

GREATER VALLEY GLEN COUNCIL

COMMITTEE: Government Relations

MEETING DATE: January 21, 2009

(To be submitted to President at least 120 hours in advance of monthly board meeting)

PROPOSED MOTION FOR BOARD ACTION:

The City Council should revise ordinance number 180441 also known as “Eviction of Tenants from Foreclosed Residential Rental Properties or Article 14.1 of Chapter IV of the Los Angeles Municipal Code. After the one-year sunset clause, the City Council should not renew the ordinance, unless previously altered to apply only to buildings with five units or more.

This ordinance was not properly vetted. Neighborhood Councils and stakeholders did not have sufficient time to comment. The issue was initiated by the City Council on December 11, 2008 and signed into law on December 23, 2008.

This ordinance:

1. Should only apply to rental buildings with five units or more.
2. Negatively impacts the salability of foreclosed homes, condos and townhouses because tenant-occupied properties are difficult to sell and eventually sell for a lower price on average than vacant or owner-occupied properties. A buyer would not be wise to buy a property with a tenant intact unless it is an apartment building or the buyer is seeking a rental property.
3. Hurts buyers, (often first time buyers with limited funds), who will inherit a property with a tenant, then have to go through the costly eviction process and possibly incur tenant-related damages to the home. It also hurts buyer insurance and financing options. The buyer may have to obtain a non-owner occupied loan at a much higher interest rate.
4. Will lead to more “for sale” inventory on the market and drive down property values. It hurts the real estate market as a whole when properties sit for a long time then sell for less. It also hurts the sellers who lost the home (and may face greater tax consequences with a lower sales price) and the taxpayers whose money is going to bail out banks. It also hurts neighbors who are looking to refinance their home, which they often cannot do when property values in the area are low.
5. Will lead to scams. Opportunists will take advantage of banks by creating fake rental agreements at “under market” value rents, then leave with thousands in relocation fees and reimbursement of a security deposit that they never paid in the first place. .
6. Will lead to fewer short sales and potentially greater tax consequences for those who are losing their property to foreclosure. Tenants will have no reason to cooperate with short sales. They will have incentive to let properties go into foreclosure because they will want the relocation fees.
7. Will lead to reluctance by banks to lend in the future, especially on rental properties.
8. Will potentially reduce tax revenues.
9. May violate the Costa-Hawkins law.

Instead, the City Council should:

1. Mandate that banks inform occupants (tenants) by mail when a notice of default is filed on a property.
2. Revise the ordinance so that it only applies to multi-family residences that are 5 units or greater.
3. Encourage banks to keep the exterior of vacant properties tidy and watered, and free from vagrants.”

PROPOSED COMMUNITY IMPACT STATEMENT (if applicable) – 100 words or less:

(Attach to any applicable Council File) Council File # 07-2438-S9

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COMMUNITY BENEFIT STATEMENT (if applicable – 100 words or less)*

***all non-operation expenditures must attach Agency or Department Letter Requesting item(s) or donation(s) to Committee prior to Committee vote;**

Protect Greater Valley Glen property owners and buyers and renters .

PROPOSED BUDGET EXPENDITURE (if any): None

IMPACT ON FISCAL YEAR BUDGET ALLOCATION BY CATEGORY & QUARTER:

(1st quarter 7/1-9/30 – 2nd quarter 10/1-12/31 – 3rd quarter 1/1 - 3/31 – 4th quarter 4/1-6/30) No impact

All Non Operational Expense Motions must attach Agency or Department Letter Requesting item(s) or donation(s);

About the ordinance and arguments....

In the first two quarters of 2008, there were 5,800 foreclosures in Los Angeles. 60% were in the San Fernando Valley. During the second half of 2008, LA foreclosures were down 51% unlike other cities where there has been an increase.

In its motion, the City Council admits that 96% of foreclosed rental properties are subject to the rent stabilization ordinance (RSO), 56 multi-family projects are not. They add that there are some tenant-occupied single-family residences as well, but no exact number is provided.

Prior to this ordinance, state law provided that bank would have to give the tenant at least a 60-day notice to vacate the property and must reimburse the tenant's full security deposit.

In Nov. 2008, the City Council voted to draft a law banning evictions of renters in foreclosed properties. This new ordinance makes the Rent Stabilization Ordinance (RSO) applicable to all residential rental properties, including single-family dwellings and newly constructed multi-family dwellings. It has a one-year sunset provision, but can be extended by City Council vote.

It is understandable that the City Council would want to protect tenants who have done nothing wrong, but this new law goes too far.

My experience as a Realtor for 20 years is that tenants typically stop making their monthly payments when they realize a foreclosure is coming. They will usually end up with one to two months (and sometimes more) of rent free during this process.

A. The new law is not necessarily problematic for newer multi-unit buildings that are five units or greater. There are two reasons.

1. These properties are purchased up front as rental properties. The bank would have a rental schedule prior to a foreclosure; in other words, the bank would have confirmation as to the true values of the rental units. The bank's appraiser would have looked at the units and set particular values for each.

2. Multi-unit buildings are typically sold with tenants intact; therefore, letting the tenants remain will not affect the sales price in any substantial way. Buyers are used to doing a "drive by" then viewing the interiors only when their offer is accepted by the seller. The numbers matter most in this sort of transaction; the interior of the units is of a lesser concern. .

* Those who are opposed to rent control law will no doubt worry about a slippery slope in which all properties (not just those build prior to 1978) will eventually be subject to rent stabilization laws. However, a slippery slope seems unlikely.

B. Why it is a bad law for single-family residences, condos, townhouses and buildings with 4 or fewer units (although there are few buildings with 4 units or less built after 1978):

The new law will encourages scams

Single family residences or buildings with four units or less are rarely purchased up front as income properties; therefore, the bank is unlikely to have a rental schedule on their books. Without this, the bank will be subject to scams. For example, two sellers with two separate homes who are facing foreclosures could agree to rent each other's houses for a minimal sum of \$200 per month. The bank would not be permitted (per the new law) to evict the scammers and would even have to pay the delinquent sellers who are posing as renters thousands of dollars in relocation fees (as per RSO law) and security deposit monies (even though none were actually paid). In a similar scenario, a seller facing foreclosure could put a friend or relative into the soon-to-be bank-owned house as a "renter" for a minimal monthly sum. Since the rent is far below market, the "renter" friend could give the seller a monthly kickback, plus split the eventual relocation fee with him or her.

The new law will lead to an increase in foreclosures

Short sales are a popular way to avoid foreclosure. They are less disastrous for the property owner's credit and save the bank foreclosure expenses. They mean a higher sales price because a property can be sold before it falls into disrepair. The higher sales price is better for the owner losing the house (tax-wise) and the bank (which has potentially been supplemented by taxpayer bailout funds from Congress). Overall it is a win-win for everyone, or at least turns a bad situation into a palatable one. Currently, I find tenants cooperative with the short sale process. They will often move if their lease has ended or will be amenable to showings. But with the new law, it is not in the tenant's best interest to cooperate. If they stay put, they can receive thousands in relocation fees. Tenants can and do ruin sales when they want to. On many occasions as a Realtor, I have heard them tell buyers things like "Oh, this is horrible neighborhood" or "the house is falling apart" – anything to ruin the sale so they don't have to move. By putting their situation under rent control law, they can get away with living rent-free while the bank forecloses and later get thousands of dollars in relocation fees in addition to security deposit monies in full. Why be cooperative when they themselves can profit handsomely from the bank later? Uncooperative tenants = fewer short sales and more foreclosures.

The new law will lead to lower sales prices for foreclosed single-family residences

About 99% of the time, single-family residences sell for a higher price when they are not occupied by a tenant. The only exception would be a tenant who is neat and tidy, has gorgeous furniture and allows Realtors full access to show the premises. This is extremely rare. I can remember one instance in over 20 years of selling real estate. I normally tell my sellers that they should not sell a single-family rental property until it is vacant if they want to get top dollar. As stated above, a tenant may intentionally make snide comments or keep the property messy so as to discourage buyers, or even refuse to allow access. I realize they are supposed to allow access by law, but trust me, if you don't go along with them, they can sabotage a sale. Tenants can easily make the property unsaleable. Properties with lockboxes sell the fastest and often for the highest price, and tenants rarely allow lockboxes. Many agents do not want to go to the trouble to arrange showings through tenants, so decline to show tenant-occupied properties at all. I myself am always hesitant about showing a property with a tenant because it is invariably more of a hassle to show and usually shows poorly. Lower sales prices hurt overall market conditions. When the sales price is lower, the previous owner can be subject to greater tax consequences, and banks get less revenue, which means public funds are wasted (in light of the taxpayer bailout dollars that continue to go to banks). Plus it means banks will have less to lend in the future. In addition, a new buyer is not going to want to purchase a house in with a tenant intact.

The new law puts a huge burden on the new buyers of foreclosed properties

According to the RSO, when a property is sold, the tenant remains with the property. This puts an undue burden on the new buyer, especially for single-family residences if the buyer would even agree to purchase it in the first place. Most buyers of single-family residences (condos, townhouses) and even 1-4 unit buildings plan to live on the premises. Often they can barely scrape together the funds to buy. Now they are being saddled with a tenant whom they cannot evict until 60 days after the close of escrow due to the new ordinance. Only a savvy investor who gets a house dirt cheap would be interested in buying a house with a tenant. As a Realtor, I advise buyers to stay away from any tenant-occupied property unless the tenant is off the property well in advance of the close of escrow. Otherwise the buyer can lose appraisal, inspection and other fees and costs, and the tenant may refuse to leave at the COE. I've seen it happen time and time again. It is wholly unreasonable for the City Council to expect buyers—many of them novices at real estate transactions—to inherit tenants and go through the difficult and expensive eviction process. The tenant can also cause thousands of dollars in damage after the sale. Even if a buyer agrees to take the tenant, he or she might not be able to obtain an owner-occupied loan (since technically the property will not be owner-occupied after the COE); thus would be forced to pay a higher interest rate for a rental property loan and buy landlord insurance.

The new law will exacerbate a downturn in the real estate market

Banks will lose thousands of dollars due to the ordinance and will be less likely to want to lend, especially on rental properties. Taxpayer bailout dollars will be lost. Buyers will not want to make offers on properties that fall under this ordinance if for no reason other than the difficulty with evicting the tenant after the sale. These properties will sit on the market and hurt the market further. The City would be responsible for a further decline of values.

* Instead of the new ordinance, maybe banks should be required to keep foreclosure properties in reasonable condition on the exterior and defend from vagrants

It is in their best interest to keep the property up and keep vandals and vagrants away.

FYI: Current Law:

The current law with respect to tenants and foreclosures: Bank can evict with 60-days notice, regardless of whether there is a lease. Bank must return security deposit.

In rent controlled buildings, tenants cannot be evicted except for just cause. Just cause would be not paying the rent, trashing the place, engaging in illegal activities. Foreclosure does not qualify as "just cause" although it does in many East Coast communities.