Attachment G
Homeowners' Post-Hearing Opening Brief

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BEFORE THE COUNTY OF SANTA BARBARA

MOBILE HOME RENT CONTROL ORDINANCE

In re: NOMAD VILLAGE MOBILEHOME PARK,	**HOMEOWNERS' POST-HEARING OPENING BRIEF** Hearing Dates: September 19-20, 2011 Hearing Officer: Stephen Biersmith, Esq.

Petitioners, NOMAD VILLAGE MOBILE HOMEOWNERS (hereinafter "Home owners"), hereby submit the following post-hearing opening brief and legal points and authorities in support of their Petition filed herein.

I.

STATEMENT OF FACTS

Nomad Village is a 150-space mobilehome park located in an unincorporated area within the County of Santa Barbara (hereinafter "the County), and subject to the County of Santa Barbara Mobile Home Rent Control Ordinance (hereinafter "the Ordinance") found at Chapter 11A of the Santa Barbara County Code of Ordinances. All spaces within the park are covered by the Ordinance; none are subject to long-term leases which are exempt from rent control. Space rents in the park range from a low of $287.00 to a high of $430.00. The average space rent in the park is approximately $315.00, pending the outcome of this Petition. The noticed increase of

$161.00 plus 75% of CPI for the last three years will thus result in more than a 50% increase in rental cost for the average Homeowner, and for some shall be much larger.

The park land is owned by a family trust, but is leased to the park operator. For many years, possibly as many as 50, a ground lease apparently governed this relationship. When that lease expired in 2008, it was not renewed with the former park operator. The current operator, Lazy Landing, LLC (hereinafter the "Park Owner"), signed a new 34 year lease effective August 1, 2008, which includes a monthly ground lease amount negotiated at the time of purchase that calculates rent as a twenty (20%) percent of the gross rental income received by the Park Owner. Due to the expiration of the prior long-term lease, the County reassessed the local property tax due to a "change of ownership". Park Owner's Exhibit "G" confirms that notice of the reassessment was sent by the County and received by the Park Owner on May 26, 2009. County records indicate that the 2008 Supplemental taxes resulting from the reassessment were paid (apparently without protest) on December 10, 2009 and January 4, 2010. Testimony during the hearing confirmed that, to date, no actual assessment appeal has been filed by the Park Owner, although it is alleged that the Park Owner desires to do this, and can obtain the permission of the landowner in whose name the appeal would need to be prosecuted. It is undisputed that no annual rent adjustment, or rent increase of any kind, has been charged to residents since the current Park Owner assumed operations.

On January 26, 2011, Homeowners received a 90-day Notice of rent increase as required by law. Although it, and its attachments, are not a model of clarity, and tend to mix and match terms in such a way that it is confusing and difficult to decipher, it is apparent that three distinct rent amounts are being sought. These are set forth in Park Owner's Exhibit "C" as follows:

1. A CPI-based increase to existing base rent calculated based upon 75% of the CPI, which

Constitutes the annual adjustment which is allowed by the Ordinance without a hearing. A cumulative total of three years' worth of annual adjustment is included in the notice, since rent has not been increased for three years. This amount differs for each homeowner, but approximates $7-10.00 per month. Homeowners have stipulated at hearing that they are not challenging this specific portion of the increase.

2. An additional "permanent increase" to base rent in the amount of $58.16, which is derived from alleged increases in property taxes ($25.59 see Item 1) and ground lease payments ($32.57 see Item 2). Homeowners have objected to these amounts.

3. An additional "temporary increase" which is styled as a 7-year pass through in the amount of $102.84, which includes interest at 9%. This amount is based upon four pass through categories involving alleged capital expenses that are to be amortized over time, and not considered as ongoing operating expenses; i.e. (numbers taken from Exhibit "C" para.s:

Capital Improvements (Item 3)- for various costs already incurred ($90,000.00) and for costs to be incurred in the future ($370,000.00);

Uncompensated Increases (Item 4)- for the increased property taxes billed as a result of the reassessment and increased land lease costs that were paid for a 33 month period from August, 2008 through April, 2011 (i.e. prior to the effective date of the noticed rent increase) and are now sought pursuant to a theory described at hearing as "regulatory lag";

Anticipated Professional Fees (Property Taxes) (Item 5)- for estimated legal costs for pursuing an assessment appeal;

Anticipated Professional Fees (Rent Petition) (Item 6)- for estimated attorney's and expert fees to prosecute the instant administrative rent hearing and any forthcoming judicial proceedings.

Homeowners also object to these amounts.

Meet and confer sessions and an exchange of incomplete information ensued with authorized resident representatives, however no settlement or accord could be reached. Thus, Homeowners timely filed a Petition pursuant to Ordinance sec. 11A-5 (b), contesting the rent increase and requesting a hearing. The Petition was filed because the sum total of $161.00 which exceeds the three years' of cumulative CPI increases, far exceeds 75% of the CPI, and is thus reviewable under the Ordinance. The Ordinance does not require, nor do the County's "Mobilehome Rent Control Rules for Hearings" mandate, that any particular basis for the Petition be identified on its face. The County has verified that the Petition was indeed filed by a homeowner majority, and that it is valid.

II

THE PARK OWNER'S OBJECTIONS TO THE PETITION SHOULD BE OVERRULED

Homeowners desire to confirm their response and opposition to a pre-hearing Brief filed by the Park Owner which challenged the legality of the Petition. The Park Owner filed a response to the Homeowners' Petition which sets forth two objections to the Petition. Although not mentioned at the hearings, Homeowners position remains that each should be denied.

The first is rather confusing, but appears to allege that since the $161.00 sought in addition to the cumulative annual "75% of CPI adjustment" is not "rent", but has been labeled by the Park Owner as something else, it is not reviewable. In fact, a portion of the $161.00 is requested to be permanent, and thus cannot be anything but base rent in character. It will be charged monthly for the use of the mobilehome space, and clearly is part of the "noticed increase" as that phrase is used in Ordinance sec. 11A-5 (a), (b) and (d). Review by a hearing officer is not limited only to amounts which the Park Owner might choose to label as "base rent",

but applies also to a review of capital expenses or increased operating expenses which the park owner might attempt to capitalize and pass through to the residents as a "temporary increase". Support for this appears in Ordinance sec. 11A-5 (a) (3), which requires that such amounts be itemized in the notice of increase (which the Park Owner attempted to do), and again in sec.s (4)-(6) thereof, which allow the hearing officer to award amounts to cover increased costs of capital expenses, new or old, or capital improvements. Clearly the items which comprise the $161.00 are subject to review once a hearing is requested, as here. Otherwise, a Park Owner could "end run" the Ordinance by calling these increase amounts something else, and realize large increases in monthly rental charges without any review. It is the entire "increase" which must be measured, and here the $161.00 amount is required to be reviewed. Thus, this objection should be overruled. Since this issue was not raised at hearing, it was presumably waived.

Additionally, Park Owner appears to challenge whether the Petition was properly signed by a Homeowner majority. The process of verification is delegated to the County Clerk, who in this case has not rejected the Petition. Pursuant to Rule 4, the Petition is thus deemed verified. Absent evidence to the contrary, the Clerk's finding should control, and the objection be overruled. Should the hearing officer wish to subpoena the Clerk or review the actual Petition to verify signatures, Homeowners have no objection. But the word of the Clerk should control, and Homeowners should not be made to produce at hearing every resident who signed the Petition in order to verify same. By not raising the issue at hearing, the Park Owner appears to have conceded this issue.

III

THE PARK OWNER'S REQUEST FOR $58.14 IN "PERMANENT RENT INCREASES" IS EXCESSIVE

1. Ordinance Authority and the Applicability of the Maintenance of Net Operating Income (MNOI) Formula.

Contrary to the Park Owner's assertion that the Ordinance "provides for rent increases for increased Park operating expenses" in the dollar-for-dollar fashion which appears on Exhibit "C", the Ordinance does not specifically contain such authority. While the Hearing Officer is given ability in Ordinance sec. 11A-5 (i) to order an amount in excess of one-half of the automatic increase (i.e. 75% of CPI) to "cover operating expenses", that section goes on to state that the Hearing Officer has discretion "to add such amounts as are justified by the evidence..." Subsection (f) thereof describes a laundry list of factors to be considered (i.e. which "may" be included), and again refers to "all relevant factors". An alleged increase in one expenses category cannot be used to pass through that entire increase in a vacuum, dollar-for-dollar, without looking at <u>all</u> relevant factors. One such factor is the park owner's income. While an increase in an expense item is relevant, it should be considered in a broader context; i.e. within a fair return formula which takes into account all expenses and income of the park owner. A direct pass through of a specific expense item is not authorized by the Ordinance; the pass through of a capital item (of which property taxes and lease payments are not) is allowed (and shall be discussed below in connection with the "Temporary Increases" which are sought.

There is no precedent in Fair Return theory or analysis for the kind of passing through of an expense charge "in total" such as the Park Owner seeks here. The Park Owner's expert, Michael St. John, shows tacit agreement with this premise, since he employed with great care

parallel MNOI calculations referenced in Exhibit "D" which, although not specifically referenced in the Ordinance, are a well recognized fair return theory adopted by many ordinances and approved by the Courts. The Maintenance of Net Operating Income (MNOI) analysis has been praised by commentators for both its fairness and ease of administration, and was approved by a Court of Appeal in connection with a rent increase hearing in the City of Oceanside. *See Oceanside Mobilehome Park Owner's Assn. v. City of Oceanside (1984) 157 Cal. App. 3d 887.* In 1998, in a case involving application of Escondido's mobilehome ordinance (which, as with the case of this Ordinance, listed factors to be considered in a fair return case but did not identify a specific formula or methodology for calculating fair return), the court specifically upheld the use of an MNOI approach, calling it a "fairly constructed formula" which provides a "just and reasonable" return on investment. *See Rainbow Disposal v. Mobilehome Park Rental Review Board (1998) 64 Cal. App. 4th 1159.*

Ordinance sec. 11A-1 states that as an overriding purpose, the Ordinance is designed to ensure that a park owner receives "a fair return on their investment". An inquiry into fair return is thus appropriate. Any fair return analysis should be fairly used, and MNOI fits the bill. The fact that the park owner's own expert has chosen this theory to verify the reasonableness of the Park Owner's requested increase amounts establishes that it can and should be used by this Hearing Officer as an objective and court-tested standard by which the "reasonableness" of the requested rent increase can be determined. As stated below, the MNOI theory that the park owner has chosen, and which the Homeowners will accept as the standard to use, must, however, be properly applied. In that regard, Homeowners have several objections and contentions. But the overriding importance and use of the MNOI formula in concept cannot be understated, and Homeowners' position is this: In connection with the noticed $58.16 "permanent" rent increase,

the hearing officer should <u>not</u> consider each of the separate categories labeled as items 1 and 2 on a dollar-for-dollar basis, but instead should include these two expense categories (if appropriate) in a proper MNOI formula to establish a fair return, and thus a "reasonable" amount for the rent increase. Both Dr. St. John and Dr. Baar have testified at length about the efficacy and relevance of this formula, and have jointly validated its use here.

2. Specific Objections and Contentions Re: Park Owner's MNOI Calculations

A. <u>Property Tax Increase Expense</u>

Notwithstanding the foregoing, and the need to recognize this as but one expense which should be inputted into a proper MNOI formula, the expense amount claimed by the Park Owner should not be included in the MNOI calculation. The Exhibit "C" page 2 "Notes" attached to state in footnote "1" that the tax amounts shall not be "passed through" if a challenge to the assessment is successful (thus admitting that this increase is being attempted as a 'pass through' of a non-capital item, rather than included in a proper fair return formula). If there is any chance that the reassessment was improper, and the increased tax is not even legally owed, then the legality issue should be sorted out first via an assessment appeal, and no amount should be allowed until any legal challenge is completed (although it appears that the park owner has not yet even initiated any such challenge, and indeed stated that it is waiting for the Hearing Officer to award its projected attorney's fees <u>first</u> before it would do so!). Clearly the Park Owner's request in this regard is inconsistent. On the one hand, it seeks a "permanent increase" for a property tax increase which it alleges to be wrongful and will purportedly seek to overturn. If this were to occur, the Park Owner's own expert admitted that the rent increase stemming therefrom (i.e. $25.59 per month) would need to be terminated and any amount paid to date refunded. The complexity of this scenario, and the limited ability of individual Homeowners to

track the appeal process and enforce its results to ensure their refunds, highlights the unwieldy nature of the request. The hearing officer would, as part of any award, be forced to deal with this contingency, and would have to make this portion conditioned upon certain future events. But the Park Owner styles this amount as being "permanent". At the same time, the Park Owner seeks a $50,000.00 pass through to pay for the proposed appeal of the permanent tax increase. The Park Owner cannot have it both ways. Either the increase is "permanent" or it is not. Because of its contingent nature, and the possible error of the County in making the increased assessment, this item is premature, and should not be included in the MNOI calculation

B. Lease Payment Increase

As stated above, this item should also be treated as one expense amongst many which, if allowable, should be inputted into a proper MNOI formula. But this is clearly an expense which should not be included in Dr. St. John's analysis. The ground lease payment is not an operating expense, but rather an investment expense incurred by the Park Owner in connection with the acquisition of the park, the lease rights or whatever it acquired. It is a payment from one owner to another, made in connection with the purchased right to control the land. As such, it is a bargained for part of the purchase price, and not an expense. MNOI calculations would typically not allow such an item, since it is circular in nature (i.e. an increase in revenue increases the ground lease payment, which in turn requires an even greater increase in revenue, and so forth), and thus iterative. A park owner would have no incentive to negotiate a lower rent amount if it knew that the entire increases could be passed through to its tenants, and if the park land were someday purchased this amount would go away. Any increase in ground lease rent, which is thus capable of manipulation much like mortgage interest (which is

disallowed by the Ordinance) should not be considered as an operating expense when calculating fair return.

Homeowner's expert, Dr. Baar, has extensive experience in connection with the drafting and interpretation of mobilehome rent ordinances. He strongly opined that this category should be excluded for each of the above reasons. He testified that where a mobilehome rent ordinance allows such an expense, the ordinance specifically provides for such, and Exhibit "3" contains examples of ordinances which do include such a cost. Significantly, the Santa Barbara County Ordinance is silent on the subject. Dr. St. John testified that ground lease expense has been allowed "many times" but "not all of the time", and admitted that it is "relatively rare" that this sort of expense appears at all. He could not recall any specific cases in which he was involved where such an expense was allowed, or when it was not allowed, or where he ever gave an opinion that it should be allowed. Apparently this is the first case in which he has so testified. Absent any such experience, the testimony of Dr. Baar in this regard is more persuasive to disallow the ground lease expense.

Again, the circular nature of the ground lease rent formula means that ground rent will always be increasing, and the fact that it is calculated not as a fixed expense, but as a percentage of collected rents, means that it will also fluctuate from month to month. The Park Owner could agree to re-negotiate the amount in order to obtain concessions elsewhere from the land owner, with the knowledge that any increased amounts can simply be passed through to the Homeowners. If revenues decrease due to vacancies, the ground lease payment will decrease. And if the property were ever purchased it would go away completely. The presence of these contingencies and variables, and the resulting complexity required for building them into any

conditional award that the hearing officer might need to fashion, compels a finding that this expense must also be excluded.

Even if this expense item is accepted, the calculation is incorrect. According to the income and expense detail provided by the Park Owner in Exhibit , the actual paid lease amount in 2008 was $83,288.42, and not $54,905.00. Thus, the actual differential between 2008 and 2009 is $30,238.00. Together with the corrective calculation above, this yields a total difference between 2008 and 2009 for Permanent Increases of $68,293.68, which would result in a rent increase of $37.94 even if the Park Owner's 'stand alone' theory is accepted.

3. Proper Application of the St. John MNOI Analysis

As previously stated, Homeowners do not object to the use of the MNOI formula, and are willing to accept it as the best fair return formula to be used in this case. But it must be properly and accurately applied. The Park Owner's expert has presented an MNOI analysis which is alleged to be a "supporting" or "verifying" calculation for the $58.16 "permanent" increase. Dr. St. John has conducted parallel MNOI calculations in Exhibit "D", which find as follows:

Comparing a 1994 Base Year to a 2010 Current Year:

-Indexing at 75%, the increase would be $44.30.

-Indexing at 100%, the increase would be $57.04.

Comparing a 2007 Base Year to a 2010 Current Year:

-Indexing at 75%, the increase would be $55.53.

-Indexing at 100%, the increase would be $57.09.

Of course these calculations include both items 1 and 2 from above as permissible expenses.

There are too many combinations that could result from the above for Homeowners to calculate every conceivable scenario that could result; the final MNOI number will depend upon a number of factors:

Which Base Year should be used? Dr. St. John admitted that it was "kind of a toss up" as to whether 1994 or 2007 should be used, and admitted that his first choice was 1994 based upon the most historical documentation then available. He only employed the "side-by-side" use of the 2007 calculation after reading Homeowners' pre-hearing brief. Based upon the testimony of Dr. Baar, Dr. St. John's first instinct would appear to be the more correct one. Dr. Baar recalled how in prior matters in which he has viewed Dr. St. John's testimony, he has always taken the position that the base year should precede the adoption date of the ordinance. Since 1994 is the oldest available data, it would follow that 1994 should become the base year for purposes of this hearing. Dr. Baar agreed with this.

What indexing should be used? Both experts agreed that it is common for ordinances to provide for indexing at 75% of CPI when employing an MNOI analysis. Exhibit 2 evidences this to be true. Because the Santa Barbara ordinance indexes the annual adjustment at 75% of CPI, it follows that a 75% index should be used when applying MNOI.

Thus, the most accurate MNOI application is the one calculated using a base year of 1994 @ 75% indexing; i.e. $44.30 according to page 4 of Table 3-B in Exhibit D. This needs to be compared to the $58.16 increase sought based upon the stand alone "dollar-for-dollar" calculation, which is thus not an accurate fair return number. MNOI application establishes the unreasonableness of the $58.16 amount, even before any expense items are deducted.

From this $44.30 amount, certain expense adjustments must also be made:

-When the property tax expense is removed (see above), the MNOI result is near zero.

-When the ground lease expense is removed (se above), the MNOI result is near zero.

-Dr. St. John admitted during the hearing that a $2,500.00 expense item for Franchise Taxes was pre-paid for 2011, and thus should be deducted from the 2010 expenses. This results in an undisputed $1.39 deduction from the $44.30 figure above, even if all other expenses remain included.

-Dr. St. John also identified a $4,500.00 late charge that was incurred in connection with a bank payment. Although he felt that this expense should still be included, it is clear that it should not be, since it is a one-time, non-recurring expense which was within the Park Owner's power to avoid. Deducting this amount from the $44.30 figure, even if all other expenses remain included, results in a further $2.51 reduction.

Thus, even if expense items 1 and 2 are included, the correct MNOI total would be $40.40. This is the largest possible permanent rent increase that should be awarded, subject to further reduction for the exclusion of property tax and/or ground lease expense. (Homeowners will not perform those calculations here, but reserve the right to do so in their closing brief.)

IV

THE PARK OWNER'S ATTEMPT TO PASS THROUGH $102.84 IN "TEMPORARY INCREASES" SHOULD BE DENIED IN ITS ENTIRETY

Homeowners object to the increase amounts labeled as "Temporary Increases" in the Park Owner's increase summary sheet (Items labeled as 3 through 6) based upon the following:

1. General Objections and Observations

Each of the items described in this section is sought as a "pass through"; i.e. the amount

requested is designed to be amortized over a seven (7) years, at nine (9) percent interest, to reimburse the Park Owner for the cost of the item. This constitutes treatment of each as a capital item, rather than a deductible expense. But to be treated as a capital item, in this case for the most part where payment is sought before the expenses have actually been incurred, the following must be true:

-The improvement or repair for which the increase is sought must be specifically identified, so as to confirm that it is indeed a capital item, as opposed to a deductible expense.

-Ordinance definitions of a "capital improvement" and a "capital expense" must be met in order to authorize the increase; i.e. the "addition or betterment" must be identified, or the "existing facilities or improvements" for which the expected repair or replacement adds an expected life of at least one year. Until the specific work is identified by type and cost, these definitions, found in Ordinance sec. 11A-2, cannot be established.

-"Anticipated Professional Fees", including legal fees, which are claimed as capital items in items 3, 5 and 6 need to be specifically explained and accounted for, as well as supported by good faith estimates or billings incurred. Such items are not considered as capital expenditures, and thus cannot be amortized and passed through, where their inclusion would violate Internal Revenue Service precedent. In Revenue Ruling 78-389 (1978-2 Cum. Bull. 125), the Service found that legal expenses incurred in the prosecution of a suit to invalidate as municipal ordinance that would prohibit the operation of a taxpayer's business were deductible as ordinary and necessary business expenses when they arose from the taxpayer's business activities and did not result in the acquisition or disposition of a capital asset. Thus, in general, these sought after "professional fees" cannot be treated as capital items. Park Owner's expert admits that he has treated each such fee request the same as a capital item, based upon his belief that the Ordinance

authorizes him to do so by analogy. But there is no precedent or authority stated for this, whether from the Ordinance language or elsewhere. These are clearly non-capital in nature, and regardless of their amount should not be allowed.

The manner of amortizing each of the principal amounts, together with interest at 9%, over 7 years is the product of an estimate made by Dr. St. John. However he testified at length during the hearing about the hardship upon the residents that a shorter amortization period could create, and stated that he would have "no objection to a 15-year amortization". In this regard, in the event that any of the "temporary" increase amounts are allowed, it is submitted that the hearing officer should construct a parallel calculation which amortizes the amount at both 7 and 15 years, so that each resident can choose the option that best suits their financial capabilities. This is particularly appropriate when amortizing road repair expenses, which are typically amortized over a longer period of time.

2. Specific Objections and Challenges

Item 3: Capital Improvements

Item 3 of Exhibit 3 is labeled as "capital improvements", which means that the definition found in Ordinance sec. 11A-2 (a) must be established. It is unclear how or why $50,000.00 of "professional fees" would be required in connection with any proposed capital improvement, especially since architectural and engineering costs have already been broken out separately. Nor should they be allowed based upon the IRS authority cited above. This amount should therefore be disallowed.

With respect to the claimed $90,000.00 of "A & E" fees already incurred, the actual amount would appear to be $62,145.55 as verified by Exhibit "J". Expense items listed on

Exhibit "J" which were incurred by the previous park operator, Nomad Village, Inc., are not subject to reimbursement to the current.

In addition, any portion of this remaining amount that relates to repairs, maintenance, upgrades or replacement of the sub-metered gas or electric system may not be passed through to Homeowners, pursuant to the authority of the case of *Rainbow Disposal Company, Inc. v. Escondido Mobilehome Rent Review Board 64 Cal. App. 4th 1159 (1998)* marked as Exhibit "4" during the hearing. In that case, a $200,000.00 amount was disallowed, based upon the authority of a 1995 Public Utilities Commission Ruling (*Re: Rates, Charges, and Practices of Electric and Gas Utilities Providing Services to Master-metered Mobile Home Parks (1995) 58 Cal. P.U.C. 2d 709)*. In that decision, the Commission found that the sub-metered discount received by park owners each month to compensate them for operating sub-metered systems includes "among other things, a factor for investment-related expenses for all initial and ongoing capital upgrade costs, and return on investment." During the hearing, Dr. St. John opined that costs related to system upgrades should not be disallowed, since the discount in his opinion only covers repairs or maintenance. Dr. St. John's resume gives no indication that he has any expertise in utility matters, or that he has consulted in connection therewith. In fact, he admitted that, consistent with the *Rainbow* decision, all income and expenses related to sub-metered utility systems are typically excluded from an MNOI calculation. Clearly his opinion is directly contrary to both California caselaw and Commission decision. Since expenses related to electric system upgrades cannot be charged in a rent control jurisdiction, and such expenses found in this category must also be excluded. Other than the first three entries which appear on Exhibit "J" relating to fence repairs, and the sewer repair cost, all other expenses listed appear to bear some relationship to electrical system upgrades, including the $20,760.00 paid to Cusac Construction. For the above-

stated reasons, they cannot be passed through to Homeowners, and must be deleted from this category. The total pass through amount appears to be $22,192.50 for "A & E Fees" already incurred.

The $320,000.00 amount listed for future "Infrastructure" amounts is not identified. In fact, the Park Owner testified that they were not yet sure what they were going to spend this amount on. Until verifiable items are identified, so as to be confirmed as capital items that will benefit the Homeowners, nothing can be passed through. Otherwise, there is no way for Homeowners to verify if the designated work is being timely performed. As well, Exhibit M identifies an estimate for $270,945.00 to upgrade the electrical system, which cannot be passed through pursuant to the authority stated above. The Park Owner testified that this work would be done first, before any street repairs could be accomplished. Since it is unlikely that both could be completed within 6 months, with the rainy season fast approaching, and the $320,000 amount does not match any of the larger street repair estimates submitted as a part of Exhibit "M", this entire, unquantified and vague amount must be denied. At minimum, it is premature.

<u>Item 4: Regulatory Lag Amounts</u>

This can only be described as a very creative category, and suffers from some of the same infirmities as Items 1 and 2. For if a property tax appeal is successful, and the amounts previously paid to the County are refunded, a commensurate refund would be due to Homeowners. And is ground lease expenses are disallowed for the reasons set forth above, they cannot be allowed to be charged here.

But the biggest problem with this category goes to its basic concept. Dr. St. John admitted that he could cite no specific precedent for going back in time some 33 months (33 is

the correct total, not 34) to recapture expenses that the Park Owner never elected to bill to the residents sooner. The result is unfair; i.e. residents are hit with a cumulative sum all at once, now including interest, of which they had no prior knowledge. Dr. Baar testified that no more than 12 months of this "lag" should be charged to the Homeowners.

If any amount is charged, then it must be based on 33 months instead of 34, resulting in a .75 cent reduction from the $32.74 amount being sought. The calculation presented for this item 4 incorrectly counts for 34 months, when instead the number of months from August, 2008, when Park Owner acquired the lease rights, through April, 2011 (i.e. the last month before the requested increase would take effect) is 33 months.

This category attempts to pass through retroactively, supplemental tax and land lease allegedly incurred in 2008 and 2009, and for which the park owner chose not to previously seek any increase during those years. There is no precedent in the Ordinance for such a theory, which if allowed would enable a park owner to go back in time any number of years to allege that an expense increase, or one-time payment of some type, had not been fully compensated. These are not capital items, and are subject to the same analysis set forth in Headnote III above. These amounts are compensated as a part of the three years of automatic CPI increases which will be allowed by the Hearing Officer. They were never noticed when incurred, and recovery was never sought when the expense was incurred. To allow them now would create a precedent for retroactive recovery which would make such expenses difficult to track or prove, and which would keep Homeowners at risk of having to pay rent increases to cover new expense item whenever discovered, or whenever the park owner might get around to requesting them. This would also create chaos and play havoc with prior increases ordered based upon facts and data

then presented, which could be turned on its head by new "expenses" claimed in later years for the same periods.

Item 5: Anticipated Professional Fees – Property Taxes

This is clearly not a capital item, since it does not relate to the acquisition or disposition of a capital asset, and because it is prospective as per its definition it has not yet become an expense of the Park Owner. If actually incurred, the Park Owner is free to include this amount in a future rent notice, where it can be properly analyzed and adjudicated under the Ordinance. Furthermore, no basis for the expense has been disclosed; i.e. it is unknown who the fees would be paid to, what they would seek to accomplish and what good faith basis, if any, exists for achieving any benefit to the Homeowners. The fact that the Park Owner has not, to date, initiated any such challenge speaks volumes about the confidence level in such a pursuit, and how Homeowners would in any way be "bettered" by such a cost. Homeowners cannot be expected to fund what could turn out to be fruitless legal challenges, and provide the Park Owner with the equivalent of an attorney's fee guarantee, even if the Park Owner were to lose.

During hearing, the park owner admitted that to date, no actual steps have been undertaken in furtherance of the appeal. According to the website maintained by the County of Santa Barbara, which has posted the Rules of the Assessment Appeals Board, any appeal must be filed no later than November 30th of the current year for "regular" assessments, and within 60 days after notification for "supplemental" assessments. Because Exhibit "G" confirms notification to the Park Owner on May 20, 2009, and the Park's records show the supplemental taxes paid in full by early 2010, the time for filing any appeal would appear to be long gone. As such, this category cannot be allowed.

Item 6: Anticipated Professional Fees – Rent Increase

This category still represents a complete unknown at this point. But it can be inferred, due to the huge amount projected that it encompasses not only the legal fees require for this 2 day hearing, but also fees to fund a projected appeal through the courts if the Park Owner were to lose all or any portion of its case at the administrative level, as well as for any remanded hearings. For that reason, all of the same arguments set forth in item 5 above would apply to this item. Any fees incurred for appeals or remand can be awarded on remand. But they cannot be claimed before any such expenses are incurred, as they are not capital items capable of being monitored during the six-month period described in the Ordinance. Treating this item the same as a capital item by analogy simply does not work.

During his testimony, Dr. St. John could not estimate what fees he would charge through the hearing process. Nor were any other billings entered into evidence to support attorney's fees (Counsel for Park Owner has agreed to provide same with his opening brief). This is still thus an unknown, for which Homeowners will reserve comment in their closing brief. But Dr. Baar testified very clearly that $125,000.00 was a hugely excessive amount for fees in a hearing such as this, and Exhibit 5 shows that fees of less than $50,000.00 would be routine in a hearing such as this. Homeowners reserve the right to argue this item further once counsel's actual, itemized fees are received.

V

CONCLUSION

Only the CPI portion of the increase is deemed "automatic" based upon evidence or authority presented thus far by the park owner. All other portions of the requested increase; i.e. the $161.00 amount, must be reviewed by the Hearing Officer before they can become an

ongoing part of the monthly rental cost, whether as base rent or a pass through. Homeowners objections to the amounts sought are based not only upon methodology, but also upon errors and inconsistencies in the calculations themselves. Homeowners cannot at this point even begin to calculate all of the different amounts which might be awarded if only certain mistakes are corrected or certain re-calculations are made. But they need not do so in any case, for the bottom line is this: If the mutually accepted MNOI formula is properly applied, with the ground lease or property tax cost extracted, the amount to be granted for the "permanent" base year rent increase above and beyond what is automatically allowed is "zero". And if the "temporary increases" are confined to legitimate capital items which have been properly identified and estimated by reasonable cost, then the allowable amount of any such pass throughs is also at or near "zero".

For these reasons, and reserving the right to make additional arguments in their closing brief, Homeowners respectfully request that the Petition be granted and the $161.00 requested increase be denied.

Dated: October 19, 2011

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