REPORT OF THE
CHIEF LEGISLATIVE ANALYST

DATE: July 18, 2022

TO: Honorable Members of the City Council

FROM: Sharon M. Tso KEK for
Chief Legislative Analyst

Council File No. 21-1244
Assignment No. 21-12-0935

SUBJECT: Real Estate Speculation by Large Tech and Private Equity Firms

SUMMARY
On November 12, 2021, the City Council adopted instructions related to Motion (Martinez – Raman, C. F. 21-1244) to address real estate speculation by private equity firms and tech companies that has affected housing affordability across the nation and has resulted in the displacement of long-term residents in the City (Attachment A). Council instructed the Chief Legislative Analyst (CLA) and the City Attorney to report on strategies the City can use to prevent large tech and private equity firms from engaging in speculative practices that involve purchasing affordable single family housing in the City.

In response, our Office reviewed news reports, research, programmatic proposals in other jurisdictions, and past City policy proposals, and consulted with the City Attorney to consider: (1) expansion of homebuyer assistance programs offered by the City; (2) legislation that prevents the displacement of long-term residents; (3) legislation that limits real estate speculation by private equity firms and investment vehicles; and (4) past and current Council efforts that address housing affordability, displacement of residents, and corporate ownership of residential real estate.

RECOMMENDATIONS
That the City Council:

1. Instruct the Los Angeles Housing Department (LAHD) to report on the feasibility of developing home ownership education and counseling programs or contracting with educators to offer home ownership education and counseling programs for prospective homebuyers and current home owners in the City;

2. Instruct LAHD to report on the feasibility of applying for CalHome grants from the California Department of Housing and Community Development (HCD) to fund first-time homebuyer and housing rehabilitation assistance, homebuyer counseling, and technical assistance activities to support home ownership, especially for low- and very-low-income individuals and households;

3. Instruct LAHD to review Los Angeles County Assessor property rolls and report on an estimate of the number of single family homes owned by investment vehicles including real estate investment trusts (REITs), partnerships, corporations, and limited liability entities in the City, including as a proportion of total units, as well as possible policy responses to limit the amount of properties that is permissible for a single entity to own;

4. Instruct LAHD, in consultation with the Department of Building and Safety, to report on the implementation of SB 1079 to prohibit real estate trustees from bundling foreclosed properties for sale;

5. Instruct the CLA, with the assistance of LAHD, to report on how opportunity to purchase policies impact property sale timelines and property values, and their overall effectiveness in preventing the displacement of long-term residents;

6. Adopt the attached Resolution to support Senate Bill (SB) 649 in its 2021-22 State Legislative Program to authorize local governments to allow a local tenant preference in affordable housing that is acquired, constructed, preserved, or funded with State or local funds or tax programs; and

7. Adopt the attached Resolution to support Assembly Bill (AB) 1771, the California Housing Speculation Act, in its 2021-22 State Legislative Program for an additional 25 percent tax on the portion of capital gain from the sale or exchange of residential properties in California within three years of the purchase of the property.

BACKGROUND

Housing affordability has been a significant piece of the national housing crisis, especially in the State of California. In March 2022, Los Angeles home prices were up 14.6 percent compared to the previous year, with homes selling for a median price of $1 million. Low housing inventory and high demand for homes have resulted in bidding wars that have increased home prices even further, despite rising interest rates, inflation, and record high housing prices. Increasing home prices drive up rents, displace residents who are priced out of their neighborhoods, and make it significantly more difficult for prospective first-time homebuyers who do not have equity gains from previous property ownership to leverage funds to purchase property in the City.

Home prices increase for a multitude of reasons, including a strong economy, high demand for homes, low housing supply, low interest rates, area desirability, as well as local and global politics. The quick buying and 'flipping' of properties, especially in high demand markets like Los Angeles, has also contributed to increasing home prices. Flipping is a strategy of "distressed property investment" in which buyers purchase properties rapidly and sell them in relatively similar condition, perhaps with cosmetic repairs, to incoming residents or other landlords, profiting from a speculative bet on increased property values or from the exploitation of low-information buyers.[1]

In competitive housing markets like Los Angeles, prospective owner-occupants, or people who plan to purchase a home to reside in it, increasingly compete with real estate and corporate investors or entities that purchase properties primarily for investment, to purchase homes. When homes are sold to investors to be converted into rentals or left vacant for speculation, prospective homeowners and "mom and pop" landlords are crowded out of the market and communities suffer, particularly communities of color. Recent studies suggest that corporate ownership of residential properties is associated with higher rates of eviction and foreclosure than individual ownership, high rent increases, excessive fees, unethical management practices, and the removal of thousands of units a year from the market. Long-term residents who can no longer afford rising rents or housing prices leave their neighborhoods and communities in search of more affordable housing.

[1] Ferrer, Alexander. "Beyond Wall Street Landlords: How Private Equity in the Rental Market Makes Housing Unaffordable, Unstable, and Unhealthy." *The Just Recovery Series*. Strategic Actions for a Just Economy, 2021, https://www.saje.net/wp-content/uploads/2021/03/Final_A-Just-Recovery-Series_Beyond_Wall_Street.pdf. Accessed 22 Mar. 2022.

Over the last few decades, there has been a trend of consolidation of housing ownership into the hands of corporate entities and investment vehicles, and out of the hands of individual owners, that has been driven by financial deregulation, policy shifts, tax incentives, as well as the recovery from the 2008 subprime mortgage crisis. In 2021, investors purchased nearly one in seven homes sold in America's top metropolitan areas, the highest share of U.S. homes in at least two decades. In Los Angeles County, investors purchased ten percent of homes in 2021.

In recent years, real estate speculation has been facilitated by 'instant buying,' also known as iBuying, a streamlined process that uses data, algorithms, and technology to simplify the home selling and buying process, with most of the transaction occurring online. iBuying allows sellers to circumvent the conventional process of listing a property with a real estate professional, advertising the property, and waiting for a buyer, and allows deals to close much quicker. Sellers can also avoid paying commissions to real estate agents by selling to an iBuyer directly for cash offers.

Companies who use this transaction model, known as 'instant buyers' (iBuyers), have expanded rapidly since they entered the market in 2014, with increased funding from global investors. During the COVID-19 pandemic, buyers and sellers both reaped the benefits of iBuying: quick, online home inspections; virtual home showings through high-definition photos and videos; cash offers for homes; and the ability to close deals in the matter of a few days. As a result, iBuyer activity in 2021 doubled from pre-pandemic levels.

While iBuyers offer a pared down home buying process, they ultimately operate as industrial-scale real estate 'flippers,' as they are looking to quickly buy and resell homes for a profit. iBuyers have also facilitated the concentration of corporate ownership of homes by selling homes in bulk to other large investors. The share of iBuyer purchases resold to investors increased from five percent at the beginning of 2019 to 22 percent by the end of that year. Resales to large investors surged to 38 percent at the onset of the pandemic in 2020, as iBuyers looked to reduce their risks amid market uncertainty and widespread lock downs.

iBuyers make up only a small part of the real estate market and do not operate everywhere in the U.S., since they work best in areas with high real estate turnover such as metro areas. iBuyers purchased approximately 70,402 homes in 2021, which was just over one percent of all homes purchased in the U.S. last year. The top five states that comprised 75 percent of overall iBuyer purchases since 2017 include Texas, Arizona, Florida, Georgia, and North Carolina. While these five states generally ranked in the top five since 2017, a ramp up of activity in California in 2021 brought the State into the top five, replacing North Carolina. Home sales from iBuyers accounted for 1.2 percent of total home sales in Los Angeles and Orange counties during the second quarter of 2021.

CHALLENGES AND CONSIDERATIONS

Currently, there is not sufficient data to show whether iBuying has significantly driven up single family home prices or increased real estate speculation in the City. However, our Office recognizes the intent of the Motion to address housing affordability, the displacement of long-term residents who are priced out of their neighborhoods, and the concentration of home ownership by corporations and real estate investors. Our Office recommends that Council explore policies that support owner-occupied home ownership, especially among vulnerable renters who are at risk of displacement, and limit corporate and investor real estate speculation in the City.

Legal and Regulatory Challenges

iBuyers have experienced various legal and regulatory challenges in recent years. In November 2021, Zillow Offers, the iBuying arm of Zillow Group that launched in April 2018 and the largest iBuyer in the market at the time, announced that they would be leaving the iBuying realm due to $420 million in reported losses earlier in the year. That decision followed an October 2021 company announcement that Zillow Offers would lay off 25 percent of its employees and would not buy any additional homes through the end of 2021.

In January 2022, a class action federal securities lawsuit was filed against Zillow Offers, claiming that Zillow failed to disclose to investors that they did not have the ability to accurately price homes and that pandemic-related supply and labor shortages led to an inventory backlog in late 2021. The suit seeks to certify a class of Zillow stockholders who purchased stocks from August 2020 to November 2021. It was also reported that Zillow Offers was overpaying sellers for properties to buy the market share of properties away from Opendoor, its largest competitor, and was unable to recover those expenses by reselling the properties due to volatile housing markets.

iBuyers have also faced challenges for inaccurate and incomplete property listings. In March 2022, the North Carolina Real Estate Commission (NCREC) suspended Opendoor's brokerage license over several disclosure issues on homes that were listed for sale, including failures to correct inaccurate listings and display required fair housing language and broker license numbers on property listings. The suspension was contemporaneously stayed the same day, once Opendoor agreed to institute new company policies and require brokers to attend remedial courses offered by NCREC, which allowed Opendoor to continue its license and operations in the state.

Analysts argue that iBuying is an inherently risky and largely untested business model that carries low margins and requires high debt to finance transactions. Despite these risks, iBuying is continuing to grow and expand into new markets. Offerpad and Opendoor are the largest iBuying companies based on transaction volume and are the only U.S. publicly traded companies whose majority revenue and expenses come from home flipping. Offerpad reported a $41 million net income for the first quarter of 2022, up more than 250 percent from this time last year.

STRATEGIES

Motion (Martinez – Raman, C.F. 21-1244) focuses on three main issues that are exacerbated by iBuying and real estate speculation: 1) housing affordability, 2) the displacement of long-term residents, and 3) corporate and investor ownership of housing in the City. These issues arise because real estate speculation and investment contributes to driving up home prices, increases housing scarcity by removing properties from the market, and competes with owner-occupants for home ownership.

To address these issues, this Office recommends that the City implement a multi-faceted approach by: 1) expanding and enhancing its homebuyer programs, 2) conducting additional research to establish an effective opportunity to purchase policy, 3), supporting legislation or administrative action to establish local tenant preference policies in the State, and 4) supporting legislation or administrative action to limit single family home ownership by REITs, partnerships, corporations, and limited liability entities in the City.

A. Housing Affordability

Most California households are currently priced out of home ownership in the State because of affordability. According to a report from the California State Treasurer's Office, the average price paid by a first-time homebuyer in California in 2021 was $712,040. Only 26 percent of households and 17 percent of Latino and Black households in the State are able to afford that price. It is in the State and City's best interest to address its housing affordability challenges, as home ownership is a key element for families to secure housing and economic security, build intergenerational wealth, and create stronger communities.

The City has supported multiple programs to assist homebuyers in the City with loan assistance and tax incentive programs, and continues to monitor legislation to address housing affordability issues. On February 23, 2022, Council adopted Motion (Martinez – de León, O'Farrell, C.F. 22-0038) to direct LAHD to report on an assessment of the financial need among low- and moderate-income potential homebuyers in Los Angeles, and provide recommendations on the resources needed to expand the City's first-time homebuyer programs and meaningfully increase the number of loans and financing options. The LAHD report is pending.

According to the U.S. Department of Housing and Urban Development's Office of Policy Development and Research, home ownership education and counseling, in addition to home loan assistance and tax incentive programs, can substantially improve prospective and current homeowners' comprehension of their choices, financial decision-making, and ability to address issues that arise with their homes or finances. Home ownership counseling and education can help participants lower their housing costs, save more income, improve their credit, avoid delinquency, address defaults, and avoid foreclosure. LAHD currently does not offer home ownership counseling and education programs, but this Office recommends that the City expand its homebuyer programs to include education and counseling to provide timely, powerful assistance to prospective and current homeowners and continue to support owner-occupant property ownership in Los Angeles.

Los Angeles Homebuyer Assistance Programs

LAHD currently offers three programs that assist homebuyers with housing affordability: Low Income Purchase Assistance (LIPA), Moderate Income Purchase Assistance (MIPA), and the Mortgage Credit Certificate (MCC).

The LIPA program helps first-time, low-income homebuyers purchase homes in the City by providing loans for down payment, closing, and acquisition costs. The MIPA program also provides loans of up to $75,000 for down payment, closing, and acquisition costs, but is not limited to first-time homebuyers. The MCC program provides a dollar-for-dollar reduction to a homebuyer's potential federal income tax liability and increases the household income available to qualify for a home mortgage. Program eligibility for all three programs depends on household income.

The County of Los Angeles also offers housing affordability assistance through the Home Ownership Program (HOP) and Affordable Homeownership Opportunities Program (AHOP) for first-time homebuyers. HOP provides a zero percent second mortgage loan for up to $85,000, or 20 percent of the property purchase price, whichever is less, with a deferred payment. Repayment is required when the home is sold, there is a transfer of title, or the home is no longer owner-occupied. To qualify, a homebuyer must not have owned a home in the last three years, must not exceed 80 percent of the County median income, and the home must be owner-occupied.

AHOP provides first-time homebuyer down payment assistance to low- and moderate-income households. The homebuyer must meet the credit underwriting criteria established by the lender providing the first mortgage loan, as well as underwriting for the Los Angeles County Development Authority (LACDA). The LACDA provides financial assistance via a secondary mortgage, with all payments deferred until sale, transfer, or refinancing. As a result, the LACDA shares in a percentage of the equity accumulated on the property, depending upon circumstances that exist at the time of subsequent sale, transfer, or refinancing.

State Homebuyer and Homeowner Assistance Programs

Significant efforts are also being made at the State level to address housing affordability. On June 30, 2022, Governor Newsom approved a $308 billion State budget for the 2022-23 fiscal year that includes $850 million in new, one-time funds for home ownership assistance for very-low, low-, and moderate-income individuals through the 'California Dream for All' and CalHome programs.

The 'California Dream for All' program offers first-time homebuyers making up to 150 percent of their Area Median Income with a second mortgage that covers 17 to 20 percent of the purchase price of a home, as well as extensive mortgage counseling. The State is reimbursed the loan when the homebuyer refinances or sells the home. Unlike other programs, the California Dream for All program does not include price limits on purchases, which would allow homebuyers in more expensive regions like Los Angeles and San Francisco to benefit from the program and remain in their neighborhoods. The 2022-2023 state budget allocated $500 million to the California Housing Finance Agency (CalFHA) for the program's inaugural year, to begin in 2023. CalFHA also continues to offer government and conventional deferred-payment junior loans for down payment and/or closing cost assistance through the MyHome Assistance Program to first-time homebuyers who meet income eligibility limits.

The CalHome program provides grants to local public agencies and nonprofit corporations for first-time homebuyer and housing rehabilitation assistance, homebuyer counseling, and technical assistance activities to enable low- and very-low-income individuals to become or remain homeowners. The program is administered by the California Department of Housing and Community Development (HCD) and was allocated $250 million for 2022-23 and $100 million for 2023-24. In previous years, HCD has released Notices of Funding Availability (NOFAs) to announce annual funding amounts, eligibility, and distribution.

This Office recommends that LAHD report on the feasibility of applying for CalHome grants from HCD when the 2022 NOFA is released to fund the expansion the City's first-time homebuyer programs to include home ownership education and counseling programs.

B. Displacement of Long-Term Residents

Several cities in the U.S. such as New York, San Francisco, and Washington, D.C. have established purchase opportunity and community preference policies to address the displacement of long-term residents in areas that experience gentrification, redevelopment, or a housing shortage. These policies have existed in the United States since the 1980s with New York instituting the first such law. Community preference and local purchase opportunity policies prevent displacement by giving current residents preference, or a "right of first refusal" for new affordable housing in their neighborhoods. Supporters say that community preference policies are a crucial way to fight displacement, but housing advocates argue that these policies are exclusionary and violate fair housing laws.

The City first considered a purchase opportunity policy in 2007 (C.F. 07-3291) based on the District of Columbia's implementation of the Tenant Opportunity to Purchase Act to address a severe rental housing shortage. More recently, Council actions (C.F.s 18-0159, 19-1127, 22-0372) have supported community preference or "right of first refusal" policies that prevent the displacement of long-term residents in areas experiencing gentrification or undergoing redevelopment in Los Angeles. More specifically, a right of first refusal allows designated entities to acquire property by matching an existing offer, and may also require an owner to provide an offer of sale to designated entities whenever a sale is proposed to another party. These kinds of purchase opportunity policies aim to preserve affordable housing, prevent displacement, and create home ownership opportunities.

There are a number of local purchase opportunity laws in the State, which vary based on the type of purchase opportunity provided (e.g., rights of first refusal, rights of offer, or rights to purchase) and the kinds of entities that are eligible to participate. California law currently provides public agencies, non-profit organizations, for-profit purchasers, and tenant associations the opportunity to purchase federally- or locally-funded housing developments with expiring affordability covenants, provided that the entities will continue the developments' low-income use (CA Government Code 65863.11). Purchase opportunity rights are also provided when land-use concessions are granted pursuant to State density bonus law. (Id.) In addition, tenants also have an exclusive right to contract for the purchase of their apartment units when a condominium conversion is requested. (e.g., Cal. Government Code Section 66427.1, LAMC Section 12.95.2).

On April 13, 2018, Council adopted Motion (Harris-Dawson, Wesson, Price – Bonin, et. al, C.F. 18-0159) to instruct the CLA, LAHD, and Economic and Workforce Development Department, in consultation with the City Attorney and Department of City Planning, to report on: 1) how residents, businesses, and organizations may be considered eligible for targeted affordable housing and business stabilization policies, similar to San Francisco's Neighborhood Resident Housing Preference, and 2) the feasibility of a neighborhood stabilization program, and the steps required to establish such a program. The report is pending.

On May 6, 2022, Council adopted Motion (Buscaino – Price, C.F. 22-0372) to request that the Housing Authority of the City of Los Angeles (HACLA) adopt a policy similar to San Francisco's Neighborhood Resident Housing Preference for the Watts community, as defined by the boundaries of the Watts Neighborhood Council, to prevent the displacement of vulnerable residents amid the redevelopment of the Jordan Downs public housing. The HACLA report is pending.

Opportunity to Purchase and Neighborhood Preference Programs

District of Columbia – In 2007, the City considered establishing a "right of first refusal" policy to prevent the displacement of long-term tenants, especially in instances where owners of affordable housing properties were planning to sell their building(s) or convert them to condominiums. On December 5, 2007, Council directed the CLA to review the District of Columbia's Tenant Opportunity to Purchase Act (TOPA) program and report on how such an approach could be implemented in Los Angeles (C.F. 07-3291). On June 20, 2008, Council adopted the Motion, as amended, and approved the formation of a Task Force to study how the TOPA Program could work in the City of Los Angeles, and how to implement the program. No information or actions from the TOPA Task Force were available for review.

The TOPA was enacted in Washington, D.C. in 1980 to address a housing crisis characterized by a severe shortage of rental housing, which included nearly 60,000 households in need of housing assistance, a loss of rental housing due to condominium conversions that impacted low-income and elderly tenants, and new conversion controls to preserve affordable housing. The TOPA requires owners of rental occupied units to offer tenants the right of first refusal when they decide to sell the building. Owners are required to notify tenants and the Mayor's Office of the opportunity to purchase, which initiates a process that provides tenants time to organize, raise funds, and solicit outside assistance. In addition, the TOPA provides tenants and tenant organizations the ability to sell their rights for payment or partner with a developer or non-profit in the purchase of the building. In 2018, new legislation was enacted that exempted single family dwellings from the TOPA, including homes, condos, Accessory Dwelling Units, and co-ops, unless occupied by elderly or disabled tenants, showing that the ordinance is not as expansive as it was at its inception.

A study examining the TOPA program found that it has effectively helped some tenants purchase their units. From 2011-2021, the program helped preserve nearly 1,400 units of affordable housing. In one case, the TOPA prevented the eviction of 26 families on one street, leading researchers to conclude that it provides a necessary legal opportunity structure for community organizations to fight redlining and gentrification. However, while the TOPA can be an effective way to keep tenants in their homes, the complexity of the process may affect how many people are able to access this resource. In addition, tenants who can afford to buy their homes at the time of sale are typically not in the lowest-income groups, signaling that TOPA laws may not protect the most vulnerable renters. Furthermore, such programs require significant financial resources from municipalities and are likely unable to serve households at the lowest income levels.

Considerations

In 2020, the city of Berkeley considered establishing a TOPA ordinance, but faced strong opposition from community organizations, property owners, and real estate groups who argued that the policy would delay property sale timelines and would not be effective in preserving affordable housing. In response, Berkeley Mayor Jesse Arreguín made several amendments to the initial policy by adding exemptions for non-corporate owned, single family homes; homes with owner-occupied accessory dwelling units; and certain property owners with health issues. However, the changes were not popular with TOPA advocates, who said that the amendments would make the policy ineffective in preventing the displacement of vulnerable renters. In late 2021, Mayor Arreguín decided to delay sending the draft ordinance to the Berkeley City Council. No further action has been made since the Mayor's decision.

In its report dated June 6, 2008, the CLA informed that in order to ensure a successful TOPA program in Los Angeles, the following three components would need to be developed: 1) a mechanism to ensure that tenants are notified of the opportunity to purchase their building before it is sold to an outside buyer; 2) a tenant support system; and 3) a public education mechanism to solicit and distribute information. According to the lessons learned included in the same report, there are additional issues with the TOPA program, including the program's vulnerability to corporate mergers, challenges with retaining institutional knowledge among all key players, and the difficulty of acquiring Title Insurance for TOPA transactions.

If the City wishes to pursue the Washington, D.C. TOPA program model, extensive outreach to tenant organizations and the public will be required, as well as continued management of public education efforts and engagement with tenant support organizations. Even if the program is implemented effectively, it may not prevent the displacement of the City's most vulnerable renters. Due to program complexity and the community support infrastructure, knowledge, and outreach required to implement the TOPA, this model is not the most effective at preventing the displacement of long-term renters the City.

Should Council choose to further evaluate the TOPA program, the TOPA Task Force could be activated to conduct the necessary outreach and program development. Council should provide guidance as to who should participate on the Task Force. It is recommended that LAHD be directed to coordinate the Task Force.

San Francisco - COPA – In June 2019, San Francisco established the Community Opportunity to Purchase Act (COPA) to allow certain Qualified Nonprofit Organizations designated by the Mayor's Office of Housing and Community Development the right of first offer and right of first refusal to purchase multifamily residential buildings in the city, with the condition that the property be maintained as rent-restricted affordable housing in perpetuity.

Under the COPA, the seller of a multifamily residential building must provide each Qualified Nonprofit an opportunity to make an offer to purchase the building before offering the building for sale to the public. Each Qualified Nonprofit then has five days to provide a written notice to the seller if it wishes to consider making an offer to purchase the building, and an additional 25 days to submit a purchase offer. The seller may accept or reject any offer. If the seller rejects all offers or if no Qualified Nonprofit makes an offer, the seller may offer the building for sale to the public. If the seller receives a market-rate offer, the seller must provide each Qualified Nonprofit Organization another opportunity to make an offer, based on the terms and conditions of the market-rate offer. If a Qualified Nonprofit matches the market-rate offer, the building must be sold to the Qualified Nonprofit pursuant to the offer.

The total funding allocation for the COPA for its inaugural year was $37 million, which included close to $3 million for non-profit capacity building, especially in neighborhoods with the most vulnerable tenants and communities of color. In addition, the city of San Francisco provides fast, flexible financing of up to $375,000 per unit through its Housing Accelerator Fund to assist Qualified Nonprofits to quickly acquire properties. In less than a year, the COPA assisted the affordable housing nonprofit Mission Economic Development Agency to purchase six residential buildings and prevent the displacement of their tenants. As of 2021, nine non-profit organizations were on the San Francisco Mayor's Office of Housing and Community Development's Qualified Nonprofit list.

The San Jose City Council is currently considering a COPA ordinance to address their local housing and displacement crisis. If passed, the ordinance will be enacted by the end of 2023. East Palo Alto and Oakland are also considering similar ordinances.

Considerations

In October 2021, East Palo Alto began discussions to consider establishing an opportunity to purchase act to offer renters, housing nonprofits, or the city a right of first offer to purchase investor-, corporate-, and absentee-owned multifamily housing properties before they are sold to the public. However, in March 2022, East Palo Alto's City Council voted to postpone further discussion for up to ten months amid strong opposition from landlords and real estate groups who argued that the ordinance interfered with their rights as property owners, would extend property sales timelines, and would cause property values to fall. East Palo Alto Council members are now considering eliminating the requirement to allow tenants, nonprofits, or the city to match subsequent bids for single-family homes, and have asked city staff to research the effect that opportunity to purchase ordinances have had on property markets in cities that have implemented them.

While the COPA has prevented the displacement of vulnerable renters in a short time, implementation of a COPA program in the City would require significant funding, including costs for capacity building among community based organizations. In addition, the development of a COPA policy for the City may face strong opposition from landlords and real estate groups who claim that it may cause property devaluation and delay property sales. If the City wishes to pursue the San Francisco COPA program model, our Office recommends that the CLA, with the assistance of LAHD, provide an in-depth analysis on how opportunity to purchase policies impact property sale timelines and property values, as well as their overall effectiveness in preventing the displacement of long-term residents.

San Francisco - Neighborhood Resident Housing Preference – San Francisco's Neighborhood Resident Housing Preference was established in 2015 and aims to prevent rampant speculation, preserve existing affordable housing in gentrifying neighborhoods, and ensure community stability. The policy requires 40 percent of units in new, affordable projects funded by the city to be set aside for residents already living within a half mile or within the same supervisorial district as the project being built. As of 2019, 39 percent of affordable units built from 2016 to 2018 were occupied by people from the surrounding areas through the Neighborhood Resident Housing Preference plan.

Considerations

Preference policies have a complex history because they have been used in the past to exclude communities of color from white suburban neighborhoods. Housing preference policies have been legally challenged as violations of the Fair Housing Act (FHA), which prohibits discrimination in the purchase, sale, rental, advertising, and financing of housing – public or private – on the basis of race, color, national origin, religion, sex, familial status, and disability.

In both 2016 and 2019, HUD requested to review San Francisco's Neighborhood Resident Housing Preference law, claiming that it violated the FHA and could perpetuate segregation. In August 2019, HUD requested ten years of documentation regarding the approvals and permitting of multifamily developments to "examine whether San Francisco's current practices impose artificial, arbitrary, and unnecessary impediments to fair housing choice by limiting affordable housing development that provides access to opportunities for [protected classes]."

The city submitted relevant documentation and discussed the policy with HUD, but HUD was not able to make a final determination about the policy. Due to the lack of sufficient HUD housing vouchers and federal funding for housing, the city only applies the Neighborhood Resident Housing Preference to projects that are not federally funded. If a development project has federal funding, the city submits the Tenant Selection Policy for that individual building to HUD for approval.

The City of Los Angeles would require overall HUD approval, rather than project by project approval, to effectively implement a program similar to San Francisco's Neighborhood Resident Housing Preference, as all supportive housing units in the City rely on Project Based Voucher funding, and approximately 30 percent of units rely on federal funding through Community Development Block Grant or HOME Investment Partnerships Program funds. The City should only consider a similar program once HUD has made a final determination on the legality of the legislation.

SB 649: Local Tenant Preference

On February 19, 2021, California Senator Dave Cortese introduced Senate Bill (SB) 649 to establish a State policy supporting local tenant preferences for lower income households that are subject to displacement risk. This bill seeks to authorize local governments to allow local tenant preference in affordable housing that is acquired, constructed, preserved, or funded with State or local funds or tax programs. The bill is currently pending in Committee. Our Office has prepared an attached Resolution to support SB 649 in its 2021-22 State Legislative Program.

C. Corporate/Private Equity Home Ownership

Innovations in federal financial policy, taxation, and the corporate structure in the late 1990's facilitated the ability of investment vehicles such as REITs and LLCs to benefit from favorable tax policies and have significantly transformed property investment. As a result, the U.S. housing sector has undergone a dramatic process of financialization, or the expanding and dominant role of financial markets and corporations in the field of housing, that has contributed to unaffordable and insufficient housing.

The housing crisis of 2008 also contributed to the consolidation of housing ownership into the hands of corporate entities and investment vehicles, and out of the hands of individual owners. In the years leading up to the 2008 housing crisis, homeowners were targeted by predatory mortgage lending and many families lost their homes to foreclosure, especially in communities of color. According to foreclosure reports from 2010, nearly eight percent of Black and Latino families lost their homes to foreclosures, compared to less than five percent of white families.

In 2012, the Federal Housing Finance Agency launched the 'Real Estate Owned Initiative' to sell government-owned foreclosed properties to qualified investors for use as rentals, a pilot program that accelerated the concentration of housing into the hands of corporations and private equity investors. Some of the world's largest private equity groups, hedge funds, and investors purchased 200,000 homes at below market prices in a larger effort to bail out the housing market. Over time, these corporations found that it was financially lucrative to be in the rental market, and investor ownership of rental properties of all sizes grew sizably by 2015. However, various studies have found that corporations are not the best landlords and are more likely than smaller landlords to raise rents, evict tenants, and poorly maintain their properties. A 2018 HUD study in Atlanta found that large corporate landlords were 68 percent more likely than smaller landlords to file eviction notices.

According to recent reports, investors are preparing for what they believe could be another opportunity to buy distressed real estate assets at bargain prices, as families struggle to make mortgage payments due to increasing inflation and the expiration of federal and state mortgage relief programs established during the COVID-19 pandemic. According to Redfin, real estate investors bought 18.4 percent of homes that were sold in the U.S. in the fourth quarter of 2021, up from 12.6 percent the previous year. Increased influence of real estate investors in the housing market will make it increasingly harder for prospective owner-occupants to purchase homes. According to estimates from the National Association of Realtors, about 2.5 million homebuyers will be shut out of the market, in part due to competition with investor purchasing.

Home ownership by corporations and investors has the power to change communities. In May 2022, an investment fund backed by Goldman Sachs purchased an entire community of 87 single family homes in Central Florida for just over $45.7 million. Home owner associations across the nation have been responding to this trend by voting on leasing amendments and other actions to make it harder for corporations to purchase homes, such as requiring anyone buying a home in their housing development to live in the unit for at least a year before renting it out. Lawmakers at the local and federal levels have also recently taken action to limit corporate expansion in the housing market and prevent the bulk purchases of foreclosed properties by corporations and private equity entities, which are detailed later in this report.

The City has initiated multiple actions to limit real estate speculation and corporate ownership of housing and continues to monitor related legislation. Motion (Bonin – Harris-Dawson, C.F. 20-0199) was introduced on February 12, 2020 and informed that anonymous shell companies and LLCs facilitate real estate speculation in the City. According to the U.S. Census Bureau, nearly three million homes and 13 million apartment units in the U.S. are owned by shell companies, including LLCs, Limited Liability Partnerships (LLPs), and Limited Partnerships (LPs), resulting in the proportion of residential rental properties owned by individuals falling from 92 percent in 1991 to 74 percent in 2015. The Motion also stated that some housing units purchased by shell companies remain vacant, as they are held as investments and not offered as housing, which further exacerbates the City's housing crisis.

Further, the Motion informed that in September 2019, New York amended their state tax law (New York State Tax Law §1409) and Administrative Code (New York Administrative Code §11-2105) to require the name and address of every member of an LLC that acquires or sells residential real estate in the state. The laws were enacted with the intention of only covering the sales of properties with one to four units, but has been interpreted as affecting every transaction involving a residential unit, including the sale of cooperatives and condominiums. The reported information would then be available through public record requests. These laws aim to curb money laundering and tax evasion, and help enforce code violations by anonymous landlords.

On October 20, 2020, Council adopted the Motion to direct: 1) the City Attorney, in consultation with the CLA, LAHD, and researchers, experts, and activists in the field, to report on recommendations to adopt a Citywide ordinance requiring the disclosure of beneficial ownership of LLCs purchasing real estate in the City of Los Angeles; 2) the City Attorney, CLA, and LAHD to report on recommendations to include other types of corporations, beyond LLCs in the ordinance; and 3) the CLA, CAO, and LAHD to report on an estimate of the number of residential units currently owned by LLCs in Los Angeles, including as a proportion of total units. The report is currently pending.

On March 1, 2022, S. 8439 was introduced in the New York State Senate to expand New York's state tax law and Administrative Code to apply to all real estate purchases, amid efforts to target assets of international oligarchs in response to the Russian invasion of Ukraine. The new bill is pending.

On June 25, 2021, Council adopted Resolution (Rodriguez – Bonin, C.F. 21-0002-S96) to support AB 1199 (Gipson) that would create transparency relating to property ownership in the State and impose a tax on larger corporate landlords. Revenue from the tax would fund critically needed services such as homebuyer education, tenant and small landlord relief, homeless prevention, and job training apprenticeship programs. The bill died in Committee.

Considerations

In 2021, Assemblymember Mike Gipson also introduced AB 889 to require LLCs and LPs owning single family or multifamily rental properties in the State to report specific information annually to the Secretary of State's Office to be published in a searchable public database. Both AB 1199 and AB 889 failed to pass, indicating challenges to pass legislation to require the disclosure of beneficial ownership in the State of California.

There are similar efforts at the federal level to require the disclosure of beneficial ownership reporting. The U.S. Treasury Department's Financial Crimes Enforcement Network (FinCEN) will issue final regulations to require every foreign or domestic legal entity (e.g. operating businesses, holding companies, LLCs, etc.) to report the identities of beneficial owners of the entity, as well as individuals who filed forms to register the entity by the end of the year. FinCEN estimates that 25 million existing legal entities, plus an additional three million new legal entities each year will be subject to the regulation.

This regulation may not achieve the same goals intended by AB 1199 and AB 889, as exemptions can waive the reporting requirement for banks, investment companies, pooled investment vehicles, companies that have a physical address in the U.S., and companies that have filed a federal income tax or information return in the U.S. demonstrating more than $5 million in gross receipts. State and local level legislation that aims to disclose beneficial ownership reporting of real estate investment vehicles and corporations would be most effective at identifying individuals who are purchasing multiple single family homes and amassing huge portfolios of rental properties in the City.

While beneficial ownership reporting can assist the City with enforcing code violations for corporate and private equity landlords and make investor property ownership information available to the public, it will not limit the concentration of properties owned by corporations and real estate investment vehicles. Instead, this Office recommends that the Council instruct LAHD to conduct an audit of the number of single family homes owned by real estate investment trusts, partnerships, corporations, and limited liability entities in the City, and explore legislation to limit or cap the number of properties that can be owned by those entities.

Legislation

The following legislation can help prevent the bulk sale of foreclosed properties to corporations and investment vehicles and disincentivize the accumulation of single family homes by corporations and investors to be used as rental and/or investment properties in the State.

SB 1079: Residential Property Warehousing

Senate Bill (SB) 1079, "Homes for Homeowners, Not Corporations" was introduced by Senator Skinner on February 18, 2020 and approved by the Governor on September 28, 2020. This bill applies to all residential properties with one to four housing units in California and went into effect on January 1, 2021, with a five-year sunset.

This bill:

- Prohibits real estate trustees from bundling foreclosed properties for sale, instead requiring each property to be bid on separately.
- Mandates compliance with recently enacted laws regarding the eviction of tenants, including relocation assistance and just cause eviction in the case of a post-foreclosure eviction.
- Extends the nonjudicial foreclosure process to allow "Eligible Tenant Buyers" and "Eligible Bidders" (prospective owner-occupants, nonprofit associations, or cooperative organizations engaged in the development and preservation of affordable housing) the opportunity to purchase a foreclosed property within 15 days after a trustee sale closes, if they match or exceed the last and highest bid price at auction.

SB 1079 aims to mitigate the negative impacts from a potential upsurge in foreclosures as a result of COVID-19 and limit the accumulation of foreclosed properties by large investors. This law provides prospective owner-occupants, public entities, and community housing organizations a right of first refusal and an additional 15 days to exceed winning bids for properties sold at foreclosure auctions. In addition, eligible tenant buyers are provided the right of purchase by matching the winning bid within 45 days of a foreclosure sale. SB 1079 also seeks to facilitate the upkeep and quick rental of foreclosed properties that investors may otherwise keep vacant by increasing the penalty to $5,000 per day of violation.

This law does not designate the appropriate agency or City department to implement this legislation. The City may need to adopt an ordinance in order to implement this law. We recommend that Council instruct LAHD and the Department of Building and Safety to report on how the City can implement the provisions of SB 1079.

AB 1771: California Housing Speculation Act

On February 2, 2022, California Assemblymember Chris Ward introduced Assembly Bill (AB) 1771, the California Housing Speculation Act. AB 1771 proposes an additional 25 percent tax on the portion of capital gain from the sale or exchange of residential properties within three years of the purchase of the property. The additional tax rate would decline in annual increments until it is eliminated after seven years. Assemblymember Ward asserts that "most California homeowners keep their property for ten to 16 years, so it would not affect most people buying a home for personal use." Tax revenue from the bill would be allocated to affordable housing development and infrastructure projects. The bill seeks to discourage real estate speculation, the buying and quick selling of homes for a profit, and the driving up of home prices across the State. The bill requires a two-thirds majority vote in the California Assembly and Senate to become law. Our Office has prepared an attached Resolution to support AB 1771 in its 2021-22 State Legislative Program.

Susan Oh

Susan Oh
Analyst by KEK

Attachment A: Motion (Martinez – Raman, C. F. 21-1244)

Attachment B: Resolution to support SB 649, Local Tenant Preference

Attachment C: Resolution to support AB 1771, the California Housing Speculation Act

ATTACHMENT A

MOTION

The median price of a single-family home in the United States has increased by 28% over the last two years. The City of Los Angeles ranks among top most unaffordable cities in multiple studies each year. As of August 21, the LA City recorded a price increase of 11.3% compared to the prior year.

The housing crisis has been further exacerbated by high tech companies such as Zillow, Opendoor, Rockethomes, and Redfin as well as private equity firms. These companies primarily target affordable, single-family homes and compete to buy up as much inventory as possible, flip them, and then sell them for a profit. At Zillow, a recent earnings report shows agents selling these homes at a 13.1% profit.

This trend systematically increases the pricing of single-family homes in a real estate market that is already experiencing skyrocketing housing prices. Low-income Angelenos, who have lived in their neighborhoods for decades, are unable to compete with these iBuyers. This has led to many longtime residents being pushed out of their homes, neighborhoods, and communities.

I THEREFORE MOVE that the City Council instruct the City Legislative Analyst and City Attorney to report back with recommendations on strategies the City can use to prevent large tech and private equity firms from engaging in speculative practices that involve purchasing affordable, predominantly single family housing.

PRESENTED BY: ____________________
NURY MARTINEZ
Councilwoman, 6th District

SECONDED BY: ______________________

ATTACHMENT B

RESOLUTION

WHEREAS, any official position of the City of Los Angeles with respect to legislation, rules, regulations or policies proposed to or pending before a local, state or federal governmental body or agency must have first been adopted in the form of a Resolution by the City Council with the concurrence of the Mayor; and

WHEREAS, rising rents, gentrification, redevelopment, and a housing shortage threaten to displace thousands of households in California; and

WHEREAS, these pressures force low-income Californians, who are disproportionately people of color, to overcrowd their homes or move away from their employment and communities in search of more affordable housing; and

WHEREAS, neighborhood preference policies have the ability to stabilize neighborhoods and protect tenants at risk of displacement by providing them priority placement for affordable housing in their neighborhoods; and

WHEREAS, on February 19, 2021, California Senator Dave Cortese introduced Senate Bill (SB) 649 to establish a State policy to support local tenant preferences for lower income households who are at risk of displacement; and

WHEREAS, SB 649 would authorize local governments to allow a local tenant preference in an affordable housing development that is funded by local and/or State funds, including funding from tax-exempt bonds; and

WHEREAS, SB 649 creates two types of tenant preferences to prevent displacement: the Anti-Displacement Tenant preference that sets aside a portion of affordable housing to low-income applicants who live in areas categorized as high-risk of displacement, and the Neighborhood Tenant Preference that makes newly available affordable housing available to low-income applicants who already live in the vicinity of the affordable housing; and

WHEREAS; SB 649 will allow local governments to implement tenant preference policies that can help families at risk of displacement find affordable housing in their communities;

NOW, THEREFORE, BE IT RESOLVED, with the concurrence of the Mayor, that by adoption of this Resolution, the City of Los Angeles hereby includes in its 2021-22 State Legislative Program SUPPORT for SB 649 to authorize local governments to allow a local tenant preference in affordable housing that is acquired, constructed, preserved, or funded with State or local funds or tax programs.

ATTACHMENT C

RESOLUTION

WHEREAS, any official position of the City of Los Angeles with respect to legislation, rules, regulations or policies proposed to or pending before a local, state or federal governmental body or agency must have first been adopted in the form of a Resolution by the City Council with the concurrence of the Mayor; and

WHEREAS, in 2021, home prices in the State of California increased by 17 percent, and in some regions exceeded 20 percent year-over-year with forecasts of a continued rise in 2022; and

WHEREAS, inferred market analysis suggests that investor-bought homes represented approximately 51 percent growth of sales in Southern California from 2020 to 2021, compared to a national average of 20 percent; and

WHEREAS, real estate investors are winning home bidding wars with all cash offers, upzoning and redeveloping housing into luxury properties, and landbanking undeveloped properties, ultimately making properties unaffordable and unavailable for prospective owner-occupant homebuyers in the market; and

WHEREAS, growing real estate speculation in Southern California has inflated home prices and made it increasingly difficult for first-time homebuyers, who do not have equity gains from previous property ownership to leverage funds to purchase property, and are often forced to move out of their communities and away from city and job centers in search of more affordable housing; and

WHEREAS, currently pending in the California State Assembly is the California Housing Speculation Act (AB 1771) that proposes an additional 25 percent tax on the portion of capital gain from the sale or exchange of residential properties within three years of the purchase of the property; and

WHEREAS, after the third year of the original purchase, the surtax would be reduced by 20 percent until it is eliminated after seven years; and

WHEREAS, California Assemblymember Ward asserts that most California homeowners keep their properties for ten to 16 years, so AB 1771 would not affect most people buying a home for personal use; and

WHEREAS, tax revenue from AB 1771 would be allocated to affordable housing development and infrastructure projects; and

WHEREAS, AB 1771 aims to discourage real estate speculation, the buying and quick selling of homes for a profit, and the driving up of home prices across the State;

NOW, THEREFORE, BE IT RESOLVED, with the concurrence of the Mayor, that by adoption of this Resolution, the City of Los Angeles hereby includes in its 2021-22 State Legislative Program SUPPORT for AB 1771 to impose an additional 25 percent surtax on the portion of capital gain from the sale or exchange of residential properties within three years of the original purchase of a property.