cost increases since 2020 is for buildings that have not sold, and consequently have not been reassessed for property tax purposes, within the past four years (*Table 10*). The estimates of the utility cost increases in the past few years are based on information about rate increases. The estimate of the increases in management costs is based on the CPI. The estimate of maintenance, outside services, and miscellaneous costs are based on the percentage increases in labor costs. The estimate of the increase in insurance costs is based on industry reports.

Property Taxes and Assessments

In contrast to other types of operating expenses, property tax bills, which include property tax and assessments, are public record. Furthermore, databases may be acquired from the Assessor with property tax amounts, the number of units, and the construction year of each parcel. On this basis it is possible to calculate average property tax amounts per unit.

The average property tax bill in buildings with five or more units that are subject to the RSO is \$147 per unit per month. In properties with three or four units, the average is \$192 per unit per month.

Pursuant to Proposition 13, the property tax rate is fixed at one percent of assessed value and increases in assessed value are limited to two percent a year, except when a property is sold, in which case the property is reassessed at market value, which is usually the purchase price. Therefore, property taxes can only increase by two percent per year, except when a property is sold.

Additional voted indebtedness raises the overall property tax rate to 1.2 percent. Property tax bills also include additional fees for additional assessments, which are for specified public services and bond costs. In properties with three or more units, the average total of assessments per unit per month is \$12.59.

Property tax bills per unit vary by large amounts among properties depending on differences in purchase prices that are largely determined by the year of purchase. For example, the average for units in buildings purchased before 2000, which contain 38 percent of all units, is under \$100 per unit per month. The average for units in buildings purchased between 2005 and 2014, which contain 22 percent of all units, is \$169. The average for units in buildings purchased since 2015, which contain 26 percent of all units, is \$256 (*Table 11*).

Assessments

Real property owners are subject to nine different types of assessments, which are in addition to the 1.2 percent tax on assessed value. These assessments are

included in property tax bills.⁷⁰ Rather than being based on property value, the assessments are based on square footage.⁷¹

As indicated, the average total of assessments is \$12.59 per unit per month. The totals fall under \$22 per unit per month in properties that contain 96 percent of all of the units in buildings with three or more units.

Consistent with the fact that single-family rental dwellings are larger and typically have more land, the average total of the assessments on these properties is \$23 per unit per month.

A very small number of properties that are subject to the RSO have been subject to large assessments associated with special improvement projects.

Table 11: Property Tax Bill Amounts Per Unit, Including Assessments

Last Sale Date	RSO Buildings 5+ Units: Percent of Units	RSO Buildings 5+ Units: Average Monthly Bill per Unit	RSO Buildings 3-4 Units: Percent of Units	RSO Buildings 3-4 Units: Average Monthly Bill per Unit
Before 1980	12%	\$48.83	11%	\$53.49
1980-1984	4%	\$77.85	4%	\$84.65
1985-1989	7%	\$91.27	7%	\$112.85
1990-1994	5%	\$98.48	5%	\$126.91
1995-1999	10%	\$78.29	8%	\$116.15
2000-2004	14%	\$113.28	15%	\$160.68
2005-2009	9%	\$168.76	9%	\$235.04
2010-2014	13%	\$169.65	15%	\$196.55
2015-2019	16%	\$244.88	17%	\$293.35
2020-present	10%	\$262.14	11%	\$343.91
Total	100%	\$146.64	100%	\$191.64

Source: Economic Roundtable team analysis; Los Angeles Housing Department. 2024. Dataset A: RSO Inventory; Report Dashboard for RSO – LAHD; Los Angeles County Assessor. 2024. SBF Abstract (DS04); Los Angeles County Treasurer and Tax Collector. 2024. Secured Tax Roll (Current).

Management and Maintenance

Projections of management and maintenance expenses are complicated by a lack of publicly available data and the overlapping nature of these categories when they are reported.

Under California law: “A manager, janitor, housekeeper, or other responsible person shall reside upon the premises and shall have charge of every apartment house in which there are 16 or more apartments.”⁷² Forty-five percent of the units covered by the RSO fall into this category. Commonly, the owner manages smaller properties. Management functions, especially in larger buildings, are performed by a combination of on-site managers and off-site management companies.

In the financial statements in apartment sales marketing statements, four percent was standardly listed as the projected ratio of **off-site** management costs to rental income, the equivalent of \$64 per unit per month for apartments with an average rent of \$1,600. In the case of properties with 16 or more units, which require on-site managers, the projections are in the range of four to six percent of rental income. In the case of an apartment renting for \$1,600, these amounts would be in the range of \$64 to \$96 per unit per month.

While the amounts for utility, insurance, and trash collection expenses per unit vary greatly in the offering memoranda, in most cases there is a uniform projection of maintenance expenses of \$500 per unit per year (\$42 per month).

In dollar terms, a sample of 59 “garden type” buildings in the IREM sample for 2019, which had rents more comparable to the average for Los Angeles, the median total cost for the sum of management and maintenance expenses was \$213 per unit per month. In the National Apartment Association sample for Los Angeles in 2021, these expenses totaled \$381 per unit per month. However, the rents for this sample were 50 percent higher than the City average.

Insurance

In past years, insurance costs were only about two to three percent of gross income on the average. National Apartment Association data on the insurance costs for one hundred larger buildings in Los Angeles in 2021 reported an average annual cost of \$40 per unit per month. Institute of Real Estate Management data from 2017 and 2019 for four samples ranging from 49 to 62 large buildings in the Los Angeles metropolitan area reported averages ranging from \$20 to \$37 per unit per month.⁷³ In income and expenses projections in marketing reports in real estate listings in 2022 and 2023 for buildings with between ten and nineteen units in buildings constructed before 1979, half reported insurance costs ranging from \$30 to \$49 per unit per month and a third reported costs ranging from \$20 to \$29 per unit per month. In the offering memoranda in 2024, the average was \$20 per unit per month higher.

The steep increases in insurance costs of the past two years, the new difficulties in obtaining coverage and narrowing scopes of coverage are commonly known. Major insurance carriers have been leaving the market. Apart from the increases in premiums, insurance carriers are now requiring increased deductibles (e.g. a \$25,000 deductible in property insurance policies and higher deductibles in liability policies), thereby increasing the risks that apartment owners now undertake.

In response to the surge in insurance costs, national surveys specifically of insurance costs have been conducted. Consideration of those surveys is subject to the qualification that insurance risks and in turn insurance costs vary greatly among regions. One survey by a nationally recognized source of real estate

data, indicated that as of the second quarter in 2023, the average cost of property and liability insurance for apartments in Los Angeles was \$100 per unit per month.⁷⁴ On the other hand, the financial statements in the offering memoranda of apartment buildings for sale in Los Angeles in 2024 consistently project much lower costs.

If it is assumed that these costs have doubled in the past few years, the increase per unit per month would be about \$40, an increase from about \$40 to \$80 per month per unit. Any projection of an average is subject to qualifications that substantial variations from any average may be common and that the insurance cost situation is highly volatile in an upwards direction.

Utility Costs

Increases in utility rates have substantially exceeded the rate of increase in the CPI. However, the impact of these rate increases has not been substantial in relation to overall rental income, apartment operating costs, and net operating income because the amounts of these costs are small relative to rental income.

Water

Table 12. Water Rates per Hundred Cubic Feet, City of Los Angeles DWP

Last Sale Date	1 st Rate Tier	2 nd Rate Tier
Apr 15, 2016	\$5.552	\$9.271
Jul. 2016	\$4.612	\$8.077
Jan. 2017	\$5.996	\$9.205
Jul. 2017	\$5.775	\$8.815
Jan. 2018	\$6.299	\$9.864
Jul. 2018	\$6.406	\$9.820
Jan. 2019	\$6.392	\$9.704
Jul. 2019	\$6.545	\$9.623
Jan. 2020	\$6.093	\$9.537
Jul. 2020	\$6.773	\$9.115
Jan. 2021	\$7.112	\$9.152
Jul. 2021	\$7.249	\$9.379
Jan. 2022	\$7.361	\$9.720
Jul. 2022	\$7.866	\$ 10.246
Jan. 2023	\$8.395	\$ 10.272
Jul. 2023	\$7.833	\$ 11.300
Jan. 2024	\$8.948	\$ 12.226
Avg. 2018-2020	\$6.418	\$9.611
Avg. July 2022-Jan 2024	\$8.261	\$11.011
Pct. Increase – 2022-2024 compared with 2018-2020	29%	15%

Source: Economic Roundtable team analysis; Los Angeles Department of Water and Power rate history data.

In most buildings, water service is master-metered, and all are serviced by the Los Angeles Department of Water and Power (LADWP). *Table 12* shows water rates charged by the LADWP since spring 2016.

Currently, water costs average about \$40 per apartment unit per month. *Table 13* sets forth average cost data for different size buildings with a breakdown by zone that was provided by LADWP based on a sample of 494 buildings. Since 2017, the increase in cost has been in the range of \$7 to \$15 per month per unit. About half of this increase has occurred since 2020.

Table 13: Average Monthly Water Bill, City of Los Angeles

Building Size	Zone	Buildings in Sample	2017	2020	Nov. 2022-Oct. 2023
3-4 Units	1	12	\$24.43	\$31.85	\$30.77
5-10 Units	1	13	\$20.13	\$23.30	\$26.94
11-49 Units	1	10	\$19.50	\$27.67	\$29.88
3-4 Units	2	156	\$34.58	\$38.30	\$41.51
5-10 Units	2	153	\$27.66	\$33.31	\$37.49
11-49 Units	2	104	\$29.66	\$36.13	\$43.09
3-4 Units	3	9	\$37.38	\$42.66	\$41.01
5-10 Units	3	11	\$44.77	\$51.09	\$66.87
11-49 Units	3	19	\$38.34	\$47.33	\$51.53
50-99 Units	2 & 3	7	\$27.96	\$32.57	\$42.92
Total		494			

Source: Economic Roundtable team analysis; Los Angeles Department of Water and Power rate history data

Sewer

Sewer rates are determined by water usage and have been equal to about 80 percent of the first-tier water rate. The rate for sewage is now 29 percent above the level in 2017 (*Table 14*).

Table 14: Sewer Rates per Hundred Cubic Feet, City of Los Angeles

Years	Rate per Hundred Cubic Feet
1972-78	\$0.05
1978-79	\$0.07
1979-80	\$0.12
1980-81	\$0.43
1981-84	\$0.47
1984-86	\$0.59
1986-87	\$0.63
1987-88	\$0.66
1988-89	\$0.89
1989-90	\$1.13
1990-91	\$1.37
1991-92	\$1.88

1992-2003	\$2.26
2003-04	\$2.33
2004-05	\$2.49
2005-06	\$2.66
2006-07	\$2.85
2007-08	\$3.05
2008-11	\$3.27
2011-12	\$3.42
2012-13	\$3.57
2013-14	\$3.73
2014-15	\$3.97
2015-16	\$4.23
2016-17	\$4.51
2017-18	\$4.80
2018-19	\$5.11
2019-20	\$5.44
2020-24	\$5.80

Source: Economic Roundtable team analysis; Los Angeles Department of Sanitation rate history data.

Assuming that these costs are about two-thirds of water costs, the monthly cost per unit would be about \$30, and the increase in monthly costs per unit of about 20 percent from 2017 to 2018 to the present would be about \$6. The increase in costs from the rate for the 2019–2020 fiscal year to the current rate is 6.6 percent.

Solid Waste Collection

Solid waste collection costs typically range from \$18 to \$30 per unit per month. This range is based on a review of income and expense statements in the offering memoranda. National Apartment Association data for large multifamily properties in Los Angeles in 2021 indicated a similar average.

The Department of Sanitation undertakes solid waste collection for buildings of four units or less, while waste collection for buildings with five or more units is undertaken by private companies that have exclusive franchise contracts for designated portions of the City. Before 2017, the collection of waste was open to all licensed operators.

Prior to the authorization of the franchise scheme by the City Council in 2017, apartment owners protested that it would result in substantial cost increases. It was commonly estimated that the fees would triple, but the authors are not aware of any documentation of such a claim.

Going forward from 2017, the franchise agreements set forth a standard for setting allowable annual rate increases. The amount of these increases is calculated on the basis of a weighted cost index based on measurements of increases in the CPI “Employment Cost Index” published by the Bureau of

Labor Statistics and the and “Producer Price Index for Transportation Industries” published by the St. Louis Federal Reserve.⁷⁵ There is a ceiling of five percent on annual increases. If a larger increase is justified, any amount over five percent is rolled over to future years.

Since 2017, cumulative rate increases of 43.3 percent have been authorized (Table 15).

Table 15: Increases in Solid Waste Collection Rates Permitted under Franchise Agreements

Rate Adjustment Year (Beginning January 1)	Calculated Indexed Rate Increase	Additional Rate Increase Over CPI (See source note)	Total Rate Increase	Notes
2017	N/A	N/A		Beginning of Contract
2018	3.05%	0.00%	3.05%	
2019	3.57%	0.00%	3.57%	
2020	2.66%	3.75%	6.41%	0.25% in accordance with amended section 7.32 (Adjustment to process recyclables); plus 3.50% in accordance with amended section 7.3.3 (Organics Infrastructure)
2021	2.40%	3.75%	6.15%	0.25% in accordance with amended section 7.32 (Adjustment to process recyclables); plus 3.50% in accordance with amended section 7.3.3 (Organics Infrastructure)
2022	4.80%	3.00%	7.80%	3.00% in accordance with 7.3.4 (Rate Look Back)
2023	5.00%	0.00%	5.00%	The calculated rate was 8.41% however the contracts have a 5% annual cap. The additional 3.41% is rolled over to future years.
2024	5.00%	0.00%	5.00%	The calculated rate was 5.07% however the contracts have a 5% annual cap. The additional 0.07% is rolled over to future years.
Cumulative Increase 2018-2024			43.3%	
Cumulative Increase 2020-2024			26%	

Source: Los Angeles Department of Sanitation rate history data. Note: Rate Adjustment begins on January 1st of the year shown in the table, Calculation of cumulative increases by Economic Roundtable.

Assuming that solid waste collection costs have increased by 43 percent since the franchise agreements went into effect in 2017, the increase over the 2017 would be about \$7 per unit per month. The increases over the 2020 level would be about \$5 per unit per month.

Gas and Electricity Costs

In about 80 percent of the units covered by the RSO, gas and/or electric costs are sub-metered.⁷⁶ The costs incurred by owners of properties that are master-metered for gas and/or electricity are discussed in *Chapter 16* of this report.

Nominal Fees

The City imposes a few types of fees related to public services. In terms of rental income, they are nominal.

Systematic Code Enforcement Fee (SCEP)

Under the SCEP program, rental units may be subject to an inspection once every four years in order to determine code compliance. The City imposes a fee on rental units for the administration of this program. Until 2022, the full amount of this fee could be passed through to tenants.

In 2022, the SCEP and RSO ordinances were amended to increase the annual fee per unit from \$43.22 to \$67.94⁷⁷ and to limit the portion of the fee that could be passed through to tenants to one-half of the fee.⁷⁸

The increase of this cost to apartment owners – as a consequence of the reduction in the pass-through amount to half the fee and the increase in the fee – is **\$2.83 per unit per month** ($(1/2 \times \$67.94)/(12 \text{ months})$).

Business License Fee⁷⁹

Apartment House License Fees are applicable to apartment houses with more than four families. They are nominal, descending in cost per apartment unit by the size of building, with a maximum possible fee of \$37 per unit per year (**\$3.08 per unit per month.**), as shown in *Table 16*.

Table 16. Business License Fees for Apartment Houses, City of Los Angeles DWP

Last Sale Date	Annual Fee	Minimum Fee Per Unit	Maximum Fee Per Unit
Apr 15, 2016	\$185	\$18.5 (\$1.50/mo)	\$37 (\$3.08/mo)
Jul. 2016	\$200	\$13.33	\$18.18
Pct. Increase – 2022-2024 compared with 2018-2020	\$221	-	\$13.81

Source: Economic Roundtable team analysis; Los Angeles Office of Finance, Business Tax Registration Certificate (BTRC) program data. Note: See Los Angeles Municipal Code § 7.14.010 (License Fees).

Los Angeles Housing Department RSO Unit Registration Fees

The annual registration fee is \$38.75 per rental unit (\$3.23 per unit per month). Fifty percent of this fee can be passed on to the tenant as a surcharge.⁸⁰ The net cost to rental property owners for this fee is \$1.61 per unit per month.

Findings

- In Los Angeles, operating expenses for apartments average about 35 percent of rental income.
- Assuming an average monthly rent of \$1,600 and an average operating expense ratio of 35 percent, monthly operating costs per rental unit average \$560.
- Property taxes average \$146 per unit per month for properties with five or more units and \$191 for properties with three or four units.
- Total utility costs for water, sewer, gas, and electricity generally amount to less than 10 percent of the rent. Therefore, the increases in utility rates that have exceeded the rate of inflation in recent years have not had a substantial impact on the net operating income obtained from rental properties.
- Offering memoranda for apartment properties project four percent of rent for offsite management expenses.
- Insurance costs, which formerly amounted to only about two or three percent of the rents, may have doubled within the past few years and keep on increasing in a steep upward trajectory.
- The balance of rental income net of operating expenses - net operating income - is the return on the investment in the property, which is available to cover debt service and provide cash flow.



13. Returns from Rental Properties

*Photo credit:
Economic Roundtable*

Explanation of Returns from Rental Properties

Net Operating Income

“Net operating income” is the overall return from the overall investment in rental property net of operating expenses. Typically, it is in the range of 55 to 70 percent of rental income.

Net operating income is a measure of the yield from a property and is a central determinant of market value. The amounts that investors pay for properties are linked to projected net operating income levels and anticipated appreciation.

Net Income

“Net” income is the cash flow, minus both operating and mortgage expenses. While net operating income-to-rental income ratios are somewhat uniform, varying percentages of net operating income are required to cover mortgage payments (the cost of purchasing the capital that was used to undertake the apartment investment).

The amount of money required to cover mortgage payments depends primarily on the length of ownership, whether or not the property has been refinanced with a larger mortgage and/or a mortgage with a lower or higher interest rate since the purchase date, and/or whether adjustments in loan interest that were not fixed rate for more than five or ten years have impacted mortgage payments.

Lenders typically require a particular ratio of net operating income to mortgage payments (the debt service coverage ratio) in the range of 1.15 to 1.25. At the outset, low cash flows equal to only a few percent of the cash investment are anticipated. The standard expectation of investors is that the cash flow will increase as rents and net operating income increase, while mortgage payments will decline as a share of overall income.

This expectation makes the investment attractive notwithstanding the low returns at the outset and the known risk that the mortgage interest rate is fixed for only a limited term (e.g., five or ten years).

“After-tax” net income returns may be at a higher level as a result of depreciation allowances that offset taxable net income from the property and other sources.

Growth in Net Operating Income under the RSO

Assuming that operating expenses are about 35 percent of income, leaving 65 percent of income for net operating income, net operating income per month per unit is about \$950. Data from the financial statements in the offering memoranda, with few exceptions, report net operating income ratios of 65

percent or higher. In addition, data from Costar reports average capitalization rates (net operating income/purchase price) in the range of five percent on average prices exceeding \$250,000 per apartment unit. This supports the conclusion that net operating incomes are in this range.⁸¹

Although operating expenses have increased at greater rates than the CPI, net operating income from rental housing investments has grown at faster rates than the CPI. Net operating income has grown at a rate of 3.9 percent since 2000, compared to 2.6 percent rate of increase in the CPI.⁸² The rate of growth has not been even. Net operating income has increased at an annual rate of 3.3 percent since 2017. Net operating income did not increase from 2020 to 2023. In dollar terms, net operating income levels in 2023 were \$225 per unit per month above their level in 2015.

Cash Flow Position

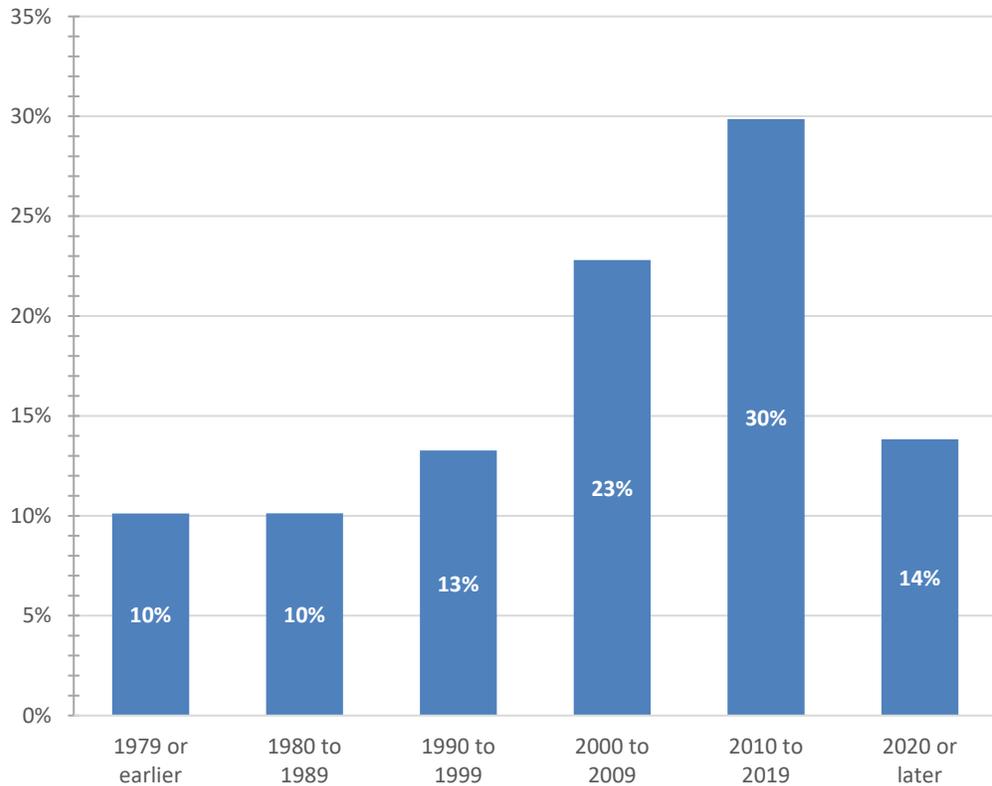
Fifty-six percent of RSO properties, containing 58 percent of units, excluding condominiums, were purchased before 2010 (*Figure 57*). Thirty-four percent of properties, containing 36 percent of units, were purchased before 2000. The length of ownership has been virtually the same for different size properties.

Table 17: Per Unit Increase in Net Operating Income and Cash Flow and Appreciation in Value During Ten Years of Ownership – Prototype

	Year 1		Year 10	
CPI Increase 3.4% average				40%
	<u>Per Month</u>	<u>Annual</u>	<u>Per Month</u>	<u>Annual</u>
a. Rental Income	\$1,000	\$12,000	\$1,500	\$18,000
b. Operating Expenses	\$350	\$4,200	\$525	\$6,300
c. Net Operating Income		\$7,800		\$11,700
d. Capitalization Rate		5%		5%
e. Purchase Price & Market Value	Purchase Price	\$156,000	Market Value	\$234,000
f. Original Cash Invest. & Current Equity	Original Cash Invest.	\$62,400	Current Equity	\$140,400
g. Loan Principal	60% of Purchase Price	\$93,600		\$78,330
h. Loan to Value Ratio		60%		33%
i. Interest Rate		6%		6%
j. Mortgage Payments, 30 Yr. Amortization		\$6,734		\$6,734
k. Cash Flow		\$1,068		\$6,084
l. Cash Flow/Original Cash Investment	:	2%		10%
m. Appreciation				\$78,000
n. Appreciation/Year				\$7,800

Source: Economic Roundtable team analysis. Notes: Calculations are as follows: **Row b** = current year amount 50 percent above base year amount, **Row c** = a-b; **Row e** = c/d; **Row f** = e-g; **Row j** = i*g; **Row k** = c-j; **Row l** = k/62,400; **Row m** = market value – purchase price.

Figure 57: Distribution of RSO Units by Year Purchased



Source: LAHD inventory of RSO properties, excluding condominiums, and Los Angeles County Assessor DS04 data.

The growth in cash flow and appreciation associated with owning an apartment for ten years is illustrated in *Table 17*. It is based on the assumption that rents, which include vacancy decontrol increases, have increased by 50 percent compared to a 40 percent increase in the CPI, that operating expenses have increased by 50 percent, and that interest rates have not changed over the ten-year period.

Alternate assumptions about increases in rents and operating costs and/or the holding period change the outcome of the foregoing projections. Typically, apartment purchases are financed with mortgage loans that have fixed interest rates for a ten-year period and then become variable. Increases or decreases in mortgage payments due to changes in interest rates offset or augment gains in net operating income. However, the standard outcome is that attractive cash flows are obtained by holding a property for a decade in a market in which rent increases exceed increases in operating costs and provide substantial growth in net operating income.

The owners who purchased their properties prior to 2000 are in an exceptionally favorable cash flow position. Their purchase prices (typically under \$60,000 per unit) and consequently their mortgage payments are low relative to rental income, and their property taxes are low because the assessed values of their property are very low compared to current market values.

Losses in Rents because of the Eviction Moratorium

The moratoriums on evictions for non-payment of rent in order to avoid mass displacement and homelessness have had a central place in City policy. Issues related to the impact of the moratorium on rental property owners are discussed in *Chapter 8* of this report.

Trends in Market Values

As in the market for homes, apartment values are sensitive to interest rates, which in turn have a major impact on “capitalization” rates. Currently, “capitalization” rates for apartment purchases in Los Angeles are in the four to five percent range (meaning that market values are equal to the net operating income divided by four or five percent.) For example, a property with a net operating income of \$100,000 is worth in the range \$2,000,000 ($\$100,000/.05$) to \$2,500,000 ($\$100,000/.04$).

Appreciation in the value of apartments subject to the RSO has been substantial. Average values of rental units subject to the RSO have doubled over the last ten years from about \$150,000 per rental unit to \$300,000 per unit and are nearly five times above the level in 2000 (*Table 18*).

The increase in the values over the past ten years is an outcome of the combination of increasing net operating income levels and a decline in capitalization rates accompanying a decline in mortgage interest rates.⁸³ The preceding surge in value from 2000 to 2005 is largely attributable to the decline in capitalization rates from about nine percent to five percent. In the eight-year period from 2005 to 2013, which included the crash starting in 2008, apartment values were level.

Table 18: Average Sales Prices of Rental Units Properties per Unit, 5 or More Units Only, City of Los Angeles

Year	Average Price per Unit
2000	\$63,883
2001	\$79,174
2002	\$69,709
2003	\$102,715
2004	\$101,021
2005	\$124,369
2006	\$148,400
2007	\$122,521
2008	\$149,045
2009	\$136,547
2010	\$125,482
2011	\$112,495
2012	\$120,138
2013	\$144,160

2014	\$157,421
2015	\$196,701
2016	\$218,986
2017	\$229,955
2018	\$254,377
2019	\$263,313
2020	\$263,389
2021	\$296,674
2022	\$303,627

Source: Economic Roundtable team analysis; Los Angeles Housing Department. 2024. Dataset A: RSO Inventory; Report Dashboard for RSO – LAHD; Los Angeles County Assessor. 2024. Note: Sales price per unit based upon Assessor's Documentary Transfer Tax (DTT) Amount – where price was known and not representing a joint sale of multiple parcels, divided by total number of units.

The rate of increase has been substantially uniform across the rental housing stock in terms of building sizes, ranging from five units to more than fifty units. Properties with three or four units have appreciated at a greater rate. However, the use of sale prices of these properties to measure their rental unit values is undercut by the fact that the purchase prices of those properties represents a composite of owner occupancy values and rental unit values.

Findings

- There has been substantial growth in the net operating income of rental units covered by the RSO, although operating expenses have increased at greater rates than the CPI.
- Average values of rental units subject to the RSO have doubled over the last ten years from about \$150,000 per rental unit to \$300,000 per unit and are nearly five times above the level in 2000. The increase in the values over the past decades is an outcome of the combination of increasing net operating income levels and a decline in capitalization rates accompanying a decline in mortgage interest rates.
- The standard expectation of investors in apartment properties is that the cash flow will increase as rents and net operating income increase above their levels at the time of purchase, while mortgage payments will decline relative to overall income. This expectation and the leveraged nature of investments in rental property makes investments in rental properties attractive, notwithstanding low cash returns at the outset.
- Seventy-four percent of the units under the RSO were purchased before 2015. Thirty-eight percent were purchased before 2000. The average length of ownership has been virtually the same for different size properties.
- Net operating income from rental housing investments has grown at faster rates than the CPI.



14. Allowable Annual Rent Adjustments under Other Rent Stabilization Laws in California

*Photo credit:
Economic Roundtable*

Ordinances Adopted before 1987

Rent stabilization ordinances are currently in effect in about 33 local jurisdictions in California.

In the early to mid-1980's, rent controls were adopted by San Francisco, San Jose, Oakland and a few smaller cities with a high proportion of tenants – Berkeley, East Palo Alto, Santa Monica, West Hollywood – and a few other cities. Few if any rent ordinances were adopted between 1987 and 2015.

Currently, under most of the ordinances originally adopted before 1987, annual allowable rent increases are limited to a percentage of the increase in the CPI (Oakland and San Francisco– 60 percent of CPI, Berkeley – 65 percent of the CPI, Santa Monica and West Hollywood – 75 percent of CPI, and East Palo Alto – 80 percent of CPI.) Since 2020, three cities – Oakland, Santa Monica, and West Hollywood – have placed a three percent cap on allowable annual increases. Under the San Jose Ordinance, the allowable increase is fixed at five percent per year.

Rent Freezes during the Pandemic

During the pandemic, apart from Los Angeles, other cities placed freezes on annual allowable increases. These included a freeze in Los Angeles County from March 2020 to March 2023, and a freeze in West Hollywood from April 2020 to March 2023. Santa Monica did not impose a freeze. However, in November 2022, it amended its charter provision that contained its rent law in order to rollback a portion of its 2022 rent increase of six percent that had been authorized on the basis of its CPI standard.

Ordinances Adopted Since 2015

The tightening of the rental market in the last ten years has led to the adoption of local rent legislation and, as mentioned, a state ceiling on increases in apartment rents of units that are not regulated by local ordinances. Since 2016, rent laws have been adopted by about 21 other jurisdictions, including Los Angeles County, Culver City, Inglewood, and Pasadena. Eight of those ordinances were adopted between 2020 and 2022.

Eight of the 21 recent ordinances limit the annual rent increase to less than 100 percent of the increase in the CPI.

Floors and Ceilings on Across-the-Board Annual Allowable Increases

Four of the ordinances that were adopted prior to 1986, now place a three percent ceiling on annual allowable increases and two of the ordinances set a floor of three percent on annual allowable increases.

Commonly, ceilings on allowable annual increases have been adopted during periods of high inflation. As indicated, in 1979, Los Angeles adopted a seven percent ceiling. The CPI increases during those years were 1978 – 7.4 percent, 1979 – 10.7 percent, 1980 – 15.8 percent, 1981 – 9.8 percent.

Twelve of out of the 33 jurisdictions that currently have rent-control have either four or five percent ceilings, or fix the annual allowable increase at four or five percent. In Los Angeles County, the ceiling is eight percent, and the ceiling is 10 percent in eight ordinances.

California law provides for a five percent floor on annual allowable increases. Nine of the 33 rent control ordinances contain either floors on annual allowable increases ranging from one to five percent or provide for fixed annual increase allowances amounts in this range (*Table 19*). Under four of those ordinances, the floor is also the ceiling.

About half of the ordinances place a ceiling on annual allowable increases in the range of three to five percent (*Table 20*).

Table 19. Rent Stabilization Ordinance Floors on Annually Allowable Increases

Floor	Number of Ordinances
1%	2
2%	2
2% - 3%	1
3%	3
4%	2
5%	5

Source: Economic Roundtable team analysis.

Table 20. Rent Stabilization Ordinance Ceilings on Annually Allowable Increases

Ceiling	Number of Ordinances
3%	8
4%	4
5%	7
7%	3
10%	8

Source: Economic Roundtable team analysis. Note: three jurisdictions do not set a ceiling on annual allowable increases.

The following three tables summarize the annual allowable increase standards under state and local rent stabilization laws. *Table 21* compares the current and annual increase standards of the older ordinances, including restrictions that were imposed during the pandemic. *Table 22* sets forth standards under the new round of ordinances. *Table 23* provides an overview of the ordinances comparing the combinations of allowed annual increases, floors and ceilings.

The chart and schedule of allowable rent increases shown in *Table 23* illustrates that under Los Angeles’ RSO in effect prior to the pandemic, the allowable annual increases were greater than those permitted under a majority of the

Table 21. Annual Allowable Rent Increases under California Rent Ordinances, Adopted Prior to 1987

City/County	Percent of CPI	Floor	Ceiling
Berkeley	65% of CPI		7%
Beverly Hills	100% of CPI		3%
East Palo Alto	80% of CPI		10%
Hayward	fixed %	5%	5%
Los Angeles City	100% of CPI	3%	8%
Los Gatos	70% of CPI		5%
Oakland	60% of CPI		3%
Palm Springs	75% of CPI		10%
San Francisco	60% of CPI		7%
San Jose	fixed %	5%	5%
Santa Monica	75% of CPI		3%
West Hollywood	75% of CPI		3%

Source: Economic Roundtable team analysis.

Table 22. Annual Allowable Rent Increases under California Local Rent Ordinances and State Law, Adopted Since 2016

City	Percent of CPI	Floor	Ceiling
California Tenant Protection Act	5% + CPI	5%	10%
Alameda City	70% of CPI	1%	5%
Antioch	60% of CPI		3%
Baldwin Park	100% of CPI	1%	5%
Bell Gardens	50% of CPI ^(a)		4%
Commerce	5% + CPI	5%	10%
Concord	60% OF CPI		3%
Cudahy	100% of CPI		3%
Culver City	100% of CPI	2%	5%
Fairfax	75% of CPI		5%
Inglewood (5+ units)	100% of CPI	3%	10%
(1-4 units)	5% + CPI	5%	
Larkspur	5% + CPI		7%
Los Angeles County (unincorporated)	100% of CPI	2-3% ^(b)	8%
Maywood	100% of CPI		4%
Mountain View	100% of CPI	2%	5%
Ojai	Fixed %	4%	4%
Oxnard	Fixed %	4%	4%
Pasadena	75% of CPI		10%
Pomona	100% of CPI		4%
Richmond	60% of CPI		3%
Sacramento	5% + CPI		10%
Santa Ana	80% of CPI		3%

Source: Economic Roundtable team analysis. Notes: (a) An additional 3% is permitted if the rent is below 80% of Fair Market Rent as determined by U.S. H.U.D. (b) LA County ordinance: If the change in CPI is between negative two percent (-2%) and one percent (1%), the maximum allowable annual Rent increase will be equal to the change in CPI plus two percent (2%); or If the change in CPI is less than negative two percent (-2%), no annual Rent increase is permitted.

Table 23. Allowable Annual Rent Increases, with Percent Floors and Ceilings

	Percent Floors and Ceilings										CPI Increase			
	0	1	2	3	4	5	6	7	8	9	10	2%	5%	8%
LA RSO pre-May 2020	100% of CPI										Allowable Rent Increase			
											3%	5%	8%	
Antioch	60% of CPI										1.2%	3%	3%	
Richmond	60% of CPI										1.2%	3%	3%	
Santa Monica	75% of CPI										1.5%	3%	3%	
W. Hollywood	75% of CPI										1.5%	3%	3%	
Santa Ana	80% of CPI										1.6%	3%	3%	
Beverly Hills	100% of CPI										2%	3%	3%	
Cudahy	100% of CPI										2%	3%	3%	
Bell Gardens	50% of CPI										1%	2.5%	4%	
Pomona	100% of CPI										2%	4%	4%	
Maywood	100% of CPI										2%	4%	4%	
Ojai				Fixed							4%	4%	4%	
Oxnard				Fixed							4%	4%	4%	
Alameda City	70% of CPI										1.4%	3.5%	5%	
Los Gatos	70% of CPI										1.4%	3.5%	5%	
Fairfax	75% of CPI										1.5%	3.75%	5%	
Baldwin Park	100% of CPI										2%	5%	5%	
Culver City	100% of CPI										2%	5%	5%	
Mtn. View	100% of CPI										2%	5%	5%	
Hayward				Fixed							5%	5%	5%	
San Jose				Fixed							5%	5%	5%	
Berkeley	65% of CPI										1.3%	3.25%	5.2%	
Larkspur					5% + CPI							7%	7%	7%
LA County	100% of CPI										2%	5%	8%	
Oakland				60% of CPI							1.2%	3%	4.8%	
Palm Springs				75% of CPI							1.5%	3.75%	6%	
Pasadena				75% of CPI							1.5%	3.75%	6%	
East Palo Alto				80% of CPI							1.6%	4%	6.4%	
Inglewood 5+ units				100% of CPI							2%	5%	8%	
Commerce					5% + CPI							7%	10%	10%
Inglewood 1-4 units					5% + CPI							7%	10%	10%
Sacramento					5% + CPI							7%	10%	10%
California state law, applicable if no local ordinance					5% + 100% of CPI							7%	10%	10%

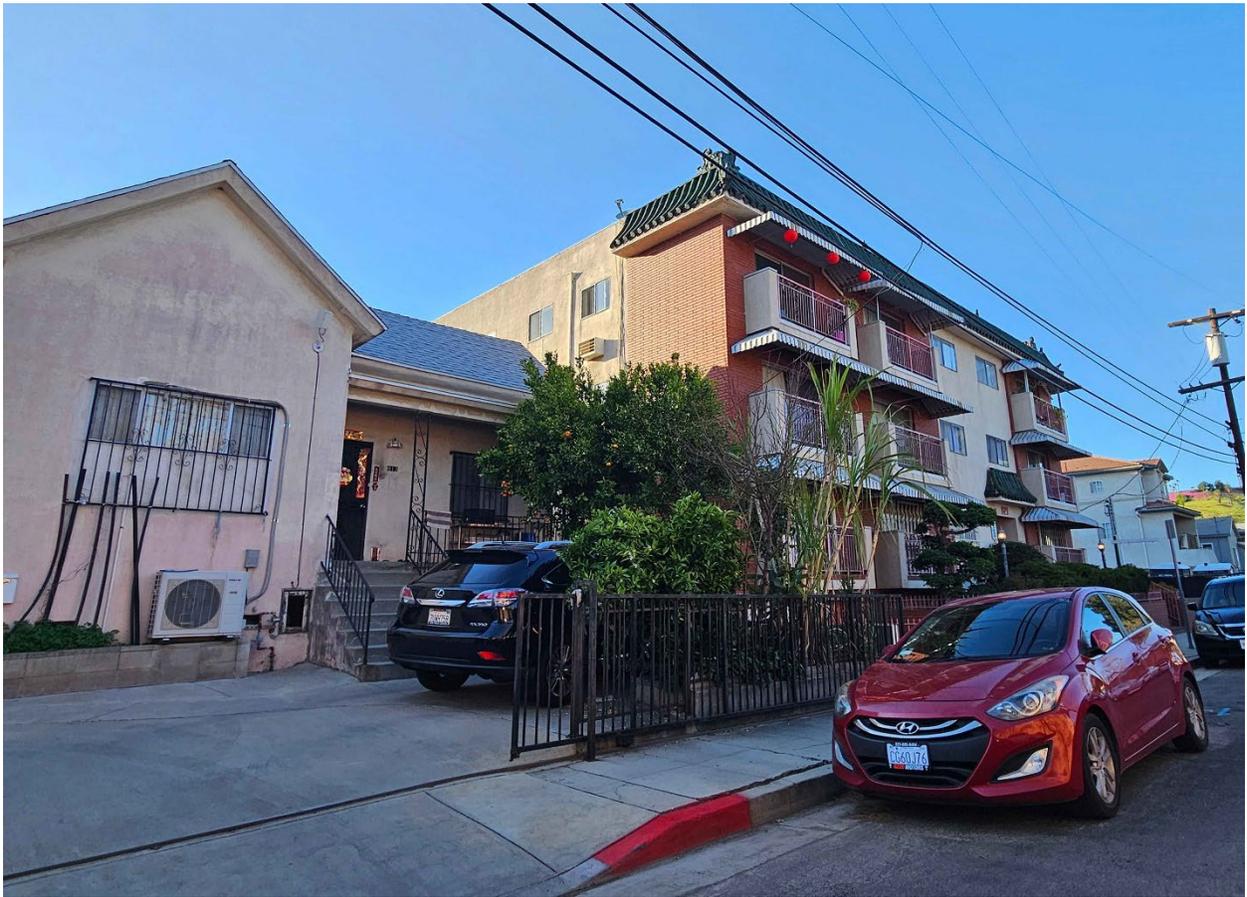
ordinances now in effect in other cities (Table 22). Due to its floor on allowable increases, it permitted higher increases than most of the current laws in other jurisdictions would now permit if the rate of increase in the CPI is under three percent.

Los Angeles' RSO ceiling of eight percent contrasts with ceilings of three, four or five percent in a majority of the current rent stabilization laws. Rather than functioning within the context of continual restrictions on rent increases, the annual increase operates within a vacancy decontrol framework. In Los Angeles, the rents of most units are reset at market levels within a five-year period. Now, and at other times, the five-year periods have included years with steep increases in market rents.

The outcome of the RSO under the standard in effect before the pandemic was to compound move-in rents set under shortage conditions with rent increases for tenants after they moved in that would exceed the percentage increase in the CPI in years with low inflation rates.

Findings

- In the 1980's, rent legislation was adopted by Los Angeles, San Francisco, Oakland, San Jose, Santa Monica, Berkeley, and West Hollywood and a few other cities.
- Within the last eight years, the tightening of the rental market has led to the adoption of local rent legislation in fifteen other jurisdictions, including Los Angeles County, Culver City, Inglewood, and Pasadena and to the adoption of a state ceiling on increases in apartment rents of units that are not regulated by local ordinances. Eight of those ordinances were adopted between 2020 and 2022.
- Most rent ordinances tie annual allowable rent increases to all or a portion of the percentage increase in the CPI and place a ceiling on the allowable increase pursuant to the CPI standard.
- Fifteen of the ordinances limit the annual rent increase to less than 100 percent of the increase in the CPI.
- Twenty-two of the ordinances now in effect place a ceiling of either three, four, or five percent on allowable rent increases based on a CPI standard, or fix the annual increase amount at four or five percent.
- Under Los Angeles' RSO in effect prior to the pandemic, the allowable annual increases were greater than those permitted under a majority of the ordinances now in effect in other cities.
- From 2010 to 2020, the outcome of the RSO under the standard in effect before the pandemic was to compound move-in rents set under shortage conditions with rent increases for tenants after they moved in that exceeded the CPI increase in years with low inflation.



15. Impacts of Alternative Policies Related to the Efficacy of the RSO Annual Adjustment Formula

*Photo credit:
Economic Roundtable*

The Annual General Adjustment Standard

The issue of what the annual general adjustment should be has reemerged in a period of earthquakes in the housing and real estate market including: 1) a period in which landlords could not terminate tenancies for non-payment of rent by tenants who in turn were economically devastated by the impacts of a pandemic, 2) a meltdown in the property insurance market, causing soaring insurance costs 3) an inflationary surge adversely impacting tenants and landlords, and 4) soaring market rents.

A starting and ending point for considering the efficacy of the annual general adjustment standard in the RSO and setting forth any recommendations about its provisions is to understand its scope, the extent of its impacts and the context in which it operates.

The RSO is an alternative to a situation that is considered less desirable, an absence of rent regulation. It performs a particular role in Los Angeles housing policy. The limits that rent regulations place on rent increases for sitting tenants are limits that historically the market has placed on feasible rent increases in other parts of the nation where rental markets are not as tight.

The RSO provides security of tenure by limiting the rent increases of a tenant after taking possession. Without this critical protection, entering into a tenancy would be a gamble with no future certainty about what rent increases may occur. On the other hand, because of vacancy decontrol, the initial rent is not regulated, so the RSO is not preserving the affordability of housing, except for long-term tenants. Only 53 percent of RSO tenants have been in their units for five or more years.⁸⁴

Vacancy decontrol is mandated by state law, the Costa Hawkins Act. The City of Los Angeles, along with all rent-control jurisdictions in the state, is required to have vacancy decontrol. This requirement preempts local controls over initial rent levels for new tenants.

In other words, for most units, the RSO places brakes on the pace in which rents may be brought to market levels, rather than substituting for market level rent increases with a CPI standard. It only regulates the rent increases during the window period between changes in tenancies, but not the base rents for each tenancy.⁸⁵ It is a limit on rent increases that are on top of market rent increases, rather than an overall limit on rent increases. Its impact differs among properties based on the frequency of tenant turnovers.

The Annual Rent Adjustment Standard – Issues and Options

Most ordinances tie the annual increase allowance to the percentage increase in the CPI and use the *CPI All-Items, All Urban Consumers Index*. Standardly, this framework is limited by a ceiling on the amounts of the allowable increase.

A number of options arise in regard to the selection of an annual rent adjustment standard. These issues include:

1) Should the annual rent increase standard be based on the increase in the CPI or be a fixed percentage or dollar amount, or based on a study of apartment operating costs?

2) If a CPI standard is adopted, which CPI index should be used?

3) If a CPI standard is adopted, what percentage of the annual percentage increase in the CPI index should be used?

4) Should there be floors and/or ceilings on the allowable increase, and/or should a declining percentage of the percentage increase in the index be used?

Drawbacks of the Alternative of a Fixed Percentage or Fixed Dollar Methodology

Under a few ordinances, allowable annual rent increases are one fixed amount. Under the San Jose ordinance, the annual allowable rent increase is five percent. An advantage of such an approach is that it simplifies the law because the annual increase amount is always the same. However, this approach disconnects the allowable increase amount from actual trends in prices, wages, and the economy. A view that a reasonable middle amount can be found on the basis of reasonable predictions of future trends would be grounded on an illusion that future economic trends can be reliably predicted.

In the past years, when fixed percentage standards have been adopted, correcting amendments have been deemed necessary when the amount set forth in the standard no longer reflected market conditions. Los Angeles, San Francisco, and Oakland were compelled to make such correcting modifications when their annual increase amount became outdated, and eventually adopted CPI-based standards. San Jose adjusted its fixed annual amount after it had been exceptionally high, eight percent per year for 20 years. However, these modifications were after a significant period in which the particular fixed annual increase amount was out of step with the prevailing price trends, as opposed to a CPI standard that modifies the annual increase allowance in accordance with CPI trends as they occur.

Allowable Annual Increases Based on Apartment Operating Cost Study Using a Weighted Cost Index

The use of the *CPI All-Items Index* to determine annual increases has been criticized on the basis that the CPI takes into account the market basket of goods purchased by an average household, which differ substantially from the basket of expenses associated with operating an apartment building. On this basis, in past decades, some jurisdictions conducted an operating cost study and used a "weighted" operating cost index based on the types of expenses incurred

by apartment owners in order to tie allowable annual rent increases to trends in apartment operating costs.

When this methodology is used, estimates are made of the ratio of each type of operating expense and net operating income (NOI) to gross income and of the rate of increase in each type of operating cost. On this basis, an estimate is made of the amount of rent increase required to cover each type of cost increase. For example, if water costs equal two percent of gross income and increased by 10 percent, then a 0.2 percent (2 percent x 10 percent) rent increase is required to cover this cost increase.

In addition, a CPI related adjustment of NOI, which typically averages about 65 percent of gross income, is included. For example, if NOI averages 65 percent of gross income and the CPI has increased by five percent, a 3.15 percent rent adjustment (65 percent x 5 percent) would be required to cover this factor. The overall rent adjustment is set at a level that would cover the sum of operating cost and net operating income adjustment factors.

The 1984 study for the RSO included a detailed description of how a weighted operating cost index could be developed for the purpose of setting annual rent increases. The report set forth a list of indexes that could be used to determine the percentage increase in each type of cost.⁸⁶

From a practical point of view, there are serious limitations to the weighted index approach. By necessity, estimates of annual increases for a substantial majority of apartment costs have been based on increases in the CPI, because information on actual increases in a large portion of apartment costs - maintenance, management, and insurance - is not publicly available and is not determined by rates that are set by public agencies.

Table 24. CPI and non-CPI Adjusted Cost Factors in Operating Cost Study

Factors	Weight of Factor Increase Measured by a CPI Index	Notes
Maintenance & Other	.10	
Insurance	.03	Insurance CPI may be used
Self-Labor & Outside Service	.02	
Management	.05	
Net Operating Income	.65	
Total Weight of Factors Represented by CPI	.85	

Factors	Weight of Factor Increase Not Measured by a CPI Index	Notes
Property Taxes	.09	2% per year
Water & Sewer	.04	Rate Increases
Solid Waste Collection	.02	Rate Increases
Total Weight of Factors Not Adjusted by CPI	.15	

Source: Economic Roundtable team analysis.

In contrast, only a small part of the weighted cost index is based on costs for which there is a significant amount of readily available information that can be used to measure the ratios of those costs to gross income and provide precise measures of increases in these costs. This portion consists of costs that are publicly regulated, e.g., water, sewer, property taxes, and common area utilities.

Furthermore, on average, 65 percent of apartment owners' rental income consists of net operating income (NOI) that covers cash flow and debt service rather than operating expenses. In a weighted cost analysis an adjustment to the NOI share of rental income would be tied to changes in the CPI.

In totality, an operating cost study methodology is more sensitive to some of the changes in apartment costs than the CPI standards that are commonly contained in rent control ordinances because it considers increases in water, sewer, refuse, gas, and electricity costs. However, this precision applies to only 35 percent of the overall rent increase calculation.

An example of the use of a weighted operating cost index is shown in *Table 24*.

Furthermore, from a public policy-making perspective, there are other drawbacks to basing the annual rent increase on an annual apartment operating cost study. Such analyses are particularly complex and unintelligible to the average citizen.⁸⁷ As a result, although they may be performed in an objective manner, the results of such studies are perceived as an outcome of magic or political pressure designed to lean towards a particular outcome. When this methodology is used, either a city council or a rent board must undertake the difficult task of determining what is reasonable based on the analysis in the operating cost study and public comments about how the analysis should be modified in order to be more accurate and reasonable. In the end, it is likely that its decision will be seen as "political."

The history of the use of the operating cost methodology in Berkeley is instructive and ironic. Because the Berkeley Rent Board was often viewed as tenant dominated, its use of an annual weighted operating cost study in order to determine allowable annual rent increases was often viewed by apartment owners with distrust. In 2006, in response to demands tied to a lawsuit by apartment owners, the Rent Board agreed to place an initiative on the ballot that replaced the Rent Board's power to set the annual rent adjustment with an annual rent increase to 65 percent of the percentage increase in the CPI. This initiative received the stamp of approval of the apartment owners and the Rent Board and was approved by the voters. In fact, over the life of Berkeley's rent stabilization program, the operating cost study methodology was more favorable to apartment owners than an annual adjustment set at 65 percent of the increase in the CPI would have been.

In 2012, Santa Monica amended its rent law to provide for annual rent increases tied to the percentage increase in the CPI, in lieu of performing

annual operating cost studies in order to determine the amount of the annual general adjustment.

CPI (Consumer Price Index) Based Standards

As indicated, most rent laws tie annual allowable rent increases to the percentage increase in the CPI. Since the pandemic, several of the ordinances that were adopted decades ago have been amended to include ceilings on the annual allowable increase and most of the new ordinances contain a ceiling.

Selection of a Price Index for Setting Annual Allowable Rent Increases

In rent stabilization ordinances, the **CPI All-Items All Urban Consumers for the Standard Metropolitan Statistical Area (SMSA)** is standardly designated as the applicable CPI. This standard has been used under the RSO.⁸⁸

In fact, there are a number of CPI indexes that are based on the prices of particular commodities or types of services. The indexes include specific measures of virtually every type of cost and service.

In the public forum, most discussion and consideration of the Consumer Price Index is centered on *CPI All-Items Index*. It is the standard that is used to measure inflation, which is based on a weighted index of the prices of the household basket of goods and services. This index is standardly used in ordinances regulating rates or setting annual fees, such as utility rate ordinances and business fee ordinances. Also, it is standardly used in commercial leases that provide for annual rent adjustments.

Social Security increases are based on an **All-Items Index**, but use a basket of goods and services for **All Urban Wage Earners** rather than **All-Urban Consumers**.

At various times, tenant and/or landlord representatives have proposed the use of alternates to the *CPI All Urban Consumers All-Items Index* on the basis that an alternate index would be more reasonable. Each proposal includes a justification for the particular index that is most favorable to its proponents in the particular year when the proposal was made. In another city, decades ago, landlord and tenant groups were each vigorously advocating the use of a particular index that favored their interests in the pending hearing over the annual general adjustment. In the middle of the hearing process the next bi-monthly index amounts were published, which happened to reverse the index that was most favorable to each interest. Suddenly the debate died.

All-Items Indexes

The *CPI All-Items Index* takes into account a basket of household costs weighted in accordance with their shares of average household expenditures.

Notably, “shelter” constitutes 35.8 percent of the market basket in the *All Items Index*. In measuring shelter costs, rent levels are used as a proxy to measure housing costs for homeowners.⁸⁹

The weights of the household costs in the *All Urban Consumers All-Items Index* are: food and beverages – 14.4 percent, shelter – 35.8 percent, energy– 3.3 percent, water, sewage and trash collection – 1.1 percent, household furnishings and operations – 4.5 percent, apparel – 2.3 percent, transportation – 15.9 percent, medical care and medical commodities – 8.0 percent, recreation – 2.0 percent, education – 2.0 percent, communication and information – 3.4 percent, other goods and services – 7.3 percent.⁹⁰ Obviously, these costs are quite different than the basket of costs associated with operating apartment buildings.

The All Urban Consumers: All Items Index compared with the Urban Wage Earners and Clerical Workers: All Items Index

The *Urban Wage and Clerical Workers All-Items Index* uses the costs of a different grouping of households while using about the same basket of households costs. The rationale for using of the *CPI for Urban Wage Earners and Clerical Workers All Items Index*, rather than the *CPI All-Urban Consumers Index*, is that the former more accurately reflects changes in the cost of living for renters because renters are more likely to be wage earners and clerical workers. Also, it is used as the basis for annual Social Security adjustments.

In fact, the differences between the overall increases in the *All Urban Consumers* and the *Urban Wage Earners and Clerical Workers* have been very small, although the differences in particular years have been as much as 0.6 percent. The index showing the greatest increases has varied. Neither index has been consistently higher than the other. Cumulatively, from 2000 through 2023, the *All Urban Consumers Index* increased by 87.4 percent compared to an increase of 88.2 percent in the *Urban Wage Earners and Clerical Workers Index*.

The All Items Less Shelter Index Compared with the All Items Index

One index, the *All Items Less Shelter Index*, is based on the costs of a market basket of household costs excluding housing.

The difference between the increases in the *All Items* and the *All Items Less Shelter* indexes have been much greater than the differences between the increases in the *All Urban Consumers* and the *Urban Wage Earners and Clerical Workers* indexes. As indicated, in the *All-Items Index*, shelter costs constitute one-third of the overall market basket

The use of an *All Items Index* in order to determine allowable rent increases is subject to the criticism that in the context of rent stabilization it is "circular" to the extent that it includes exceptional increases or decreases in rents and house prices as a factor in determining what rent increases should be permitted.⁹¹

In fact, consistent with the trend of soaring rents and house prices in the Los Angeles region, the *CPI All-Items Index* has increased at a greater rate than the *All-Items Less Shelter Index*. From 2000 through 2023, the annual increase in the *CPI All Items Index* for the area has exceeded the increase in the *CPI All Items Less Shelter Index* for the area by an annual average of 0.5 percent. The average increase in the *All-Items Index* was 2.8 percent compared to an average increase in the *All-Items Less Shelter Index* of 2.3 percent (*Table 25*).

Table 25: Increases in All Items & All Items Less Shelter CPI Indexes Compared, with Percent Increase Over Prior Year

Year	All items Consumer Price index	All items Less Shelter Consumer Price index	Increase in All items index compared to increase in All items Less Shelter Index
2001	3.3%	2.7%	0.6%
2002	2.8%	1.3%	1.4%
2003	2.6%	1.8%	0.9%
2004	3.3%	2.3%	1.0%
2005	4.5%	3.5%	0.9%
2006	4.3%	3.4%	0.9%
2007	3.3%	1.5%	1.8%
2008	3.5%	3.7%	-0.2%
2009	-0.8%	-1.7%	0.9%
2010	1.2%	2.5%	-1.3%
2011	2.7%	3.8%	-1.1%
2012	2.0%	2.1%	0.0%
2013	1.1%	0.6%	0.5%
2014	1.3%	0.8%	0.6%
2015	0.9%	-0.6%	1.5%
2016	1.9%	0.3%	1.6%
2017	2.8%	1.7%	1.1%
2018	3.8%	3.1%	0.7%
2019	3.1%	1.8%	1.3%
2020	1.6%	0.8%	0.8%
2021	3.8%	5.4%	-1.5%
2022	7.4%	9.3%	-1.9%
2023	3.5%	2.4%	1.1%

Cumulative Increases Pre-Pandemic, 2000-2020:

Total	62.3%	41.6%
Annual Average	2.5%	1.8%

Cumulative Increases, 2000-2023:

Total	87.4%	67.0%
Annual Average	2.8%	2.3%

Source: Economic Roundtable team analysis; U.S. Bureau of Labor Statistics, Consumer Price Index for All Urban Consumers for Los Angeles and Orange Counties

On the other hand, in 2021 and 2022, the increase in the *All Items Less Shelter Index* exceeded the increase in the *All Items Index* by over 1.5 percent. The City and County freezes on allowable increases and pandemic restrictions on rent increases in other jurisdictions, as well as a temporary downward cycle in market rents, may have played a substantial role in this outcome.

A Price Index Tailored by the City to Reflect Apartment Operating Costs

The franchise agreements between the Sanitation Department and the solid waste collection companies contain annual price adjustment standards that are based on a weighted index that is specifically tied to CPI indexes and other industry indexes for particular types of costs. (For a description of this standard see *Chapter 15* of this report.) This index was formulated at the outset of the contracts rather than recreated on an annual basis.

However, the context for franchise agreements differs from the context of annual general rent adjustment. The operating costs of a sanitation company consume a high percentage of revenues, while apartment operating costs take up only about 35 percent of rental income. Therefore, such a weighted index would only give a 35 percent weight to operating costs. Furthermore, property taxes would constitute a substantial share of a 35 percent weight. However, the ratio of property taxes to rental income varies enormously among properties. The combination of the two percent cap on annual property tax increases mandated by California's Proposition 13, but intermittent extreme increases of up to a few hundred percent when properties are sold, defies the establishment of a standard rate of increase for this cost.

Recommended Index

The *All-Items Less Shelter Index* is recommended for determining the annual allowable rent increase for RSO units. Its use will remove the circularity associated with using trends in market rents, which are heavily influenced by the shortage conditions that motivated the adoption of the RSO.

Limits on Allowable Increases under CPI Standards

The Percentage of CPI Increase Used in the CPI Standard

The selection of a percentage increase in the CPI to be utilized in the CPI standard that determines annual allowable rent increases is usually a contested issue that can be viewed in many ways.

Several factors temper the weight of the annual allowance standard. If the increases in the CPI return to their pre-pandemic level – three percent a year or less – the differences between a 100 percent or 60 percent of CPI standard, for example, would be 1.2 percent per year or less. Also, as indicated, in a

substantial portion of units, the annual increase standard has limited weight because rents are often reset within a few years pursuant to the vacancy decontrol provision.

An annual rent increase guideline tied to the full percentage increase in the CPI can be based on the concept that the purpose of the RSO is to prevent increases that are out of proportion with overall price trends in the economy, rather than to block reasonable rent increases. On the other hand, the annual increases have been within the framework of vacancy decontrol.

Consequently, the annual rent increases that have been authorized under the RSO are an addition to the vacancy increases that are far above the annual allowable increases if a unit had not turned over, and commonly well above the percentage increases in the CPI.

A common paradigm about annual rent increases is that they should reflect increases in apartment operating costs. To the extent that increases in apartment operating costs roughly mirror increases in the CPI, this connection stands up. Under this circumstance, an annual increase in the range of 35 percent of the percentage in the CPI would cover those cost increases but would not allow for any growth in net operating income. The California Supreme Court has ruled that “indefinitely” freezing net operating income would be confiscatory.

[An] ordinance may properly restrict landlords' profits on their rental investments, it may not indefinitely freeze the dollar amount of those profits without eventually causing confiscatory results. Cotati Alliance, supra, at p. 293 ["If the net operating profit of a landlord continues to be the identical number of dollars, there is in time a real diminution to the landlord which eventually becomes confiscatory."]⁹²

In years when operating expenses increase at the same rate as the CPI, annual increases equal to 35 percent of the CPI increase would cover operating cost increases, but would not provide for growth in net operating income from units that have not turned over.

The issue of what percentage growth in net operating income is required to permit a fair return has not been salient in the context of apartment rent controls, and fair return applications have been rare under apartment rent stabilization ordinances. This is because vacancy decontrol has permitted rent increases well above the amount needed to permit a fair return, which is usually defined as the pre-rent control net operating income adjusted by the percentage increase in the CPI since the adoption of the ordinance.

Allowable growth in net operating income has been an issue in cases involving fair return adjudications under mobile home park space rent regulations that either do not permit any additional rent increases upon vacancies or limit the amount of the increase upon a vacancy to a moderate amount (e.g., five

percent). These regulations commonly limit the annual increase to less than 100 percent of the percentage change in the CPI. (Approximately one-hundred California jurisdictions regulate mobile home park space rents.)

The California Court of Appeal has repeatedly rejected the view that net operating income must be permitted to grow by 100 percent of the percentage increase in the CPI and has upheld ordinances or rent board adjudications that allow for growth in net operating income by 50 percent of the percentage increase in the CPI.⁹³

In fact, increases in operating expenses have not mirrored increases in the CPI. On the one hand, property tax increases are limited to two percent per year except when a property is sold. On the other hand, insurance costs, which amounted to only a small percentage of rent income prior to about 2015, have soared. Also, increases in utility costs have substantially exceeded increases in the CPI, but utility cost increases are usually equal to 10 percent of rental income or less; therefore, an increase in these costs usually amounts to a small percentage of rental income.

The bottom line is that apartment operating expenses have been increasing at faster rates than the CPI. However, because overall rental income has been increasing at a rapid rate and operating costs consume only about 35 percent of rental income, growth in net operating income and the other forms of return on investment and appreciation have exceeded the rate of increase in the CPI.

Table 26. Impacts of Rent Adjustments on Investment Returns, with Low and High Inflation Rates

	Base Year	Year 2	Year 2
Total Investment	\$6,000,000		
Mortgage	\$3,600,000		
Cash Investment	\$2,400,000		
CPI Increase		2%	8%
Rent Increase Standard		full CPI	75% of CPI
Allowable Rent Increase		2%	6%
Operating Cost Increase		2%	8%
Rent	\$500,000	\$510,000	\$530,000
Operating Expenses	\$200,000	\$204,000	\$216,000
Net Operating Income (NOI)	\$300,000	\$306,000	\$314,000
Increase in Net Operating Income Over Base Year		2%/ \$6,000	5%/ \$14,000
Mortgage Interest	\$216,000	\$216,000	\$216,000
Cash Flow (NOI - Mortgage Interest)	\$84,000	\$90,000	\$98,000
Cash Flow/Inflation Adjusted Cash Investment	%	%	%
Appreciation in Property Value (Increase in NOI/6% capitalization rate)		\$100,000	\$233,333

Source: Economic Roundtable team analysis.

The main impact of differences in the annual rent increase allowance is on the rents of longer-term tenants. Its main impact on owners is on owners who have a low rate of turnover on their properties, and/or a low cash flow, and/or rely heavily on the income from their rental property to cover their living costs.

The obvious purpose of ceilings on allowable annual rent increases is to reduce the hardships that rent increases may place on tenants. A substantial portion of tenants are in an economically vulnerable position and may not be obtaining gains in income that keep up with the rate of inflation.

The impacts of CPI standards differ during times of high and low inflation. Due to the leveraging (mortgage financing) factors generally associated with apartment purchases, in times of high inflation, less than full CPI increases may still garner greater increases in net cash flow than full CPI increases in times of low inflation. *Table 26* compares returns from a full CPI increase based on two percent inflation with a 75 percent of CPI increase based on eight percent inflation.

A Descending Percentage of CPI Standard

As an alternative to setting a fixed ceiling on allowable annual rent adjustments, a few ordinances governing mobile home park space rents provide for a descending percentage of CPI increases above a specified amount, (e.g., 100 percent of the CPI increase up to x percent, 50 percent of the CPI increase above y percent). This type of standard recognizes that there are different impacts when increases in the CPI that are low vs high. Rather than simply applying a fixed share of the CPI increase to the allowable rent increase, the amount of the increase is scaled. For example, the share of the CPI change used to set the allowable rent increase is different if the increase is two percent rather than six percent.

Differences among the Impacts of Alternate Allowable Annual Rent Increases

Due to vacancy decontrol, annual rent increase standards have only a moderate impact on the overall trajectory of rents in the City of Los Angeles.

From the perspective of owning rental property, the main differences arising out of alternate annual adjustment standards will be on the rate of growth in the net operating income of properties, with consequential impacts on cash flow. In the case of recent purchasers who typically are operating on a thin cash flow margin at the outset of their investment, the impact may be dramatic. However, for a substantial portion of owners, a few more years of ownership will garner large rent increases that can be realized from upcoming turnover of their units.

Consideration of Differing Allowable Rent Increases for Smaller Properties

Traditionally, rent regulations have provided for uniform annual allowable increases for all properties covered by the regulation. Differences in allowable increases have been based on differences in the level of utility expenses covered by the apartment owner, rather than the size of the property. The paradigm has been that rent increases should be stabilized and exceptions to the across-the-board rule would be based on operating cost factors, service levels, and history of rent increases for the particular property, rather than the personal circumstances or purchase financing arrangements of the owner or the size of the property. In fact, in fair return cases under rent regulations, appellate courts in California and other states have ruled that differences in allowable rents based on differences in financing arrangements have no rational basis.⁹⁴

Currently, the RSO applies to 181,588 units in 70,314 rental properties with between two and four units. Substantial concerns have been expressed that “mom-and-pop” owners have been or will be forced out of the rental business as a result of the nearly four-year freeze (May 2020 to February 1, 2024) on annual rent increases, and will be replaced by outside investors who will take less interest in the welfare of their tenants. No systematic research has been identified that would either confirm or negate these concerns.

A flip side of the view that “mom-and-pops” have been squeezed is that, apart from the freeze period, they have been the beneficiaries of the rapidly increasing rent levels prior to the freeze, and during the freeze have been able to obtain large increases in rents as units have turned over. Consequently, they have realized large increases in cash flows and benefited from large appreciation of investments that were substantially leveraged at the outset. The data from the LAHD registration database indicates that the average rents in properties with four units or less increased from \$1,502 in 2017 to \$1,876 by January 2023, an increase of 25 percent, compared to the 24.3 percent increase in the CPI. Of course, in some properties, more likely small properties, there has been no turnover.

The other side of a policy that allowed for greater rent increases for small properties is that tenants in those properties would experience larger rent increases than the balance of the tenant population, regardless of whether their current rent level was high or low compared to prior years rent levels for the same unit.

A common view has been that if mom-and-pops are not permitted higher rent increases, they will be replaced by out of town investors. An alternative view is that if higher rent increases are permitted for smaller properties - out of town investors will pay even more per unit for those properties than for larger properties and that the increased values of smaller properties, which are already approaching \$400,000 per unit for three and four unit properties, will provide even greater incentives for the mom-and-pops to sell.

Another alternative view is that in the context of vacancy decontrols, the annual general adjustment standard will not have a significant impact on ownership patterns of smaller properties.

If higher rent increases are allowed for smaller properties, it is recommended that other conditions should be attached relating to consideration of the overall income of the property compared to prior years, the level of past rent increases for the particular unit, and conceivably the level of rent losses caused by the eviction moratorium. Certainly, such a step would impose additional staffing burdens on the Housing Department and bureaucratic burdens on owners who would want to benefit from the standard. Consequently, a standard of this type should be as objective as possible and as easy as possible for an applicant to document for application purposes. In regard to documentation of past rent levels, under the RSO owners have been required to submit information on rent levels and the move-in dates of their tenants since 2017.

Other Policy Recommendations:

City Relief for Owners Severely Impacted by the Moratorium

The impacts of the eviction moratorium have varied enormously between properties. At this point, records are available on how many households and apartment owners have obtained relief. However, empirical data about the extent of losses relative to overall rental income has been limited to national surveys of large property owners. The most severe impacts most probably would have been on small properties since each case of lost rent could have been large to relative to overall income.

If additional relief is provided for such owners, it is recommended that the relief should come from the general public (the City budget) rather than in the form of additional rent increases to be paid by tenants who have paid all of their rent.

Increased Funding of the LAHD in order to enforce the Registration Requirement

Currently, about 69 percent of all RSO units are properly registered and in the Rent Registry, leaving 31 percent with unknown rent amounts and dates of last tenant move-in.

This requirement is important because lack of full compliance raises the possibility that there are systematic differences between properly registered units, which provided much of the statistical basis for the analysis in this report, and policy considerations based on this analysis, and units that are not properly registered.

The funding for the program, \$38.75 per unit per year (\$3.22 per month, or about 0.2 percent of the average rent), is disproportionately low relative to the critical place of housing protections and housing policy in the life of 650,832 tenant households and 149,533 rental property owners in the City.⁹

Annual Studies of Increases in Utility Costs

Commonly, in discussions about rent increases, increases in utility rates are noted. However, without data on utility costs, the impact of rate increases cannot be quantified in dollar terms.

Averages of the following costs could easily be computed from the combination of LADWP and Department of Sanitation and Environment (LASAN) billing data and data in the Assessor's database on the number of units on each property.

- 1) electricity costs for master-metered buildings
- 2) water
- 3) sewer costs
- 4) solid waste collection costs

The Los Angeles Department of Sanitation and Environment should provide average costs for sewer and solid waste collection, both for buildings with four units or less, where waste is collected by LASAN, and buildings with five or more units, where waste is collected by companies under contract to LASAN. Under the franchise agreements, this information must be made available to LASAN.

Data from a relatively small sample (e.g. a few hundred properties) could provide a statistically reliable sample for the purpose of projecting average costs and the impact of rate increases on apartment operating costs.

It is recommended that the City of Los Angeles Department of Water and Power and Department of Sanitation and Environment provide this data for future studies of the Rent Stabilization Ordinance.

Findings

- The RSO provides security of tenure by limiting the rent increases of a tenant after taking possession.
- However, because of vacancy control, the initial rent is not regulated, so the RSO does not preserve the affordability of housing, except for long-term tenants, who constitute a minority of the tenant population. This limitation on rent control is mandated by state law, the Costa Hawkins Act. The City of Los Angeles, along with all rent-control jurisdictions in the state, is required to have vacancy decontrol.

- The impact of the RSO differs among properties based on their frequency of tenant turnovers.
- For decades, questions and criticisms have been raised about the use of the *CPI All-Items Index* to determine annual increases on the basis that this index is based on the increases in the costs of a market basket of goods purchased by an average household, which differ substantially from basket of expenses associated with the operating of an apartment building.
- However, apartment operating costs only constitute about 35 percent of rental income, while the annual general adjustment applies to all of rental income including the other 65 percent which is net operating income.
- In past decades, some jurisdictions have conducted annual operating cost studies of the types of expenses incurred by apartment owners in order to tie allowable annual rent increases to trends in apartment operating costs. The projections in those studies have used weighted indexes based on projections of apartment operating costs. However, most of the weight in the index is allocated to an adjustment of net operating income. Furthermore, projections of increases in major portions of operating costs, maintenance and management, are tied to increases in the *CPI All-Items Index*. The jurisdictions that used this approach have subsequently switched to adopting a CPI based annual increase standard.
- There are a number of CPI indexes that are based on the prices of particular commodities or types of services. The indexes include specific measures of virtually every type of cost and service.
- In the public forum, most discussion and consideration of the Consumer Price Index is centered on *CPI All-Items Index*.
- The *All-Items Less Shelter Index* is the CPI index recommended for use in determining the annual allowable rent increase. Its use will remove the circularity associated with using trends in market rents, which are heavily based on shortage conditions that motivated the adoption of the RSO.
- Annual rent increases should cover increases in apartment operating costs. An annual increase in the range of 35 percent of the percentage in the CPI would cover those cost increases in years in which operating costs increased at the same rate as the CPI, but would not allow for any growth in net operating income.
- In regard to ceilings on allowable rent increases, an alternative to setting a fixed ceiling on allowable annual rent adjustments is to use a descending percentage of CPI increases above a specified amount, (e.g.,

100 percent of the CPI increase up to x percent, 50 percent of the CPI increase above y percent). This type of standard recognizes the differences between different amounts of increase in the CPI.

- A disadvantage of allowing greater rent increases for small properties is that tenants in those properties would experience larger rent increases than the balance of the tenant population, although the rent levels of their units and the rate of increase in their rents may not differ from the average for other units.
- Currently, about 69 percent of all RSO units are properly registered and in the Rent Registry, leaving 31 percent with unknown rent amounts and dates of last tenant move-in. This level of non-compliance is unprecedented among the rent stabilization programs. Although, in fairness, this is a relatively new requirement for RSO landlords, whereas other jurisdictions have had this requirement since inception.
- This requirement to provide information to the Rent Registry is important because lack of full compliance raises the possibility that there are systematic differences between properly registered units, which provided much of the statistical basis for the analysis in this report and policy considerations based on this analysis, and units that are not properly registered.
- In order to inform the public and City Council, on an annual basis the Los Angeles Housing Department should be provided with data from the Los Angeles Department of Water and Power on average utility costs for buildings covered by the RSO. The information should include average water and electricity costs for master-metered buildings.
- The Los Angeles Department of Sanitation and Environment (LASAN) should provide average costs for sewer and solid waste collection, both for buildings with four units or less, where waste is collected by LASAN, and buildings with five or more units, where waste is collected by companies under contract to LASAN.
- The Sanitation and Environment Department should provide data on average costs for solid waste collection, both for RSO buildings with four or less units and buildings with five or more units.
- Under other rent stabilization ordinances that have provided apartment owners with extra rent increases to cover increases in utility costs, the permitted amounts have been 1) based on the average amounts of the rent increases that would be required to cover the actual increases in costs of the utilities rather than being a permanently fixed annual amount and, 2) limited to years in which there were significant increases in these costs.

- The Economic Roundtable recommends that Los Angeles adopt a similar policy, accompanied by a requirement that LADWP provide data on average electricity and water costs for master-metered properties covered by the RSO.



16. Allowable Additional Rent Increases for Apartment Owners Who Pay for Gas and/or Electricity

*Photo credit:
Economic Roundtable*

Overview

The rents of about 20 percent of all RSO units are impacted by the additional rent increase allowance for gas and electricity.⁹⁵ In about seven percent of all units, an additional two percent is permitted based on the provision of both services. In 11 percent of all units, landlords pay for gas, but not electricity. In 1.4 percent of all units, landlords pay for electricity but not gas (*Table 27*).

Table 27: Gas and Electricity Costs Paid by RSO Landlords

Service	Percent of Units
Gas & Electricity	7%
Gas, But Not Electricity	11%
Electricity, But Not Gas	1.4%

Source: Economic Roundtable team analysis; City of Los Angeles Housing Department Rent Registry 2024.⁹⁶

The percentage of landlords who pay for these services is much higher among buildings with 20 or more units (*Table 28*).

Table 28: Percent of Units Landlord Pays Gas and/or Electricity, by Size of RSO Building

Service	2-4 Units	5-9 Units	10-19 Units	20-49 Units	50+ Units	All Units
Gas & Electricity	5%	3%	5%	10%	13%	7%
Gas, But Not Electricity	3%	4%	5%	12%	27%	11%
Electricity, But Not Gas	2%	1%	1%	1%	2%	1%

Source: Economic Roundtable team analysis; City of Los Angeles Housing Department Rent Registry 2024.

Under the RSO, apartment owners who cover either gas or electricity costs are permitted additional annual rent increases of one percent for each of these services.⁹⁷ Typically the cost of electricity service is in the range of \$100 to \$125 per month for apartments. Average monthly gas costs for all types of residences is \$66. For an apartment with a rent of \$1,600 per month, the annual allowable rent increase is increased by \$16 per month for each of these services. In the case of a tenant who remains three years, the additional increase for the provision of one of these services is \$48 and for both it is \$96.

The allowable surcharge was adopted in the RSO in 1980, at a time when gas and electricity costs were surging. From October 1979 to June 1980, the average cost of electricity increased by 44 percent. Since that time, gas and electricity prices have been fluctuating, upwards and downwards, rather than steadily increasing. In some lengthy periods, there have been no increases or even declines in these rates while in other periods there have been substantial increases.

There is no correlation between the actual annual increases or declines in the costs of each of these services and an additional one percent annual rent increase for each of these services. Assuming that monthly electricity costs are in the range of \$100 to

\$125 and monthly gas costs are in the range of \$60, it is clear that increases in monthly rent of \$15 would be disproportionately high relative to the amount necessary to cover the increases in these costs, unless gas and electricity costs were increasing at the rate of 12 to 15 percent per year.

The approach under the RSO of providing a fixed annual adjustment for these services is unique among California rent stabilization ordinances. From time to time, other jurisdictions have allowed additional increases for these services in particular years, with the amounts of the additional allowable increase tied to the actual cost increases.

Average Cost of Master Metered Gas and Electric Services

No systematically collected data on the cost of gas and electric services in master-metered buildings in the City of Los Angeles has been identified. Data on average consumption levels in the state indicates that the average electric expense for apartments is in the range of \$125 per month.⁹⁸

A recent “Rate Alert” notice of the Southern California Gas Company indicates that the average monthly gas bill for residences is \$66.⁹⁹ Undoubtedly, the average for apartments would be lower.

Rate History

The cost of gas and electricity have alternatively remained flat for lengthy periods, decreased during other periods, and sharply increased during other periods. For example, from 1990 to 2000, average costs for electricity increased by only 10 percent. From 2000 to 2010, average costs increased by about 75 percent.

From 2014 through 2023, LADWP electricity rates increased by four percent per year on the average, with a range in annual changes in rates from -5.9 percent to 10.4 percent (*Table 28*).

Table 28: LA Department of Water and Power Electricity Rates

Year	Rate per KWH	Annual Change
2014	0.123398	-
2015	0.127232	3.1%
2016	0.11968	-5.9%
2017	0.132082	10.4%
2018	0.140074	6.1%
2019	0.151218	8.0%
2020	0.152436	0.8%
2021	0.156576	2.7%

Source: Economic Roundtable team analysis; City of Los Angeles Department of Water and Power rate history data.

While data on the specific gas and electric costs of Los Angeles apartment dwellers has not been located, data on the average price that Los Angeles area consumers paid for gas and electricity illustrates the volatility of the costs, rather than a steady progression of increases (*Table 29*).

Table 29. Average Price of Electricity & Natural Gas Utilities, Los Angeles-Riverside-Orange Counties, January 1979-2022

Year	Average Price of Electricity per KWH*	Pct. Change over Prior Year	Average Price of Natural Gas (Piped) per Therm**	Percent Change over Prior Year
1979	\$0.05		\$0.25	
1980	\$0.06	13%	\$0.32	27%
1981	\$0.07	24%	\$0.37	16%
1982	\$0.09	19%	\$0.41	12%
1983	\$0.08	-10%	\$0.52	26%
1984	\$0.08	3%	\$0.53	3%
1985	\$0.09	6%	\$0.57	8%
1986	\$0.09	1%	\$0.52	-9%
1987	\$0.08	-2%	\$0.50	-4%
1988	\$0.09	7%	\$0.54	7%
1989	\$0.10	13%	\$0.54	0%
1990	\$0.11	3%	\$0.54	0%
1991	\$0.12	12%	\$0.66	22%
1992	\$0.12	0%	\$0.62	-6%
1993	\$0.12	2%	\$0.67	9%
1994	\$0.12	0%	\$0.68	1%
1995	\$0.13	6%	\$0.72	7%
1996	\$0.13	-1%	\$0.65	-10%
1997	\$0.13	0%	\$0.66	0%
1998	\$0.13	1%	\$0.73	12%
1999	\$0.12	-9%	\$0.65	-12%
2000	\$0.12	0%	\$0.68	5%
2001	\$0.12	7%	\$1.04	54%
2002	\$0.18	44%	\$0.73	-30%
2003	\$0.18	1%	\$0.91	24%
2004	\$0.14	-24%	\$1.04	15%
2005	\$0.14	2%	\$1.10	6%
2006	\$0.16	18%	\$1.47	33%
2007	\$0.20	20%	\$1.07	-27%
2008	\$0.19	-6%	\$1.22	14%
2009	\$0.18	-3%	\$1.09	-10%
2010	\$0.19	4%	\$1.18	8%
2011	\$0.21	10%	\$1.02	-13%
2012	\$0.20	-1%	\$1.00	-3%
2013	\$0.23	14%	\$1.01	2%
2014	\$0.22	-7%	\$1.20	18%
2015	\$0.22	0%	\$1.17	-2%
2016	\$0.21	-1%	\$1.16	-1%
2017	\$0.18	-14%	\$1.22	5%
2018	\$0.18	-2%	\$1.10	-9%
2019	\$0.18	1%	\$1.34	21%
2020	\$0.19	5%	\$1.33	-1%
2021	\$0.21	7%	\$1.41	6%
2022	\$0.25	20%	\$1.88	33%
Annual Rate of Increase 1979-2022		3.8%	-	4.8%

Source: U.S. Bureau of Labor Statistics. 2024. Average Energy Prices, Los Angeles-Long Beach-Anaheim – February 2024. https://www.bls.gov/regions/west/news-release/averageenergyprices_losangeles.htm. Note: Years 1% or less or negative are bolded.

Market Dynamics

In order to place these increases in perspective, a few dynamics are noted. The additional rent increases are only cumulative for the term of tenancy, because allowable base rents are reset by the owner when a unit becomes vacant. In an apartment with the same tenant for five years, the cumulative additional rent increase for each service would likely total \$75 to \$100 over a five-year period, depending on the initial rent level, which is largely dependent on the date tenancy was commenced.

In the unusual cases of a long-term tenancy - e.g., 10 years - the additional rent increase could be in the range of \$150 to \$240 for each service provided. This amount exceeds the total cost of the service, as well as the increase in the cost since the tenant moved in.

In regard to the surcharge, the potential interplay between these increases and the operation of the rental market should be set forth. To the extent that these costs are taken into account by landlords when setting rents and by tenants in selecting units to rent, the market would take into consideration the coverage of these costs by a landlord and the extra rent increases that are allowed in return. However, these considerations may not have a real role among the numerous considerations by tenants in choosing a rental unit and the constraints in a tight rental market.

Allowances for Landlord Coverage of Gas and Electricity Under Other Rent Control Ordinances

Other jurisdictions with rent ordinances have provided apartment owners with varying types of allowances for these expenses. However, the manner in which the allowable increases were determined has differed substantially from the fixed percentage approach in the RSO and the amounts authorized were very different. In general, in other jurisdictions calculations were made of the actual amounts of the rent increases that would be required to cover the actual increases in costs of providing electricity and/or gas (*Table 30*).

Santa Monica, where allowances for master-metered buildings have been based on studies of the actual increases in these costs, the cumulative total of these adjustments since 1985 has only totaled about three to four percent of the rent for each service. Berkeley and Santa Monica have authorized uniform across-the-board rent increases to cover the provision of master-metered electricity and/or gas in particular years based on an analysis of the cost increases in those particular years (*Table 30*).

Under the San Francisco ordinance, owners may implement a pass-through that is based on the actual increases in gas and electricity costs for their individual property. Before giving tenants a notice of such an increase, the

apartment owner must provide the Rent Board with a utility cost worksheet.

Table 30: Rent Adjustments for Buildings with Master-Metered Gas and/or Electricity under California Rent Stabilization Ordinances

Jurisdiction	Type of Utility Allowance	Amount of Utility Allowance
Los Angeles	Automatic annual increase	1%/year for gas, 1%/year for electricity
Berkeley	Until 2006 authorized in particular years based on annual apartment operating cost study	1981 - 1.2% if owner pays space heating, 1982-\$4 to \$16 if owner pays gas & elec., depending on size of unit, 1983 - 0.25% if owner pays gas or elec. 1989 - 0.5% if owner pays gas or elec., 2001 - \$8 if owner pays gas 2002 - \$9 if owner pays for heating
Beverly Hills	None	
Hayward	Individualized building passthrough of cost increases up to 1%, if increase above 1% Documentation must be provided to the tenant and tenant can challenge the increase	Individualized by building
Oakland	None	
San Francisco	Individualized building pass-thru of cost increases - allowable increase = increase in cost over base year (base year for new tenants, the year before the tenant moved-in - advance administrative approval required	Individualized by building
San Jose	None	
Santa Monica	-only for units in which landlord pays all gas or pays all gas and electrical service, - only units with same tenant since Jan. 1, 1999 (units with no vacancy decontrol increases) - application and admin. authorization required, - initial submission of 1 yr. utility bills required	1985 - gas - 1%, electricity - 0.5% 1986 – electricity - 2% 1991 – electricity-\$7.00, gas & electricity -\$11 2001- electricity - \$10 2002- 2001 rent adjust. repealed 2006 -gas or gas & electricity -\$7

Source: Economic Roundtable team analysis.

Policy Alternatives

Reconsideration of the master-metered gas and electricity allowance is recommended. Possible policies include:

1. No additional increases for units with master-metered gas and electricity.
2. The authorization of fixed dollar or percentage additional rent increases for master-metered units that reflect the actual average amounts of the cost increase, when significant gas and/or electricity cost increases occur, rather than a fixed annual percentage allowance.

Statistically reliable data about electricity expenses could easily be obtained for a sample of properties through the records of the Los Angeles Department of Water and Power (LADWP). That Department does not have records of the number of units in each building, however that data is available from the Rent Registry of the Housing Department. In both

databases, the information is tied to parcel numbers so it can easily be integrated.

The City can make reasonable estimates of what percentage passthroughs will be reasonable in the future by measuring the impacts of cost increases on buildings with average consumption levels. Currently, while rate increases are known because they are publicly set, the complementary information on average consumption levels and on the ratio of these expenses to gross income is very limited.

In order to analyze the data, some staff effort would be required. However, data from only a sample of the units would be more than adequate to provide a very reliable calculation of the average. To place this cost of analyzing the data in perspective, the surcharges now add roughly \$12 million to the annually allowable rent increases under the RSO.¹⁰⁰

Reliable projections of average electric bills can be made through the combination of data in the LAHD and LADWP databases. Furthermore, Southern California Gas Company may be willing to provide statistical data about average gas costs for master-metered apartment buildings.

Using this data, the Economic Roundtable recommends that the increases in utility costs that are passed through to renters should not exceed the average actual amount of increases in those costs.

Findings

- Under the RSO, apartment owners who cover either gas or electricity costs are permitted additional annual rent increases of one percent for each of these services. This impacts the rents of about 20 percent of all RSO units. In about eight percent of all units, an additional two percent is permitted based on the provision of both services. In 11 percent of all units, landlords pay for gas, but not electricity. In 1.4 percent of all units, landlords pay for electricity but not gas.
- The approach under the RSO of providing a fixed annual adjustment for these services is unique among California rent stabilization ordinances
- In the cases of a tenancy of five years, the additional rent increase could be in the range of \$150 to \$240 for each service provided. This amount exceeds the total cost of the utility service.
- In other jurisdictions that provide apartment owners with extra rent increases to cover increases in utility costs, the permitted amounts have been based on the average amounts of the rent increases that would be required to cover the actual increases in costs of

providing electricity and/or gas, rather than being a permanently fixed annual amount.

- Los Angeles' allowance of a one percent annual increase - \$15 per unit per month – for each of these costs is disproportionate to actual increases in the costs of master-metered electricity and gas, each of which typically have an overall cost of \$100 per unit per month or less. The Economic Roundtable recommends that the increases in utility costs that are passed through to renters should not exceed the average actual amount of increases in those costs.



17. Accessory Dwelling Units

Image credit: Paul Davis Architects

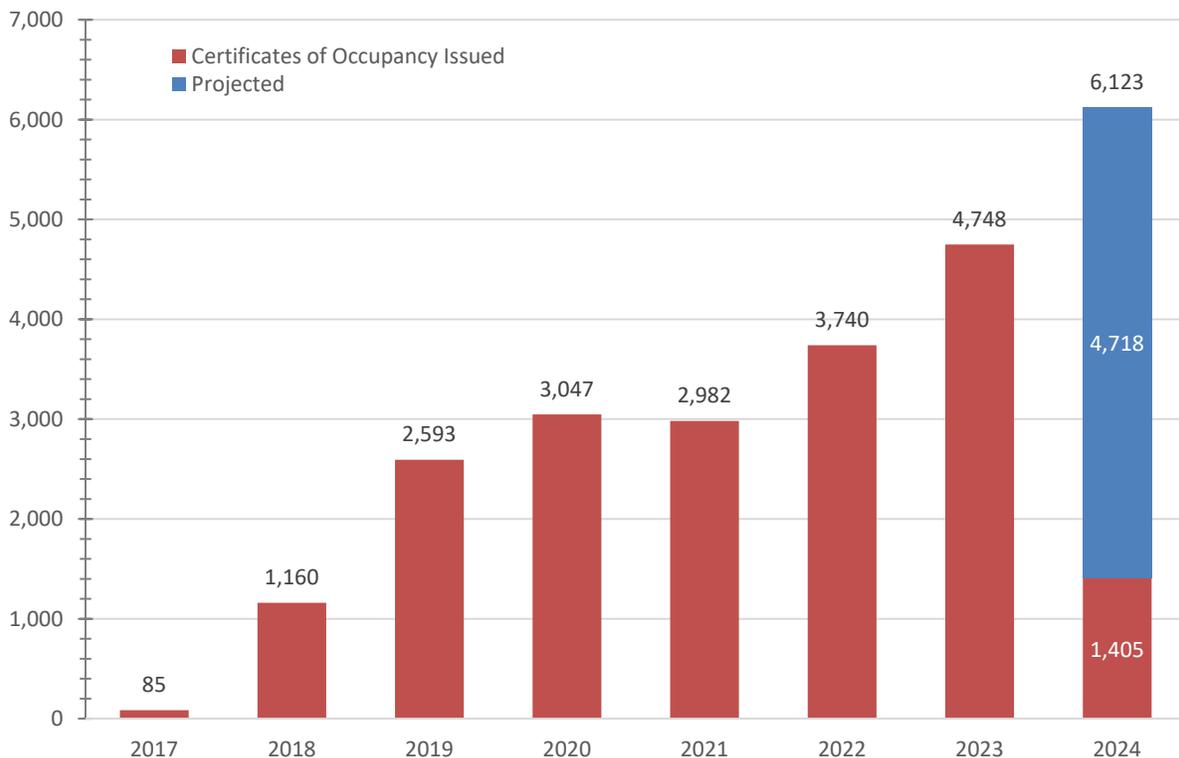
Accessory Dwelling Units in the City of Los Angeles

Accessory dwelling units (ADUs) represent an opportunity to expand the City’s inventory of rental housing with comparatively modest capital investments.

Since the City of Los Angeles’ implementation of its ADU ordinance,¹⁰¹ spurred by California’s ADU code change,¹⁰² there has been a steady increase in permit applications, permits issued, and certificates of occupancy issued for these housing additions. This chapter addresses permitted, “legal” ADUs in the City, planned and constructed since 2017. The number of “illegal” ADUs remains difficult to count.¹⁰³ Information in this section draws on data from Los Angeles Department of Building and Safety records of Building Permits, Certificates of Occupancy, and input from the City’s Housing and Planning departments.

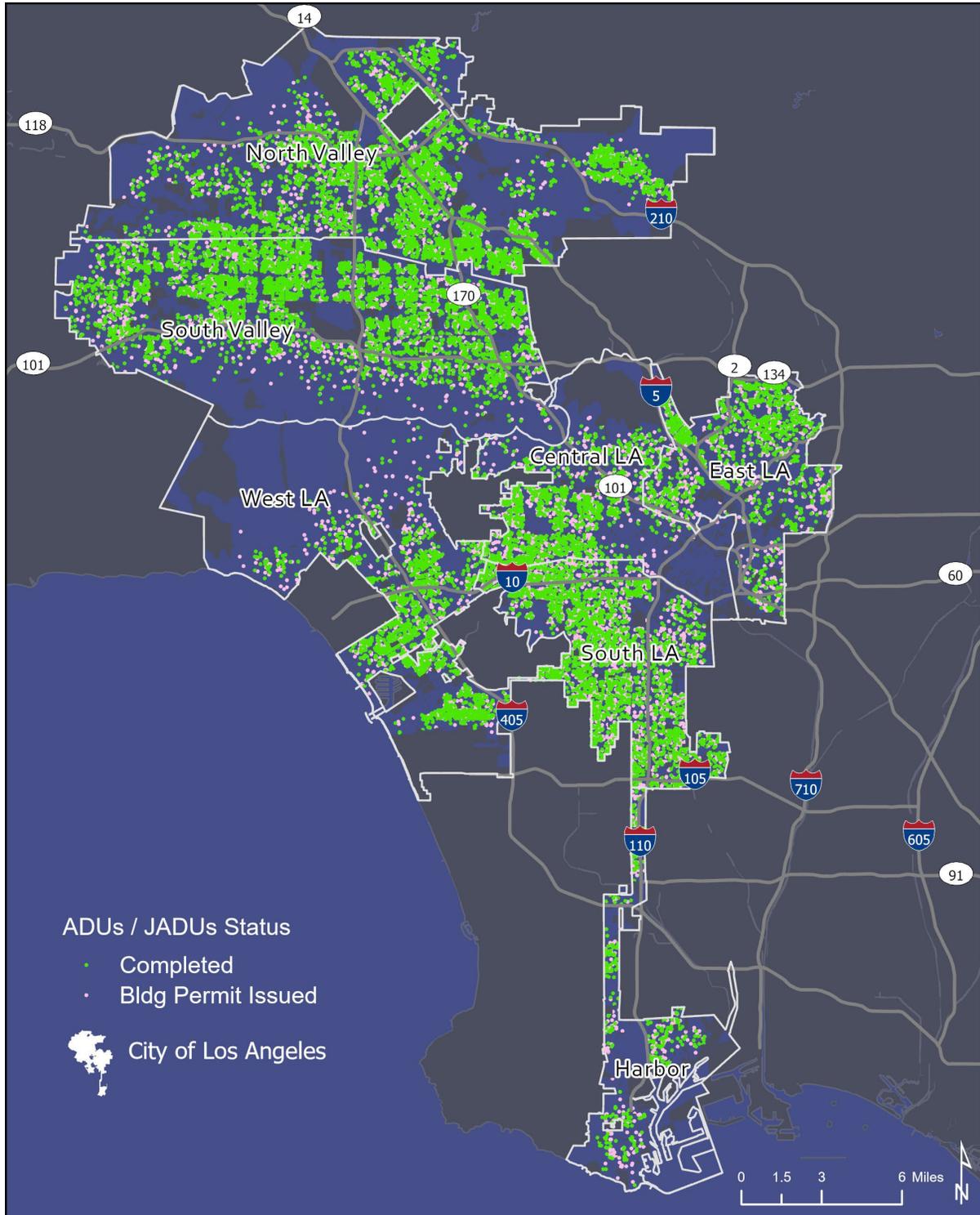
Annual numbers of “legal” ADU’s have grown almost every year, and add up to 19,760 total ADU’s produced in the City (Figure 58). This includes 1,405 produced so far in 2024 and, based on the trend since 2017, we project 6,123 by the end of this year.¹⁰⁴ ADUs are constructed in almost every neighborhood, added to “Single Family”-zoned as well as multi-family properties to help boost the city’s overall housing supply (Figure 58).

Figure 58: New ADUs Completed by Year, City of Los Angeles



Source: Economic Roundtable analysis, City of Los Angeles, Department of Building and Safety. 2024. Building Permits for Accessory Dwelling Units (ADUs and Junior ADUs) April 18, 2024.

Figure 59: Location of completed ADUs, and Permits Issues for Additional ADUs



Source: Economic Roundtable analysis, City of Los Angeles, Department of Building and Safety. 2024. Building Permits for Accessory Dwelling Units (ADUs and Junior ADUs) April 18, 2024.

City building permit data show over 11,800 building permits issued for more ADUs, although not all of the permitted units may get built and certified for occupancy, and some will take several years to complete. As

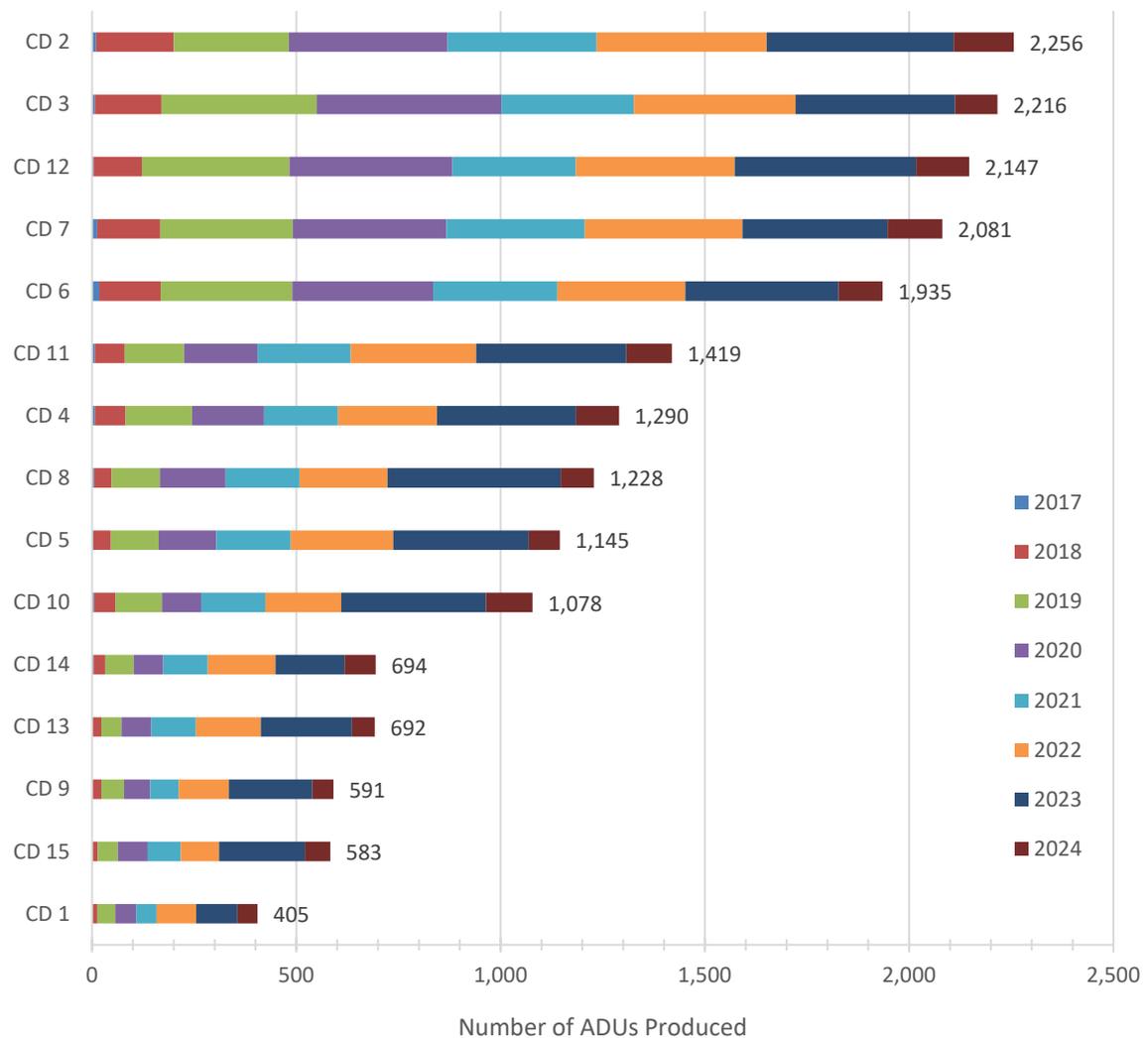
Figure 59 illustrates, some future ADUs will appear on blocks without previously approved ones.

Counted by council district and year certified for occupancy (Figure 60), over half – 54 percent – of permitted and completed ADUs are in the San Fernando Valley (districts 2, 3, 6, 7 and 12).

Council district 2 (North Hollywood, Studio City, Van Nuys), district 12 (Chatsworth, Northridge, West Hills), and district 8 (South Los Angeles) saw the largest number of ADUs completed and certified in 2023 – over 400 each.

Council district 1 (Pico Union, MacArthur Park, Chinatown, and Northeast Los Angeles), district 15 (San Pedro, Wilmington, Harbor City), and district 9 (Vermont Square, South Park, South Los Angeles) have seen the fewest produced overall, albeit with rising amounts per year.

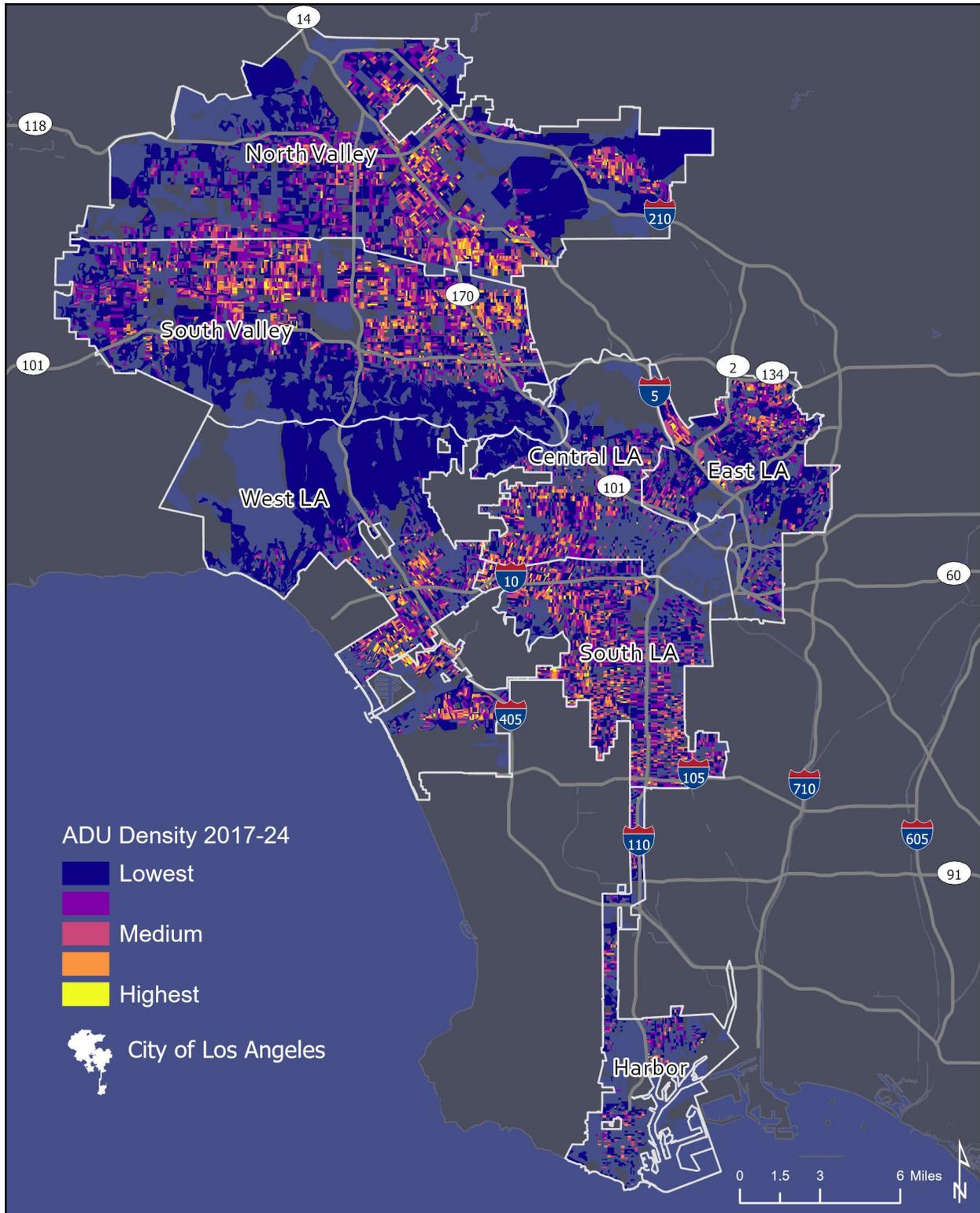
Figure 60: City of Los Angeles ADUs, by Council District and Year Certified for Occupancy



Source: Economic Roundtable analysis, City of Los Angeles, Department of Building and Safety. 2024. Building Permits for Accessory Dwelling Units (ADUs and Junior ADUs) April 18, 2024.

Neighborhoods with the highest density of ADUs are found away from hillside neighborhoods (Figure 61). These include:

Figure 61: Neighborhoods with the Highest Density of ADUs, City of Los Angeles



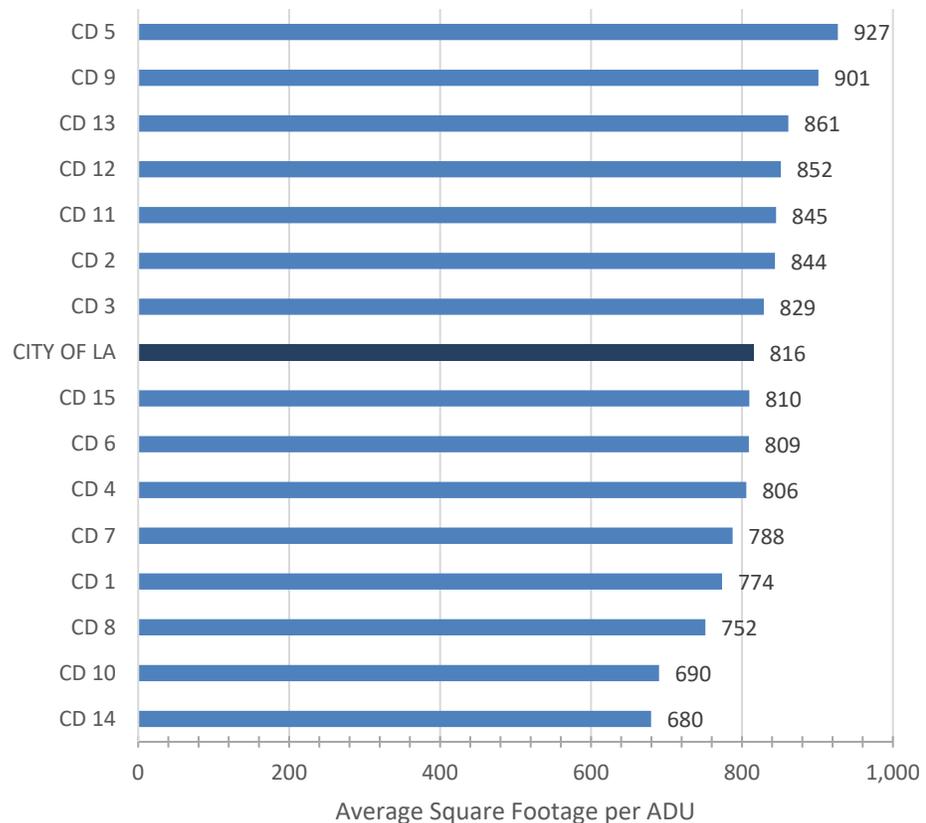
Source: Economic Roundtable analysis, **City of Los Angeles**, Department of Building and Safety. 2024. Building Permits for Accessory Dwelling Units (ADUs and Junior ADUs) April 18, 2024.

- North Hollywood, Van Nuys, Panorama City, Reseda, Canoga Park, Sunland and Arleta in the San Fernando Valley.
- Central and South Los Angeles have high densities of ADUs throughout, aside from Koreatown, Westlake, Chinatown and Downtown.
- West Los Angeles neighborhoods of Sawtelle, Westchester and Palms.
- Northeast Los Angeles neighborhoods of Eagle Rock and Atwater Village.

The average size of ADUs citywide is 816 square feet each (Figure 62). The city council districts with the largest average ADU sizes include district 5 (Cheviot Hills, Encino, Fairfax, Palms, Pico–Robertson) and district 9 (Vermont Square, South Park, South Los Angeles), both over 900 square feet.

Council districts with the lowest average ADU square footage are district 10 (Koreatown, Mid-City, West Adams and Wilshire Center) and district 14 (Downtown, Boyle Heights, Eagle Rock) – roughly 200 square feet smaller on average than the districts at the top of the range.

Figure 62: Average Square Footage of ADUs by Council District, 2017–present



Source: Economic Roundtable analysis, City of Los Angeles, Department of Building and Safety. 2024. Building Permits for Accessory Dwelling Units (ADUs and Junior ADUs) April 18, 2024.

The average valuation of ADU citywide is just over \$61,000 each, or \$92 per square foot (Figures 63 and 64). Council district 9 (South LA) has the highest valuation per ADU produced, followed by district 11 (Brentwood, West LA and Westchester). Council district 4 (Hancock Park, Hollywood, Miracle Mile, Sherman Oaks, Silverlake) and district 11 have the highest

Figure 63: Average Valuation of ADUs, by Council District

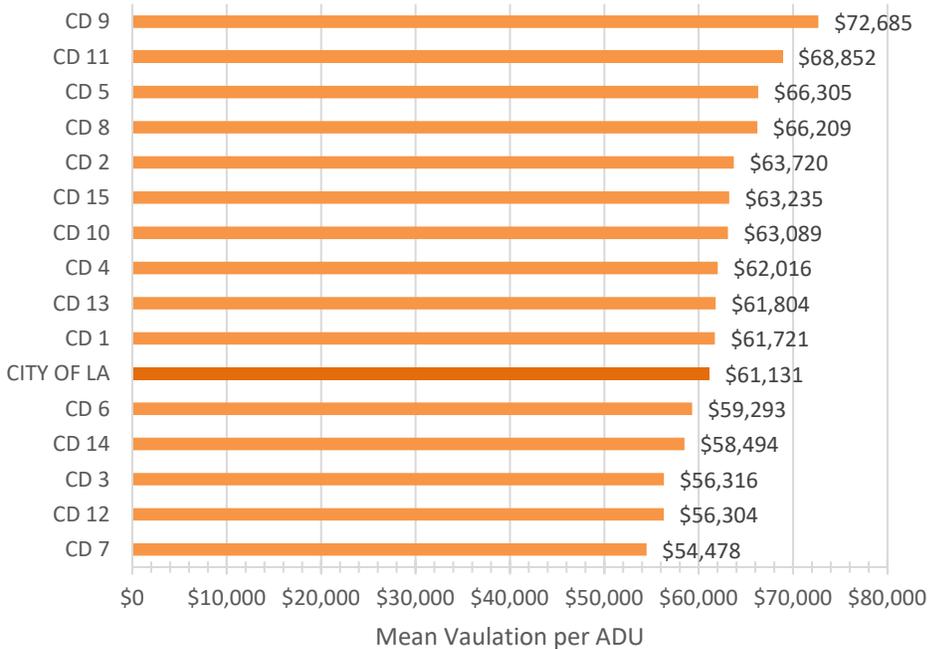
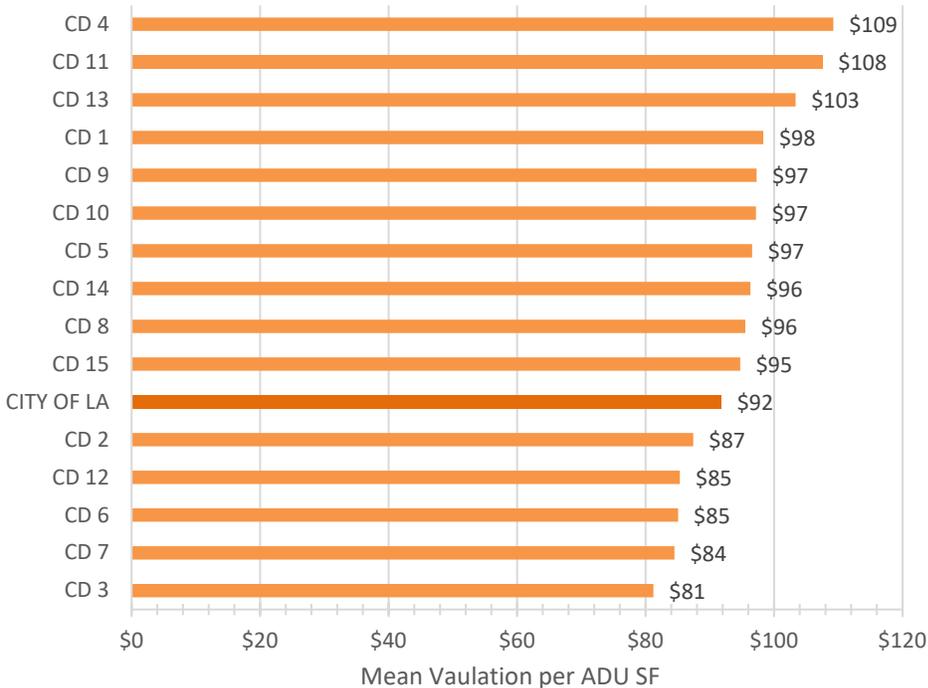


Figure 64: Average Valuation of ADUs per Square Foot, by Council District



Source: Economic Roundtable analysis, City of Los Angeles, Department of Building and Safety. 2024. Building Permits for Accessory Dwelling Units (ADUs and Junior ADUs) April 18, 2024.

ADU valuations per square foot. Council district 3 (Southwest San Fernando Valley), district 7 (Northeast San Fernando Valley) and district 6 (Central San Fernando Valley) are among the lowest in terms of ADU valuation per unit and per square foot.

While legal ADUs add much-needed housing for Los Angeles residents, they contribute only a tiny percentage to the City's housing stock each year, a total of 1.6 percent of the rental housing stock so far. In light of the urgent need for more housing production, especially affordable housing, we recommend that the City Planning Department complete its studies of potential modifications in the building and zoning codes that might encourage construction of more ADUs.

We recommend that the City consider economic incentives to stimulate more ADU production. Fees could be waived or the ADUs could be exempted from parking requirements when homeowners rent ADUs at below-market rates to low-income tenants. Additionally, the permitting process could be streamlined to reduce the time, uncertainty, and expense that deters homeowners from applying for approval.

Findings

- ADUs represent an opportunity to expand the City's inventory of affordable housing with modest capital investments.
- The number of "legal" ADUs has grown since 2017, with a total of 19,760 in the city.
- We project that 6,123 ADUs will be produced in 2024, the City's highest single-year total yet.
- Over 11,800 building permits have been issued for unbuilt ADUs.
- The average ADU in the City of Los Angeles is 816 square feet.
- The average valuation is \$61,000 each, or \$92 per square foot.
- Legal ADUs provide 2.1 percent of the City's rental housing stock. ADUs alone cannot fix the City's affordable housing –shortage.
- We recommend that the Planning Department complete its studies of potential modifications in the building and zoning codes that would encourage construction of more ADUs.
- We recommend that the City consider providing economic incentives that will stimulate more ADU production.



18. Data Appendices

Photo credit: Economic Roundtable

Appendix 1: RSO Housing Inventory

RSO Units by Building Size and Planning District

This appendix augments *Chapter 2* of this report, *Los Angeles Housing Inventory*. The Harbor has the fewest, RSO properties, while the North San Fernando Valley has the next fewest, just under 7,500 and 12,000, respectively (*Table 31*).

Central Los Angeles has the largest number of RSO properties with 50 or more units (425) and 20–19 units (1,707), with the South San Fernando Valley having the next greatest number of larger RSO properties.

Table 31: Count of RSO Properties by Total Number of Units in Building by Planning District

	1 Unit	2 Unit	3-4 Units	5-9 Units	10-19 Units	20-49 Units	50+ Units	Total
West LA	14,347	2,914	2,080	2,487	1,132	458	83	23,501
Central LA	5,985	6,455	4,759	4,456	2,425	1,707	425	26,212
North Valley	7,515	2,717	543	433	248	373	152	11,981
South Valley	17,084	2,731	1,903	2,221	1,068	963	230	26,200
South LA	3,226	16,085	10,363	3,799	1,320	451	45	35,289
Harbor	1,636	2,521	2,234	724	274	78	23	7,490
East LA	1,139	9,694	5,315	1,963	552	186	31	18,880
Total	50,932	43,117	27,197	16,083	7,019	4,216	989	149,553

Table 32: Count of RSO Units by Total Number of Units in Building by Planning District

	1 Unit	2 Unit	3-4 Units	5-9 Units	10-19 Units	20-49 Units	50+ Units	Total
West LA	14,347	5,828	7,360	17,733	14,859	12,568	8,534	81,229
Central LA	5,979	12,910	17,315	30,543	31,626	50,562	40,129	189,064
North Valley	7,513	5,434	1,946	2,839	3,338	11,486	16,064	48,620
South Valley	17,083	5,462	6,717	14,456	14,116	28,870	22,125	108,829
South LA	3,223	32,170	36,195	24,910	16,923	11,596	4,249	129,266
Harbor	1,634	5,042	7,818	4,736	3,561	2,172	2,446	27,409
East LA	1,135	19,388	18,003	12,328	7,102	5,110	3,349	66,415
Total	50,914	86,234	95,354	107,545	91,525	122,364	96,896	650,832

Source: Economic Roundtable analysis; Los Angeles Housing Department. 2024. Dataset A: RSO Inventory; Report Dashboard for RSO – LAHD. Link: <https://housing2.lacity.org/rso> Note: Includes exempt and vacant RSO units. One-unit RSO properties are located in buildings with two or more overall units built before October 1, 1978, ranging from ADUs added to older single-family properties, to older condominium buildings with at least one unit for rent.

Central Los Angeles, South Los Angeles and the South San Fernando Valley have the greatest number of RSO properties, while the Harbor and North San Fernando Valley have the fewest. Likewise, Central Los Angeles and the South San Fernando Valley have the greatest number of RSO properties with 50 or more units (*Table 32*).

Despite South Los Angeles having the second greatest number of RSO units, more of those are found in smaller RSO buildings, with less than 5,000 units in the largest category of RSO properties.

Age of RSO Inventory: Properties and Units

The age of RSO properties and units varies across the City, echoing the overall residential development history of Los Angeles.

Interestingly, three-quarters of RSO *properties* in East Los Angeles, well over two thirds of those in South LA (70 percent), and well over half (56 percent) Central Los Angeles were constructed before the 1940s (*Table 33*).

Much higher shares of RSO properties in West Los Angeles (67 percent) and the San Fernando Valley (61 percent) were constructed since 1960.

Table 33: Count of RSO Properties by Decade Built, Planning District

	West LA	Central LA	North SF Valley	South SF Valley	South LA	Harbor	East LA	Total
1939 or Earlier	2,064	14,368	723	1,231	23,942	2,585	13,655	58,568
1940 to 1949	1,968	1,419	1,623	2,973	4,456	796	1,203	14,438
1950 to 1959	3,379	2,928	3,006	4,787	2,849	1,276	1,582	19,807
1960 to 1969	7,139	3,588	1,864	5,553	2,434	1,197	1,658	23,433
1970 to 1979	8,509	2,920	4,699	11,159	122	1,531	324	29,264
1980 to 1989	15	9	6	6	23	14	35	108
1990 to 1999	7	16	6	12	34	8	27	110
2000 to 2009	29	53	4	25	134	17	34	296
2010 to 2019	188	362	24	234	162	4	40	1,014
2020 or Later	26	21	7	50	45	1	14	164
Total	23,324	25,684	11,962	26,030	34,201	7,429	18,572	147,202

Source: Economic Roundtable analysis; Los Angeles Housing Department. 2024. Dataset A: RSO Inventory; Los Angeles County Assessor. 2023. SBF Abstract (DS04). Note: Includes exempt and vacant RSO units.

The age of RSO units by planning district also varies across the City. Sixty-five percent of RSO units in East Los Angeles, 58 percent in South Los Angeles, and 48 in Central were built before 1940 (*Table 34*). West Los Angeles (67 percent) and the San Fernando Valley (61 percent) have much higher shares of their RSO properties constructed since 1960.

Table 34: Count of RSO Units by Decade Built, Planning District

	West LA	Central LA	North SF Valley	South SF Valley	South LA	Harbor	East LA	Total
1939 or Earlier	6,494	88,638	1,528	3,111	71,624	8,910	42,482	222,787
1940 to 1949	5,863	11,593	3,356	8,349	13,506	2,448	3,680	48,795
1950 to 1959	19,104	30,791	8,574	22,499	18,829	4,816	6,106	110,719
1960 to 1969	28,399	32,598	19,153	41,201	16,054	6,198	10,581	154,184
1970 to 1979	18,605	16,258	15,415	30,357	1,830	4,249	1,923	88,637
1980 to 1989	35	34	12	55	76	94	83	389
1990 to 1999	28	149	17	59	95	15	57	420
2000 to 2009	38	411	31	87	393	35	73	1,068
2010 to 2019	1,654	3,073	104	1,725	545	7	254	7,362
2020 or Later	94	675	121	336	271	1	36	1,534
Total	80,314	184,220	48,311	107,779	123,223	26,773	65,275	635,895

Source: Economic Roundtable analysis; Los Angeles Housing Department. 2024. Dataset A: RSO Inventory; Los Angeles County Assessor. 2023. SBF Abstract (DS04). Note: Includes exempt and vacant RSO units.

Appendix 2: RSO Rent Registry

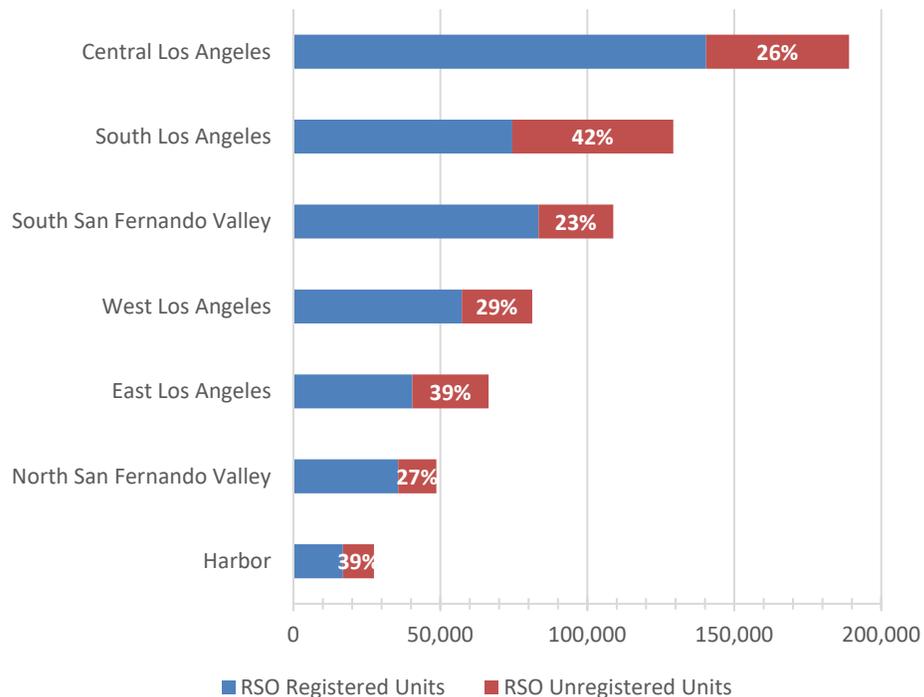
About the RSO Rent Registry

RSO property owners must register their apartment buildings annually with the City of Los Angeles Housing Department (LAHD). Since 2017, submitting information about current rents to a “Rent Registry” is an additional part of the registration process, which can be completed in two steps. A landlord must both pay the registration fees and submit the Rent Registry information for properties subject to the RSO. RSO registration is due before the end of February each year, and landlords usually pay this on time because they will incur late fees if they do not.¹⁰⁵

RSO landlords can submit information about their units to the Rent Registry at any time of the year, however, since there is no penalty for submitting past February other than not receiving an RSO certificate, which is generated once a landlord pays the registration *and* submits the Rent Registry. A registration certificate allows a landlord to accept and demand rent. The landlord can submit information to the Rent Registry online, by mail, or by dropping it off in person at an LAHD field office.

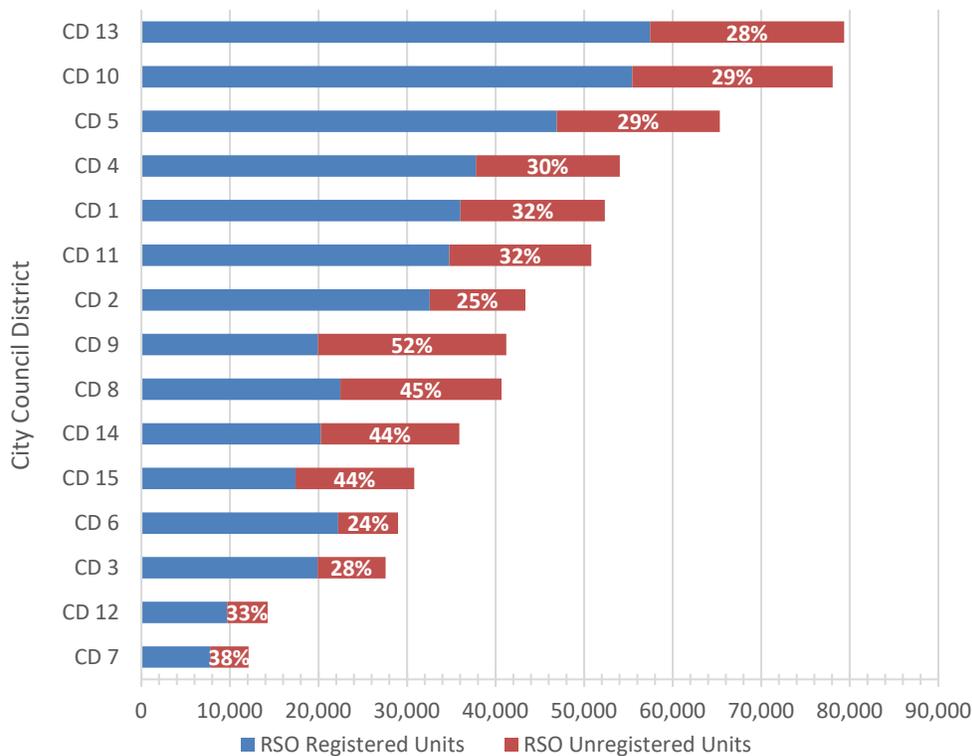
Figure 65 shows the number and share of RSO units in each planning district that did not submit information to the Rent Registry, forgoing their RSO registration certificate in the process. The highest rates of

Figure 65: RSO Units by Rent Registry Status and Planning Region



Source: Economic Roundtable team analysis; Los Angeles Housing Department. Rent Registry 2024; Los Angeles Housing Department. Dataset A: RSO Inventory.

Figure 66: RSO Units by Rent Registry Status and City Council District

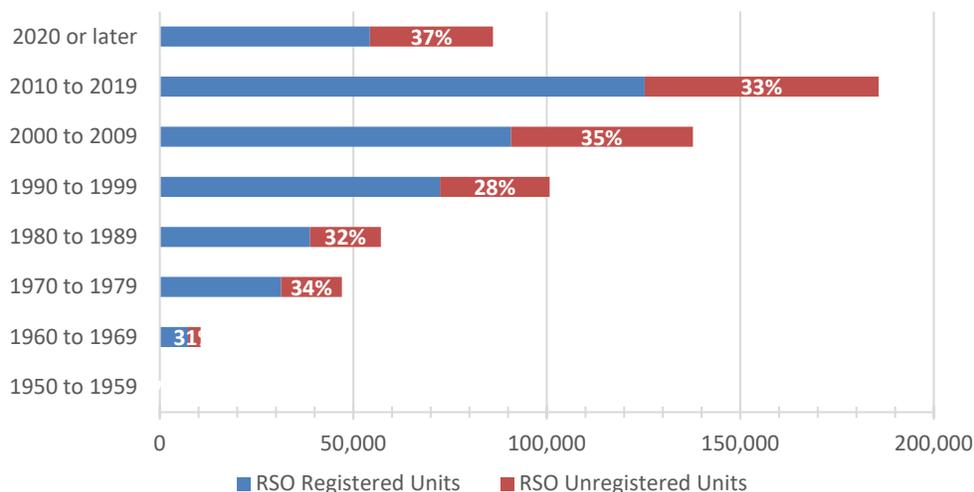


Source: Economic Roundtable team analysis; Los Angeles Housing Department. Rent Registry 2024; Dataset A: RSO Inventory.

underreporting information about units to the Rent Registry occurred in South Los Angeles (42 percent) and the Harbor (39 percent).

Figure 66 shows the number and share of RSO units in each city council district. Roughly equal percentages of units report to the Rent Registry by last year sold by decade, but the clear numeric majority of units that are not

Figure 67: RSO Units by Rent Registry Status and Year Sold



Source: Economic Roundtable team analysis; Los Angeles Housing Department. Rent Registry 2024; Dataset A: RSO Inventory.

in the LAHD rent registry were purchased in the last twenty years, since 2000 (*Figure 67*). These add up to roughly 140,000 RSO units.

In 2023, LAHD began to send notices to tenants informing them of their RSO rights and prerogative to dispute the rent amount reported by their landlord. (The Rent Registry online portal and software does not review for inaccuracies; it can only ensure that all the required fields are complete.) So far, LAHD staff use the Rent Registry data most often when a tenant complains regarding illegal eviction or rent increases, in order to see what rent amounts the landlord reported. Some LAHD internal analysis of Rent Registry data has been carried by their Policy Section staff. This Economic Roundtable team study is the first external analysis of the Rent Registry data.

Rent Registry Compliance Rate Caveat

The lower compliance rates with submitting data to the RSO Rent Registry is explained in part by its history. The City of Los Angeles Housing Department is one of just a few – along with the City of Beverly Hills – in which started its Rent Registry *retroactively*; most rent stabilization programs in California were started more recently and with their own rent registries in place from the outset. Further, when the Los Angeles City Council approved creating the RSO Rent Registry, the Housing department was urged to roll out its start-up quickly. As a result, 2017 was a soft rollout first year for the RSO Rent Registry, and Housing Department staff worked to boost participation rates in subsequent years. After the COVID-19 Pandemic outbreak in Spring 2020, many RSO properties owners were coping with unpaid rent, which also affected participation in the RSO Rent Registry.

Rent Registry Data Cleaning

The Economic Roundtable received copies of the Rent Registry database for analysis in this study from the City of Los Angeles Housing Department, covering service years 2017 through 2023. Reported annually to the City by property owners or their managers, these data allow for tremendous insights into the amount of rent paid for RSO units, with information about when tenants move into their RSO units (and by extension, the date of last vacancy decontrol), date of last effective rental increase, whether the unit was temporarily vacant or occupied by an employee, whether utilities and/or parking are included in monthly rent, and the number of bedrooms.

The Economic Roundtable team undertook some cleaning of the data in order to identify units for which rent registry records exist for multiple years, since not all RSO units are in the Rent Registry. To do this, the

study team joined all years of data, restructured the records to compare rent values for each year, and omit records for units where there were missing records. The study team then identified outlier rent values in under or above certain thresholds, which are attributable mostly to data entry typos or exorbitantly high rents.¹⁰⁶

Appendix *Table 35* shows the filters set to identify and remove outliers in the Rent Registry data. For different years, Rent Registry records are excluded for units with rents below \$300 to \$400 per month, and above \$3,500 to \$5,000 per month. This pair of filters removed less than one percent of Rent Registry records from analysis, maintaining a very robust longitudinal rent database to support the Economic Roundtable team’s analysis of RSO rent levels, with breakouts by variables including building size, year sold, and planning district.

Table 35: RSO Rent Registry Records by Properties by Decade Built, Planning District

Service Year	Low Rent Outliers	Included Records	High Rent Outliers	Low-End Filter	High-End Filter	Percent Omitted	Percent Included
2017	2,041	509,276	2,802	\$332	\$3,500	0.9%	99.1%
2018	1,798	509,838	2,483	\$300	\$4,350	0.8%	99.2%
2019	2,041	509,315	2,763	\$350	\$4,230	0.9%	99.1%
2020	1,895	509,607	2,617	\$350	\$4,337	0.9%	99.1%
2021	1,384	511,595	1,140	\$338	\$5,200	0.5%	99.5%
2022	1,346	510,860	1,913	\$350	\$4,950	0.6%	99.4%
2023	1,735	510,085	2,299	\$400	\$5,000	0.8%	99.2%
All Years	12,240	3,570,576	16,017			0.8%	99.2%

Source: Economic Roundtable team analysis; Los Angeles Housing Department. Rent Registry 2024; Dataset A: RSO Inventory.