Explain how rents would be affected if a landlord recovers the cost of capital improvements through the fair return on property process (maintenance of net operating income).

In rent controlled jurisdictions, courts hold that constitutionally landlords must receive a fair return on property. Although there are several ways such fair return can be calculated, the one most commonly used, and one approved by the courts, is the maintenance of net operating income (MNOI) process. Under that process and in simple terms, there is a comparison of a landlord's net operating income (total revenue from the rental property less certain, enumerated expenses) in a "base year" with the landlord's current net operating income (usually for the year, or for the 12 months, prior to filing a petition for an upward adjustment of rents). If the NOI in the base year, as adjusted by inflation, is less than the NOI in the current year, then the landlord is entitled to a rent increase to maintain the NOI.

Some rent controlled jurisdictions provide that the amortized cost of capital improvements may only be recovered through the MNOI process. Typically, the scope of the capital improvements that may be amortized is significantly broader that those currently found in Alameda's CIP Policy or that are being proposed in the CIP Ordinance. For example where the cost of capital improvements is recovered through the MNOI process, the cost of items such as refrigerators, windows, doors, and the like are often included and their amortization period much less (as low as five years) compared to the 15 year amortization period for all capital improvements in Alameda's current CIP Policy and as proposed in the CIP Ordinance. By including the amortized cost of capital improvements in the "expense" column for the "current" year, a landlord presumably reduces its net operating income, thereby enhancing the chances that the landlord will receive a rent increase in order to maintain the NOI.

If a landlord is granted a rent increase through this MNOI process, that increase becomes part of that tenant's base rent and the Annual General Adjustment is then applied to that higher base rent. Even if the amortization for a particular capital improvement expires, the rent is not reduced.

Example: Monthly Rent at Year 0 is $2000/month

Year 1:	2% AGA		40
	4% MNOI Adjustment		80
	Total	[2000 + 40 + 80]	$2120/monthly
Year 2:	3% AGA [$2120 x 3% = $64]		64
	Total	[2120 + 64]	$2184/monthly
Year 3:	2% AGA [$2184 x 2% = 44]		44
	1% MNOI Adjustment		22 [Adjustment applied to $2184]
	Total	[2184 + 66]	$2250/monthly
Year 4:	5% AGA [$2250 x 55 = $113]		113
	Total	[2250 + 113]	$2363/monthly

Explain how much a tenant would owe each month if a landlord recovers the cost of capital improvements through the CIP pass-through provisions, with a 5% pass-through cap, and how that monthly amount compares to the monthly rent under the MNOI process described above.

The CIP Ordinance, as proposed, would place a cumulative pass-through cap of 5% for the recovery of all amortized capital improvement costs.

As in the example above, assume the following: In year zero, a tenant's monthly rent is $2000/month. In year 1, the Annual General Adjustment is 2% and a landlord receives a 4% pass through. In year 2, the AGA is 3%. In year 3, the AGA is 2% and the landlord receives an additional pass through but the pass through is capped at a cumulative 5%. In year 4, the AGA is 5%.

With these assumptions as to a capped pass through, and the assumptions in the example above as to MNOI adjustments that parallels the capped pass through percentages, in four years, a tenant would be paying approximately $11 more a month under the MNOI calculation as compared to a pass through. Moreover, the longer the tenant remains in the rental unit, the larger the monthly difference would become.

Year 1:	2% AGA		40	
	4% Pass-through		80	
	Total	[2000 + 120]	$2120	(same as 4% MNOI)
Year 2:	3% AGA	[2040 x 3%]	61	
	Pass through		80	
	Total	[2040 + 61 + 80]	$2181	($2184 with 4% MNOI)
Year 3:	2% AGA	[2101 x 2%]	43	
	Pass through		80	
	Additional pass through			
	Capped at 1%	[2101 x 1%]	21	
	Total	[2144 + 101]	$2245	($2250 with 5% total MNOI)
Year 4:	5% AGA	[2144 x 5%]	107	
	Pass through		101	
Total		[2251 + 101]	$2352	($2363 with 5% total MNOI)

Explain how rent increases that have been frozen since April 2020 will be imposed once the local emergency is rescinded and how a pass through approved in 2021 would be imposed.

City Council has frozen rent increases that were not imposed as of April 22, 2020. Currently these rent increases are frozen until 60 days after the City Council rescinds the declaration of local emergency due to the COVID-19 pandemic. This means that for landlords who had not increased rents by the September 1, 2019 AGA (2.8%), they have been precluded from imposing that rent increase. For all landlords subject to the AGA, they also have been precluded from imposing the AGA that was effective

September 1, 2020 (1%). Assuming the declaration of local emergency is still in effect as of September 1, 2021, landlords subject to the AGA will not be able to impose the September 1, 2021 AGA.

Assume the following: A tenant's monthly rent as of April 22, 2020 was $2000/month and that the "anniversary date" for a rent increase was July 1. The landlord receives a capital improvement pass through of 5% in August 2021. The AGA for September 2021 is 2%. City Council rescinds the local emergency as of November 1, 2021.

Monthly Rent as of April 22, 2020--$2000/month
"Anniversary" Date of Rent Increase—July 1, 2020
Landlord Receives 5% Pass Through—August 2021
September 2021 AGA—2%
City Council rescinds Local Emergency—November 1, 2021

January 1, 2022—Landlord imposes a rent increase of 3.8% (AGA for 2019 and 2020)--$2076/month [$2000 x 3.8% = $2076]

July 1, 2022—Landlord impose a rent increase of 2%--$ 2160/month [$2076 x 2% = $2160]

November 1, 2022—Landlord "passes through" $100 ($2000 x 5%)—Tenant's total obligation--$2260 [$2160 + $100 = $2260]

July 1, 2023—Landlord could impose the September 2022 AGA rent increase on the $2160

Landlords will be encouraged to "bank" previously "frozen" rent increases in order not to burden unreasonably the financial impact such increases may have on their tenants. The Regulations provide that if the AGA rent increases that were frozen are "banked", such banking will not count against the limitations applicable to banking rent increases, i.e., only every other year and not more than three times for any one tenancy.

Caveat

With all the examples above, keep in mind that if all the rent from March 2020 until the local emergency is over has not been paid due to financial impacts from the pandemic, and if proper notices have been provided from the landlord to the tenant, and from the tenant to the landlord, the unpaid rent is a civil debt and not debt that could result in the tenant's eviction.