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OAKLAND

2018 AUG 31 AM 8:49

AGENDA REPORT

TO: Sabrina B. Landreth
City Administrator

FROM: Michele Byrd
Director, HCDD

SUBJECT: Options for Substantial Rehabilitation
Exemption

DATE: August 14, 2018

City Administrator Approval

Date:

8/30/18

RECOMMENDATION

Staff Recommends That The City Council Receive A Report And Direct The City Administrator To Prepare The Necessary Legislation To Amend Chapter 8.22, Article I (Residential Rent Adjustment Program) Of The Oakland Municipal Code To Address The Future Of The Substantial Rehabilitation Exemption.

EXECUTIVE SUMMARY

The moratorium on the substantial rehabilitation exemption provided within the Rent Adjustment Ordinance terminates on October 21, 2018. Staff is requesting that the City Council consider three options for addressing the future of this exemption, as follows:

1. Extend the moratorium for three years to facilitate a study of the impact of the exemption on Oakland's housing inventory and tenant displacement and how it advances City policy objectives;
2. Amend the exemption to limit its application to units that are vacant and essentially uninhabitable and restrict its use in additional ways to protect against tenant displacement; or
3. Eliminate the substantial rehabilitation exemption.

These options were discussed and voted on by the Oakland Residential Rent Board (Rent Board) on July 26, 2018 as described further in the Background/Legislative History section below. This report provides a brief analysis, as well as pro's and con's, for each option.

Should the City Council select either options 1) or 2) listed above, an extension of the existing moratorium would be needed to provide staff time to implement the selected option. A 90-day extension is being recommended in these two cases. Depending on the direction by the City Council, staff will return with the necessary legislation to implement said changes.

Item: _____
CED Committee
September 11, 2018

BACKGROUND / LEGISLATIVE HISTORY

Current Substantial Rehabilitation Exemption

The purpose of the current substantial rehabilitation exemption is to encourage private investment in deteriorated residential units in Oakland. Before an exemption is granted the current regulations require an owner:

- Spend a minimum of 50 percent of the average basic cost for new construction -- determined by using a table issued by the chief building inspector applicable for the time when the project was completed.
- Perform substantial work in each of the units in the building;
- Submit a Certificate of Occupancy (CO), or provide the last finalized permit if a CO is not available;
- If issued CO's on or before the adoption of the ordinance effective September 20, 2016, must have applied for an exemption not later than June 30, 2017, or such exemption would have been deemed to be vacated. (***Attachment A***)

Overview of the Substantial Rehabilitation Exemptions Granted in Oakland

Since 2011, there have been 267 Rent Adjustment exemptions granted. Of the exemptions granted, 35 were for substantial rehabilitation, affecting 197 units of residential housing. The annual rate of substantial rehabilitation exemptions range from a low of one property with three units in 2011, to the highest rates of nine properties comprising 58 units in 2014, and ten properties comprising 54 units in 2016. This represents less than one-third of one percent (0.31%) of the approximately 64,000 units covered under the Rent Adjustment Ordinance over a six-year period.

Of the 13 substantial rehabilitation exemptions granted in 2016 and 2017, only four were fully vacant properties, the remaining petitions involved properties with tenants. (Chart of exemptions granted since 2011 is included as ***Attachment B***)

Other Rent Stabilization Jurisdictions

There are nine (9) major cities in California with Rent Stabilization Ordinances: Oakland, Berkeley, San Jose, San Francisco, Santa Monica, Los Angeles, Hayward, West Hollywood, and Richmond. Until 1989, Los Angeles had a "Substantial Renovation" program (a type of "Substantial Rehabilitation") that exempted units from rent control when owners made renovation investments more than designated amounts. The program was rescinded because a survey of the program concluded that it resulted in displacement of tenants unable to afford the higher rents that owners charged after the units were removed from the rent control program and because it was a method of gentrification.¹ Like most other cities, Los Angeles adopted capital improvement policies which are divided into two components: renovation and capital improvements, allowing different rent increase pass-throughs under each category.

¹ Kenneth Barr report October 26, 1995: Issues and Options for the Rent Increase Standards Under Berkeley's Rent Stabilization Ordinance.

Currently, Oakland and San Francisco are the only California jurisdictions that allow a substantial rehabilitation exemption. However, requirements in San Francisco are more restrictive. These are San Francisco's requirements which all need to be met in order to qualify for an exemption based on substantial rehabilitation (**Attachment C**):

- The building is at least 50 years old;
- The building contained essentially uninhabitable residential units;
- "Substantial rehabilitation" of the building was required to conform to contemporary standards for decent, safe and sanitary housing; and
- The cost of the improvements (excluding insurance proceeds, land costs and architectural/engineering fees) was at least 75% of the cost of newly constructed residential buildings of the same number of units and type of construction.

By case law, the San Francisco exemption has been clarified to mean: "the intention [of the exemption and regulations is] to encourage landlords not merely to bring their buildings up to code (to create better housing), but to create new residential units where, essentially, there were none before (to create additional housing). Like the "new construction" exemption, this section cannot be applied to residential units where tenants are already in occupancy without contravening the Ordinance's explicit mandate to protect tenants from excessive rent increases."²

San Francisco's regulations are much more restrictive and, over the past six years, no exemptions were granted for substantial rehabilitation.³ The last substantial rehabilitation exemption granted was in 2006. (**Attachment D**)

Legislative History of Substantial Rehabilitation Exemption in Oakland

In September 2016, the City Council adopted amendments to the Rent Adjustment Ordinance that required any property owner issued a Certificate of Occupancy on or before September 20, 2016 to apply for a substantial rehabilitation exemption by June 30, 2017 or the exemption be deemed vacated.

On September 28, 2017, the Rules Committee delayed scheduling a discussion of amendments to the substantial rehabilitation regulations and requested that the Rent Board consider the matter and present recommendations.

On October 12, 2017, the Rent Board voted on the following options:

- To impose an immediate moratorium pending further study of potential impacts. The moratorium would be no less than 90 days and no more than one year.
(Vote: 4 Aye, 1 Nay, 1 Abstained)
- To eliminate substantial rehabilitation as an exemption.
(Vote: 3 Aye, 3 Nay)

² Da Vinci Group v. San Francisco (1992) 5 Cal.App.4th 27, 31

³ Per Robert Collins, Executive Director San Francisco Rent Board: most exemptions were granted in the 1980s before the Rent Board changed the regulations.

- To apply substantial rehabilitation exemption to empty or abandoned buildings only. In any occupied units, the tenants would be protected from the exemption.
(Vote: 2 Aye, 4 Nay)

While not ranked voting, each Board Member was allowed to vote on each of the options. As such, the vote did not reflect a clear preference of the Board Members as a whole. The two options receiving a majority vote were: 1) in favor of the moratorium and 2) opposition to applying the substantial rehabilitation exemption to empty or abandoned buildings only.

The results of the Rent Board vote were presented to the Rules Committee on October 19, 2017. Subsequently, on November 28, 2017, the City Council adopted Ordinance No. 13465 C.M.S. to impose a six-month moratorium on petitions for exemptions based on substantial rehabilitation filed on or after October 20, 2017.

On April 17, 2018, the City Council adopted Ordinance No. 13481 C.M.S. to extend the moratorium by an additional 180 days, until October 21, 2018.

Staff was directed to report back to the City Council with options and recommendations for modifying or eliminating the substantial rehabilitation exemption.

Staff prepared a report with recommended amendments to the exemption for the Rent Board to review and discuss at their July 26, 2018 meeting. The amendments, similar to how San Francisco's substantial rehabilitation exemption is structured, are as follows:

- 1) Require the substantial rehabilitation exemption be limited to buildings consisting of rental units over 50 or more years of age, which are vacant and essentially uninhabitable and that require substantial renovation to conform to contemporary standards of decent, safe, and sanitary housing;
- 2) Require that property owners provide proof that no preemptive, no fault evictions or displacement took place within 12 months prior to beginning the project;
- 3) Prohibit cosmetic improvements alone from qualifying as substantial rehabilitation;
- 4) Require improvements be substantial and equal at least 75 percent of the costs of newly constructed residential buildings;
- 5) Exclude rehabilitation costs that are compensated by insurance proceeds;
- 6) Deem substantial rehabilitation exemptions granted to a building temporary, expiring after 20 years.

The Board discussed these proposed amendments and surfaced a list of concerns and proposed ways to address these concerns through more narrowly defined terms, stricter timeframes, and tightened up language. Key concerns raised were:

- Ensure that properties eligible for this exemption be limited to vacant and essentially uninhabitable units;
- Eliminate or limit the ability to capture cosmetic improvements as an eligible substantial rehab cost; and
- Impose a reduced timeframe for the exemption period.

These and other suggestions are further described in **Attachment E**.

The Board also discussed two other options: 1) extending the moratorium for two to three years to enable staff to study the impact of this exemption and ensure that it is used to advance policy, and 2) eliminate the exemption entirely.

The Board voted on the three options, as follows:

- Extend the moratorium by three years and use that time to carry out a study.
(Vote: 3 Aye, 2 Nay)

- If the City Council does not approve the extended moratorium, amend the exemption using the framework of staff's proposals, but modifying the amendments further as described in **Attachment A**.
(Vote: 4 Aye, 1 Nay)

- Eliminate the substantial rehabilitation exemption entirely.
(Vote: 3 Aye, 2 Nay)

Similar to their prior vote, this was not ranked voting, and each Board Member was allowed to vote on each of the options. As such, the vote did not reflect a clear preference of the Board Members as a whole, with all options receiving a majority in favor.

ANALYSIS AND POLICY ALTERNATIVES

Analysis of Three Options

1. Extend the moratorium for three years to facilitate a study of the impact of the exemption on Oakland's housing inventory and tenant displacement and ensure that it advances City policy objectives.
 - **Description:** By extending the moratorium, staff would have the time to conduct an in-depth analysis, including drawing on the work and studies of others on this topic. Examples of areas of study and analysis are:
 - General overview of past substantial rehabilitation cases in Oakland (currently underway).
 - Collect and analyze data on rents and tenancies post-substantial rehab exemption.
 - Survey vacant properties, drawing from work already done and underway.
 - Prepare an analysis of how or whether this exemption has an impact on the city's policy objectives related to anti-displacement, ensuring owner investment in deteriorated properties, and incentivizing the re-use of vacant and uninhabitable buildings.
 - Policy analysis of how stricter provisions would impact Oakland's housing inventory and tenant displacement upon the granting of substantial rehab exemptions.

A factor in facilitating this option is Rent Adjustment Program (RAP) staff capacity. As a result of vacancies now being filled (including the Program Manager), the approval of new positions in the 2018/19 budget, and the addition of a new Deputy

Director position in the Housing and Community Development Department (HCD), the capacity will exist to carry out this option in a timely manner.

- **Pro's:**
 - Ensures a data-driven approach to determining how or whether to retain a substantial rehabilitation exemption in Oakland.
 - Provides data, which could be folded in with other data collection and analysis taking place in HCD and the City, which will better equip the Rent Board and City Council to make policy decisions on other related issues.
 - Increases RAP's and HCD's database and data collection capacity. Data collection and analysis is an area that HCD will be working to ramp up in the coming year.
 - **Con's:**
 - This activity will take staff away from other activities related to operating the Rent Adjustment Program.
 - The effort may result in information that does not materially impact City Council decision-making on this matter.
2. Amend the exemption to limit its application to units that are vacant and essentially uninhabitable and restrict its use in additional ways to protect against tenant displacement.
- **Description:** The original staff proposed amendments along with the Rent Board feedback are described in **Attachment E**.
 - **Pro's:**
 - Continues to provide this option for landlords to rehabilitate older, deteriorating properties, while seeking to eliminate its use as a tool to displace existing Oakland residents.
 - Has the potential to incentivize bringing vacant buildings back online.
 - **Con's:**
 - Will require a significant amount of time to craft ordinance language and regulations to ensure intent is met and changes are relevant to existing conditions.
 - Based on San Francisco's experience, as they made their language stricter and more narrowly focused, no exemptions were granted in 12 years. If this were to occur in Oakland, the time taken to revise the exemption provision could be considered inefficient.
 - Data is not available to back up the proposal that these amendments will have a positive impact in bringing vacant and essentially uninhabitable buildings back online.
3. Eliminate the substantial rehabilitation exemption.
- **Description:** This would remove the substantial rehabilitation exemption in its entirety. Landlords seeking to rehabilitate their buildings would still have the option to pass through the cost of their renovation work as capital improvements.

- **Pro's:**
 - Removes ambiguity and directs all landlords to the capital improvements provisions within the ordinance.
 - Will eliminate the permanent removal of units from coverage under the rent adjustment ordinance.
 - To the extent that the exemption results in rent increases beyond what is affordable to the tenants in the exempted units, the elimination of the exemption could prevent economic displacement.

- **Con's:**
 - The elimination of this exemption could reduce landlords' incentive to improve buildings if they determine that use of capital improvement rent increases did not provide adequate financial coverage. (However, an owner can file for a fair return on investment, or for other options for increases beyond capital improvement caps.)
 - Data is not available to back up the proposition that the exemption results in rent increases that displace Oakland residents.

Policy Alternatives

While not considered by the Rent Board, the City Council could allow the current regulations to stand as they were prior to the moratorium (***Attachment A***).

Summary

Of the nine major cities in California with rent stabilization ordinances, San Francisco and Oakland are the only cities that allow for a substantial rehabilitation exemption, with San Francisco's setting forth stricter requirements on what qualifies as "substantial rehabilitation." All of the other cities utilize one form or another of capital improvement pass-throughs to encourage investment in rental properties that bring buildings up to code and current sanitary housing standards.

In Oakland, units that are granted an exemption based substantial rehabilitation remain covered by the Just Cause for Eviction Ordinance. However, since they are no longer subject to controls on the rent, the increases that ensue following the granting of an exemption may become unaffordable to the current tenants and other Oakland residents who may find it difficult to remain in the city due to lack of affordable rents. While there is no collected data on the correlation between displacement and these substantial rehabilitation exemptions, rents continue to increase and tenants continue to be displaced in Oakland.

While it is important to encourage rehabilitation of deteriorating buildings in Oakland, the substantial rehabilitation exemption should either be modified or eliminated due to the potential impact the exemption may have on the ongoing problems of rising rents, tenant displacement, and loss of covered units under the Rent Adjustment Ordinance. As noted in the pro's and con's sections above, there is a lack of data to help inform a decision which could be addressed through the option of extending the moratorium to enable the proper study and analysis to occur. However, the proposed amendments to the existing ordinance as well as the elimination options have been employed in other jurisdictions and are options Oakland should consider and then evaluate annually upon enactment.

FISCAL IMPACT

Staff does not anticipate any fiscal impact caused by the selection of any of the options identified in this report.

PUBLIC OUTREACH / INTEREST

The Rent Board held two public meetings on the substantial rehabilitation exemption:

- At a meeting held on October 12, 2017 at which there were 18 public speakers.
- At a meeting held on July 26, 2018 at which there were 13 public speakers.

The Board also considered over 60 written comments submitted by stakeholders.

COORDINATION

Staff produced this report in coordination with the City Attorney's office. In addition, the Budget Bureau has reviewed this report.

SUSTAINABLE OPPORTUNITIES

Economic: The Rent Adjustment Ordinance can serve to preserve the affordable housing inventory for families, seniors, and persons with disabilities in the City of Oakland, as well as protect tenants from exorbitant rent increases while encouraging owners to invest in the housing stock of the City.

Environmental: Mitigate adverse environmental impacts of aging housing stock by ensuring investments in rental property. Encourage cohesion and the vested interest of owners and tenants in established neighborhoods resulting in positive impact on the environment.

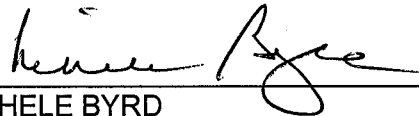
Social Equity: Improve the landscape and climate of Oakland's neighborhoods by encouraging long-term tenancies in rental housing. Assist low and moderate income families to save money to become homeowners.

ACTION REQUEST OF THE CITY COUNCIL

Staff Recommends That The City Council Receive A Report And Direct The City Administrator To Prepare The Necessary Legislation To Amend Chapter 8.22, Article I (Residential Rent Adjustment Program) Of The Oakland Municipal Code To Address The Future Of The Substantial Rehabilitation Exemption.

For questions regarding this report, please contact Michele Byrd, Director of Housing and Community Development Department at (510) 238-3714.

Respectfully submitted,



MICHELE BYRD
Director, Housing and Community Development
Department

Attachments (5):

- A: Chapter 8.22.030; Substantial Rehabilitation Exemption
- B: Substantial Rehabilitation Exemptions Granted (2011-2017)
- C: Summary of San Francisco Rehabilitation Exemption
- D: San Francisco Substantial Rehabilitation Case Log
- E: Substantial Rehabilitation Exemption: Staff Recommendations and Rent Board Comments, July 26, 2018

8.22.030 - Exemptions.

FILE
OFFICE OF THE CITY CLERK
OAKLAND

- 2018 AUG 31 AM 8:10
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- A. Types of Dwelling Units Exempt: The following dwelling units are not covered units for purposes of this chapter, Article I only (the Just Cause for Eviction Ordinance (Chapter 8.22, Article II) and the Ellis Act Ordinance (Chapter 8.22, Article II)) have different exemptions):
1. Dwelling units whose rents are controlled, regulated (other than by this chapter), or subsidized by any governmental unit, agency or authority.
 2. Accommodations in motels, hotels, inns, tourist houses, rooming houses, and boarding houses, provided that such accommodations are not occupied by the same tenant for thirty (30) or more continuous days.
 3. Housing accommodations in any hospital, convent, monastery, extended care facility, convalescent home, nonprofit home for the aged, or dormitory owned and operated by an educational institution.
 4. Dwelling units in a nonprofit cooperative, owned, occupied, and controlled by a majority of the residents.
 5. Dwelling units which were newly constructed and received a certificate of occupancy on or after January 1, 1983. This exemption does not apply to any newly constructed dwelling units that replace covered units withdrawn from the rental market in accordance with O.M.C. 8.22.400, et seq. (Ellis Act Ordinance). To qualify as a newly constructed dwelling unit, the dwelling unit must be entirely newly constructed or created from space that was formerly entirely non-residential.
 6. Substantially rehabilitated buildings.
 7. Dwelling units exempt pursuant to Costa-Hawkins (California Civil Code § 1954.52).
 8. A dwelling unit in a residential property that is divided into a maximum of three (3) units; one of which is occupied by an owner of record as his or her principal residence. For purposes of this section, the term owner of record shall not include any person who claims a homeowner's property tax exemption on any other real property in the state of California.
- B. Exemption Procedures.
1. Certificate of Exemption:
 - a.

A certificate of exemption is a determination by the Rent Adjustment Program that a dwelling unit or units qualify for an exemption and, therefore, are not covered units. For units exempt as new construction, or by state law, an owner may obtain a certificate of exemption by claiming and proving an exemption in response to a tenant petition or by petitioning the Rent Adjustment Program for such exemption. For units exempt based on substantial rehabilitation, an owner must obtain a certificate of exemption by petitioning the Rent Adjustment Program for such an exemption. A certificate of exemption may be granted only for dwelling units that are permanently exempt from the Rent Adjustment Ordinance as new construction, substantial rehabilitation, or by state law (Costa Hawkins).

- b. For purposes of obtaining a certificate of exemption or responding to a tenant petition by claiming an exemption from Chapter 8.22, Article I, the burden of proving and producing evidence for the exemption is on the owner. A certificate of exemption is a final determination of exemption absent fraud or mistake.
- c. Timely submission of a certificate of exemption previously granted in response to a petition shall result in dismissal of the petition absent proof of fraud or mistake regarding the granting of the certificate. The burden of proving such fraud or mistake is on the tenant.

2. Exemptions for Substantially Rehabilitated Buildings.

- a. In order to obtain an exemption based on substantial rehabilitation, an owner must have spent a minimum of fifty (50) percent of the average basic cost for new construction for a rehabilitation project and performed substantial work on each of the units in the building.
- b. The average basic cost for new construction shall be determined using tables issued by the chief building inspector applicable for the time period when the substantial rehabilitation was completed.
- c. An owner seeking to exempt a property on the basis of substantial rehabilitation must first obtain a certificate of exemption after completion of all work and obtaining a certificate of occupancy. If no certificate of occupancy was required to be issued for the property, in lieu of the certificate of occupancy an owner may provide the last

finalized permit. For any property that has a certificate of occupancy issued on or before the date of enactment of this subparagraph O.M.C. 8.22.30B.2.c. for which an owner claims exemption as substantially rehabilitated, the owner must apply for such exemption not later than June 30, 2017 or such exemption will be deemed to be vacated.

- C. Controlled, Regulated, or Subsidized Units. The owner of a dwelling unit that is exempt because it is controlled, regulated (other than by this chapter), or subsidized by a governmental agency (Section 8.22.030A.1) must file a notice with the Rent Adjustment Program within thirty (30) days after such dwelling unit is no longer otherwise controlled, regulated, or subsidized by the governmental agency. Once the dwelling unit is no longer controlled, regulated, or subsidized, the dwelling unit ceases to be exempt and becomes a covered unit subject to this chapter, Article I. Such notice must be on a form prescribed by the Rent Adjustment Program.
- D. Exemptions for Owner-Occupied Properties of Three or Fewer Units. Units in owner-occupied properties divided into three or fewer units will be exempt from this chapter, Article I under the following conditions:
 - 1. Two-Year Minimum Owner Occupancy. A qualifying owner of record must first occupy one of the units continuously as his or her principal residence for at least two years. This requirement does not apply to any property in which the owner resides in the premises on or before August 1, 2016.
 - 2. Continuation of Exemption. The owner-occupancy exemption continues until a qualifying owner of record no longer continuously occupies the property.
 - 3. Rent Increases. The owner of record qualifying for this exemption may notice the first rent increase that is not regulated by this chapter, article I two years after the date the qualifying owner of record starts residing at the affected property as his or her principal place of residence.
 - 4. An owner claiming such exemption must provide information to the Rent Program on when the owner occupancy began and documentation showing the minimum of two years continuous occupancy. Staff shall develop a form for this purpose.

(Ord. No. 13418, § 1(Exh. A), 2-7-2017; Ord. No. 13391, § 1, 9-20-2016; Ord. 12781 § 1 (part), 2007; Ord. 12538 § 1 (part), 2003; Ord. 12399 (part), 2002)

Attachment "B"

Substantial Rehabilitation Exemptions Granted: 2011 – 2017

	Case No.	Address	Number of Units
1	L11-0002	1061, 1061a & 1063 59th Street	3
2	L12-0009	5436-5442 Bryant Ave.	4
3	L12-0052	2337 Adeline St.	2
4	L12-0061	2415 San Pablo St.	5
5	L12-0062	765 MacArthur Boulevard	10
6	L12-0063	640 East 15th St.	9
7	L13-0001	2505 San Pablo Ave.	14
8	L13-0025	1471 Excelsior Ave.	2
9	L13-0049	764 59th St.	3
10	T13-0196	1010 Walker Ave.	5
11	L14-0007	5560 and 5562 Fremont St.	2
12	L14-0015	681 24th St.	4
13	L14-0016	4133, 4135, 4137, 4139 Martin Luther King	4
14	L14-0025	412 Monte Vista Ave.	14
15	L14-0032	771 Kingston Ave., No. 205	1
16	L14-0043	33 Deering Ct.	4
17	L14-0061	675 - 56th St.	2
18	L14-0069	1824 Lakeshore Ave.	25
19	T14-0197	350 24th St. and 352 24th St.	2
20	L15-0008	654, 656, and 658 Alcatraz Ave.	3
21	L15-0013	5414 - 5416 Boyd Ave.	2
22	L15-0034	1244 2nd Avenue	12
23	L16-0003	1601-1605 Clay Street	20
24	L16-0013	643 E. 18th St.	4
25	L16-0017	374 41st Street	4
26	L16-0026	306 Lenox Avenue	3
27	L16-0040	369 Orange Street	4
28	L16-0052	2325 Ransom Ave.	3
29	L16-0054	1426/1428 Glenfield Ave.	6
30	L16-0055	4507/4509 Martin Luther King Jr. Way	2
31	L16-0057	366 51st St.	4
32	L16-0086	373 Fairmount Ave.	4
33	L17-0011	1035-1037 Adeline St.	2
34	L17-0014	4525-4531 Edgewood Ave.	4
35	L17-0025	886-888 45th Street	5
		TOTALS	197

Substantial Rehabilitation Exemptions Per Year

	Properties	Units
2011	1	3
2012	5	30
2013	4	24
2014	9	58
2015	3	17
2016	10	54
2017	3	11
TOTAL	35	197

San Francisco Residential Rent Stabilization and Arbitration Board

GENERAL INFORMATION REGARDING LANDLORD PETITION FOR EXEMPTION BASED ON SUBSTANTIAL REHABILITATION

Landlords may file a petition to exempt a building from the Rent Ordinance if the building has been substantially rehabilitated. There are stringent requirements to qualify for a substantial rehabilitation exemption, as set forth below. Major remodeling done for the purpose of upgrading older units rarely qualifies as "substantial rehabilitation."

"Substantial rehabilitation" means the renovation, alteration or remodeling of a building containing *essentially uninhabitable* residential rental units of 50 or more years of age that require substantial renovation in order to conform to contemporary standards for decent, safe and sanitary housing. [Rules and Regulations Section 1.18]

"Essentially uninhabitable" means defects that are so severe that the building as a whole (1) is unsafe for occupancy and poses an imminent danger to the health, safety and welfare of its occupants and/or the general public, and/or (2) has been found by a court, the Department of Building Inspection, the Department of Public Health or similar agency to pose an imminent danger to the health, safety and welfare of the occupants, neighboring properties and/or the general public.

In order to qualify for exemption based on substantial rehabilitation, the landlord must, at a minimum, prove ALL of the following elements with credible documentary evidence:

- (a) That the building is at least 50 years old;
- (b) That the building contained essentially uninhabitable residential units;
- (c) That "substantial rehabilitation" of the building was required to conform to contemporary standards for decent, safe and sanitary housing; and
- (d) That the cost of the improvements (excluding insurance proceeds, land costs and architectural/engineering fees) was at least 75% of the cost of newly constructed residential buildings of the same number of units and type of construction.

In general, a petition for exemption based on substantial rehabilitation can be filed at any time after the work has been completed, as long as the work was completed after June 13, 1979. However, a landlord who recovers possession of a rental unit under Ordinance Section 37.9(a)(12) in order to carry out substantial rehabilitation work must file the petition for exemption within the earlier of two years following recovery of possession of the rental unit or one year following completion of the work. A landlord who fails to file a petition within such time and thereafter obtain a determination of exempt status from the Rent Board, shall be rebuttably presumed to have wrongfully recovered possession of the tenant's rental unit in violation of the Ordinance. [Rules and Regulations Section 1.18]

Tenants may raise objections to the Substantial Rehabilitation Petition based upon any of the following: that the work was not done; that the work was necessitated by the current landlord's deferred maintenance resulting in a code violation; that the costs are unreasonable; and/or that the work was not principally directed to code compliance. [Rules and Regulations Section 8.17]

INSTRUCTIONS FOR FILING A PETITION FOR EXEMPTION BASED ON SUBSTANTIAL REHABILITATION

1. The petition form must be completely filled out and signed by the landlord or the landlord's authorized agent.
2. In addition to the original petition, the landlord must submit a copy of the completed petition, with attachments, for each tenant and tenant representative listed in the petition, plus one extra copy for the Rent Board staff.
3. For each tenant and tenant representative named in the petition, the landlord must provide 2 business size envelopes and 1 large flat envelope (at least 9" x 12"), pre-addressed to each person, with NO return address but with the following postage affixed: one of the business size envelopes will be used to mail the Notice of Hearing and must have first class postage for one (1) ounce and, one must have first class postage for two (2) ounces for mailing the Decision. The large envelope must have sufficient first class postage for mailing the petition and supporting evidence. *If a postage meter is used instead of stamps, please do NOT include a date on the meter marking.*

San Francisco Residential Rent Stabilization and Arbitration Board

4. For each landlord and landlord representative who should receive a copy of the Notice of Hearing and the Decision, the landlord must provide 2 business size envelopes, pre-addressed to each recipient, with NO return address but with the following postage affixed: one of the envelopes will be used to mail the Notice of Hearing and must have first class postage for one (1) ounce; and, one must have first class postage for two (2) ounces for mailing the Decision. *If a postage meter is used instead of stamps, please do NOT include a date on the meter marking.*
5. The landlord must pay the cost of an independent estimator hired by the Rent Board. The Estimator Fee Schedule is available on the Rent Board's website and is based upon the full cost of the work. The fee must be paid at the time the petition is filed. Make the check payable to the San Francisco Rent Board.

ADDITIONAL SPECIFIC REQUIREMENTS

ALL of the documents enumerated below must be attached to the petition. Be sure to submit sufficient copies for the Rent Board to mail to the tenant(s) along with a copy of the petition. The materials should be assembled in the following order, with each section clearly marked and separated by tabs or dividers.

6. Written Explanation of Basis for Petition – The landlord must include a written summary explaining the basis for the petition, and why the building qualifies for exemption from the Rent Ordinance based on substantial rehabilitation. Specifically, the written summary should address each of the following requirements: that the building is at least 50 years old; that prior to commencement of the work, the building contained *essentially uninhabitable* residential units; that "substantial rehabilitation" of the building was required to conform the building to contemporary standards for decent, safe and sanitary housing; and, that the cost of the improvements (excluding insurance proceeds, land costs and architectural/engineering fees) was at least 75% of the cost of newly constructed residential buildings of the same number of units and type of construction as calculated in accordance with the applicable DBI Cost Schedule.
7. Tenant History [R & R Sec. 8.12(1)] – The landlord must submit a list of all current tenants and the amount of their current rents. In addition, if any tenants were served a notice to terminate tenancy based on the substantial rehabilitation work, the landlord must include a list of all such tenants, their last known address, the amount of rent at the time they left voluntarily or were evicted, and which tenants were evicted pursuant to the notice.
8. Detailed Description of Work Performed and Itemization of Costs [R & R Sec. 8.12(2)] – To satisfy this requirement, the landlord must include a detailed description of the nature and location of the work performed and an itemization of all costs, plus documentary evidence such as: written construction contracts, bids, change orders and/or invoices that specify the scope and cost of the work; building permit applications; 3R Reports; and, reduced copies of blueprints or plans that show the lot size, grading, elevation and existing and new building configuration, including the square footage of habitable and non-habitable areas. The building description must be sufficiently detailed to enable the Administrative Law Judge to estimate the cost of a comparable newly constructed building with reference to the Cost Schedule published by the Department of Building Inspection (DBI). (*See additional information below regarding the DBI Cost Schedule.*)
9. Evidence that Building is At Least 50 Years Old [R & R Sec. 8.12(3)] – This requirement may be satisfied by attaching a 3R report and/or records from the DBI that show when the building was constructed.
10. Evidence that Building is Essentially Uninhabitable [R & R Sec. 8.12(4)&(5)] – The landlord is required to submit with the petition either a determination of condemnation, a determination by the DBI that the premises were ineligible for a permit of occupancy, or other evidence that the building was "essentially uninhabitable." "Essentially uninhabitable" means defects that are so severe that the building as a whole (1) is unsafe for occupancy and poses an imminent danger to the health, safety and welfare of its occupants and/or the general public, and/or (2) has been found by a court, the Department of Building Inspection (DBI), Department of Public Health or similar agency to pose an imminent danger to the health, safety and welfare of the occupants, neighboring properties and/or the general public. If there is no order of condemnation or similar determination, the landlord may attempt to satisfy this requirement by submitting Notices of Violation, citations, professional inspection reports and similar evidence of code violations, with photographs of the pre-existing conditions, if possible.

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11. Current Abstract of Title [R & R Sec. 8.12(6)] – This requirement may be met by submitting a Title Report
12. Pre-Improvement Inspection Report by DBI [R & R Sec. 8.12(7)] – The petition must include a complete inspection report issued by the DBI prior to commencement of the substantial rehabilitation work. Landlords who anticipate doing substantial rehabilitation improvements should contact the DBI and request an inspection well before beginning the work.
13. Proof of Purchase Price [R & R Sec. 8.12(8)] – This evidence may include such items as the purchase agreement and/or a final escrow statement that shows the purchase price.
14. Final Notice of Completion [R & R Sec. 8.12(9)] – The petition must include a copy of the DBI's Final Notice of Completion issued after completion of the substantial rehabilitation work.
15. Eviction Notices [R & R Sec. 8.12(10)] – If any tenants were evicted because of the substantial rehabilitation work, copies of the eviction notices must be attached to the petition.
16. Proof of Cost and Payment [R & R Sec. 8.12(11)] – The petition must include proof that each of the claimed costs was paid. For each itemized cost, attach the proof of cost such as a bill or invoice first, followed immediately by the proof of payment such as a cancelled check, cash register receipt (for cash payments) or credit card statement. The documents should be clearly marked and separated according to each itemized cost. For each item, organize the documents in chronological order (earliest document first). Where a single check proves payment for more than one itemized cost, a separate copy of the check should be attached to each bill or invoice for which the payment was made. Likewise, if a single bill or invoice covers more than one item, a separate copy of the invoice should be provided for each item. If the landlord has received insurance proceeds for any portion of the costs, evidence of the insurance payments must also be supplied.
17. Current Assessment [R & R Sec. 8.12(13)] – A complete copy of the current property tax bill must be attached.
18. Claims for Uncompensated Labor [R & R Sec. 8.12(14)] – If the landlord or any other person performed work without being compensated, the landlord may include the costs of the uncompensated labor in the petition. Claims for uncompensated labor must be accompanied by a detailed log of dates, hours worked and description of the work performed. Unless the person performing the work is a licensed contractor (e.g. general, electrical, plumbing), the cost must be calculated at the standard labor rates posted by the Rent Board ("Capital Improvement Uncompensated Labor Rates"). Use the rate in effect at the time the work commenced. Persons seeking compensation at higher rates must submit a copy of the worker's contractor's license, proof of the licensed contractor's current active status, and evidence of prevailing labor rates for that trade or type of work.
19. Estimating the Cost of Newly Constructed Buildings [R & R Sec. 1.18] – Improvements will not be deemed "substantial rehabilitation" unless the cost of the work for which the landlord has not been compensated by insurance proceeds equals or exceeds 75% of the cost of a newly constructed residential building of the same number of units and type of construction, excluding land costs and architectural/engineering fees. The determination of the cost of newly constructed residential buildings is based upon construction cost data reported by Marshall and Swift, Valuation Engineers, as adapted for San Francisco and posted by the Department of Building Inspection for purposes of determining permit fees. The DBI Cost Schedule in effect on the date the Building Inspector gives final approval of the completed improvements shall apply. The applicable DBI Cost Schedule must be attached to the petition. *(If the landlord is unable to obtain a copy of the applicable DBI Cost Schedule, please contact the Rent Board's Senior Administrative Law Judge for assistance.)*

The landlord must provide a written explanation of how the landlord calculated 75% of the cost of a similar newly constructed building and complete the worksheet on Page 4 of the Petition. The method for calculating the cost of a newly constructed building is complicated, and requires the landlord to provide detailed information about the building and building site. For example, a description of such items as the degree of hillside grade, the amount of excavation and paving, the type of construction, the occupancy classification, the square footage of habitable and non-habitable areas, the type and amount of fire-rated walls, and numerous other specific features must be provided with the petition. **In order to properly calculate the cost, landlords are strongly encouraged to consult the DBI and/or retain a professional construction estimator who is familiar with the DBI's methodology.**

Attachment D

SUB REHAB CASE LOG

<u>Case #</u>	<u>Address</u>	<u>Decision</u>	<u>Date Mailed</u>
D10-3(A)	285 Turk Street	Exempt	5/13/85
F10-27C	1445 Larkin St.	Exempt	5/28/85
F10-28C	1455 Leavenworth	Exempt	6/27/85
F12-11C	400-410 Cole St.	Exempt	9/26/85
G14-18C	3314-3320 16th Street	Exempt	1/26/89
H001-16C	801 Haight St.	Exempt	11/4/86
H001-28C	818-822 Stanyan St.	Denied	1/13/87
H001-35C	131-135 Duboce Ave.	Exempt	12/4/86
H002-09C	524 Guerrero St.	Exempt	3/2/87
I003-24C	1400 Jones St.	Denied	1/3/89
I003-30C	460-1/2 Day St.	Exempt	11/7/88
J001-88C	388 5th Street	Exempt	7/17/89
J001-96C	221-231 Pierce St.	Denied	7/17/89
J002-12C	612 Steiner St.	Exempt	6/9/89
J002-52C	601-645 Minnesota St.	Exempt	7/31/89
J003-07C	731-755 Florida	Denied	4/20/90
K001-62C	1530 Jones St.	Denied	7/6/90
L001-07C	644-78 Lyon	Exempt	3/15/91
M001-17C	14 Moss St.	Admin. Dismissal	1/17/92
O002-17C	1785 O'Farrell	Exempt	8/1/96
P002-48C	481-483 Clementina	Exempt	9/30/96
Q001-23C	4335 Anza	Withdrawn	6/19/96
Q001-77C	2616-A Sutter	Withdrawn	
R002-19C	2616-A Sutter	Denied	5/22/98
Q001-92C	257-259 South Van Ness	Denied*	9/23/98
L980106	688-690 South Van Ness	Denied	12/21/99
L991387	1074-1076 Carolina Street	Admin. Dismissal	2/3/00
L980424	1117 Geary Street	Exempt	9/8/00
L011040	1345-47 25 th Avenue	Denied	2/7/02
L011181	1435 Eddy Street	Exempt	2/22/02
L010179	540 Bartlett	Withdrawn	4/2/02
L2K1274	1905 O'Farrell	Admin. Dismissal	9/28/05
L011118	1420-1424 Guerrero	Closed w/out Prej.	12/10/03
L030692	547 23 rd Avenue	Admin. Dismissal	12/9/03
L040332	1301 Leavenworth	Exempt	4/5/05
L040575	827 Pierce/1401-1403 McAllister	Denied	3/16/06
L041356	2927-2929 23 rd Street	Withdrawn	3/4/05
L041506	215-217 Precita Avenue	Withdrawn	6/7/05
L051515	1101-1123 Fillmore Street	Denied	5/26/06
L060523	2126 Steiner Street	Exempt	12/13/06
L140755	32-36 Pleasant Street	Withdrawn	7/29/14

Attachment E

Substantial Rehabilitation Exemption Staff Recommendations and Rent Board Comments July 26, 2018 Rent Board Meeting

Staff Recommendation	Rent Board Comments
(1) Require the substantial rehabilitation exemption be limited to buildings consisting of rental units over 50 or more years of age, which are vacant and essentially uninhabitable and that require substantial renovation to conform to contemporary standards of decent, safe, and sanitary housing	<ul style="list-style-type: none"> • Define “vacant” and “essentially uninhabitable.” • Ensure that the objective being met is to increase inventory of new units • Bring back units that are offline back into service. • Identify how many vacant units and/or buildings we have that could be positively impacted by this provision. • Units must be uninhabitable and exemption not cause displacement. • Grant exemption only to buildings no one has wanted to touch.
(2) Require that property owners provide proof that no preemptive, no fault evictions or displacement took place within twelve (12) months prior to beginning the project	Consider increasing; is 12 months the right timeframe?
(3) Prohibit cosmetic improvements alone from qualifying as substantial rehabilitation	<ul style="list-style-type: none"> • Define cosmetic, ensure against abuse. • Prohibit gold plating. • Put a cap on the amount of cosmetic work allowed in a given substantial rehab project.
(4) Require improvements be substantial and equal at least 75% of the costs of newly constructed residential buildings	Define “substantial.”
(5) Exclude rehabilitation costs that are compensated by insurance proceeds	Add land costs and architectural fees to this exclusion.
(6) Deem substantial rehabilitation exemptions granted to a building temporary, expiring after 20 years.	Decrease number of years (consider five or ten years) for exemption, look to amortization period for paying off cost or rehab; look at capital improvement amortization periods.
Other Rent Board comments	<ul style="list-style-type: none"> • Emphasized importance of having the opportunity to more concretely specify the restrictions through Board regulation. • Use a race and equity lens when making these revisions.