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2023 Year End Owner Update
November 2023

Dear Wellspring Property Management Owner,

I hope this letter finds you well. The purpose of this letter is to provide our property owners with an update on what has transpired in the California rental market during 2023, and a preview of what to expect in 2024. Although this letter is long and some of the market trends are sobering, we take seriously our commitment to keeping you informed.

Looking back on 2023:
The primary story of 2023 was change. A downward trend in sales and rental rates and changes in new legislation. In the 7 years I have had the privilege of managing homes for investors and 4 years prior as a sales agent, I have never seen the atmosphere we have. It is not an overstatement to say there has been a significant change in the landscape of property management in California, shifting more burdens to property owners while expanding the rights of tenants.

Below we offer a brief overview of 4 laws we have had to navigate in 2023, along with links to the laws themselves.

AB -1410 Common Interest Developments and homeowner right to rent
Bans HOAs from prohibiting the rental or leasing of a portion of a separate interest in situations where the homeowner still lives on site.

AB - 2559 Reusable Tenant Screening Reports
Establishes criteria for the voluntary acceptance of reusable tenant screening reports (RTSRs) by landlords and specifies the applicant information that must be included in RTSRs. A landlord that accepts RTSRs may not charge either a fee for the landlord to access the report or an application screening fee.

SB - 1017 Leases: Termination of Tenancy: Abuse or Violence
This new law imposes statutory damage of $100 up to $5,000 (in addition to actual damages) when a landlord or agent ignores a tenant's right to terminate a tenancy based on acts of domestic violence.

SB - 1076 Lead-Based Paint Remediation

This law requires a "firm" and at least one person onsite and employed by a firm doing renovation, repair, or painting work for compensation in a residential or public building to have a certificate for training in lead-safe work practices. Substantial civil or criminal penalties are now imposed for violating this rule.

AB - 2503 Landlord and Tenants: Lease verbiage Study

This law requires the California Law Revision Commission, by December 31, 2024, to deliver a study to the Legislature examining the establishment of consistent terminology in California law to describe the parties to an agreement, lease, or contract for the rental of residential real estate property, including mobile homes.

Although many of these laws are complex and require significant and sometimes immediate operational changes; through our internal analysis and by working closely with our legal counsel we were able to make all necessary changes. This ensures we remain legally compliant and still provide you and your property with maximum legal protection.

Aside from these changes to the legal landscape, the California rental market also experienced decreasing renter demand in 2023. Rents peaked in early 2023 and rents are currently on a downward trend, especially in the single-family home market, as compared to this time last year. In addition, we are seeing many vacant rental properties now offering move-in discounts of up to one month of free rent to attract new tenants.

Looking ahead to 2024:

It would be a mistake to think that all the legislative challenges to owning rental properties are behind us. The 2024 California legislature is expected to vote on several bills including rent control as well as limiting a landlord's ability to non-renew a lease.

Nationally, the Biden administration has proposed a federal tenant bill of rights.

The legal landscape of rental real estate will remain challenging in 2024.

Our markets in Northern and Southern California will see a new supply of rental housing in 2024 as new apartment construction increases. New rental supply is also coming from homeowners who are converting their properties to rentals rather than selling, and VRBO/Airbnb investors who are converting their properties from short-term to long-term rentals.

While we have this significant new supply of rental properties, renter demand is slowing. The effects of inflation, the ending of student loan payment deferment, and rental price increases over the past several years are resulting in some tenants delaying their planned renting experience, doubling up on housing, or simply not moving into a different rental property at all.

We expect these market changes to result in average rents remaining flat or declining modestly in 2024.

Another challenge facing landlords in 2024 is the increased cost of rental ownership. Property insurance costs and property taxes are expected to increase by double digits. The costs for maintenance and repairs have also increased dramatically over the past few years. Inflation, along with a reduction in the availability of contractors, has caused increases of up to 50% in items like paint, carpet, appliances, and general repairs over the past 24 months. We do expect the rate of these cost increases to slow in 2024.

To sum up the rental market in one sentence: Rental supply is up, renter demand is down, rents are flat or declining, expenses are up, and legal risks have increased.
While this may not be the most attractive market for investors, it is important to keep in mind that for the past decade, we have seen annual double-digit rental rate growth, annual double-digit home price appreciation, and generational low-interest rates. What we are experiencing now is simply the market correcting back to a more moderate position as we come out of this decades long hyper-growth cycle.

We do have several strategies in place to ensure you and your property remain protected and financially strong:

<u>#1 – Resident Retention:</u>
As the financial costs of resident turnover have always been the most significant expense landlords face, we will continue to focus heavily on resident retention in

2024. In 2023 our tenant retention rate was more than 80%. Although life circumstances will always result in some residents having to move out of their property, (and we purposefully non-renew some residents if they are not performing on the terms of their lease agreement), we will work to ensure all of our quality residents remain in their properties in 2024.

The reason we are able to achieve this industry leading retention rate is largely due to creating a positive experience with our residents during their lease term. Things like fast repair services, online payment options, and good old-fashioned customer service ensure our residents feel respected and want to stay with us. This results in avoiding unnecessary turnover and vacancy expenses for you, the owner.

#2 – Minimizing Vacancy Time During Turnover:
For those properties that do experience turnover in 2024 we will ensure the property is brought back to full rent-ready condition as quickly and as economically as possible. Our premium property marketing package ensures maximum visibility to people looking for a rental and our leasing team constantly monitors activity. This high touch process allows fast feedback to ensure we minimize vacancy time.

2024 is poised to be another year with additional new laws that will make significant impacts on landlords and property managers alike. We have briefly noted 7 new laws below. While some of these laws will not specifically impact all the markets we serve, we feel it important to make you aware of them, because eventually, they will make their way to all markets.

AB - 1620 Costa-Hawkings Rental Housing Act: Permanent Disabilities: Comparable or Smaller Units
Allows a jurisdiction with local rent control to require an owner of a rent-controlled unit to allow a tenant with a permanent physical disability to relocate to an available comparable or smaller unit located on an accessible floor of the property and retain the same rental rate.

AB – 1764 Housing Omnibus
Landlords will have the option to provide receipts for tenant screening fees via email when both landlord and applicant agree to it first.

SB - 267 Credit History of persons receiving government rent subsidies

Landlord must offer "ability to pay" in lieu of reliance on credit history and reports in assessing a tenant's rental application when a prospective tenant is receiving a government rent subsidy such as a Section 8 rental voucher.

SB - 712 Tenancy: Personal Micromobility Devices
SB 712 prohibits a landlord from prohibiting a tenant from owning personal micromobility devices or from storing and recharging up to one personal micromobility device in their dwelling unit for each person occupying the unit, subject to certain conditions and exceptions.

AB - 1418 Tenancy: Local Regulations: Contact with Law Enforcement or Criminal Convictions
Prohibits local ordinances that penalize tenants and landlords for various types of law enforcement contacts, i.e., local "crime free" rental housing programs and ordinances.

AB - 12 Tenancy: Security Deposits
Landlords may collect no more than one month's rent for either furnished or unfurnished units in addition to the first month's rent. There is an exception for small landlords, defined as a landlord who is a natural person or LLC and owns no more than two residential rental properties with no more than a total of four units offered for rent.

SB - 567 Termination of Tenancy: No-fault Just Causes: Gross Rental Rate Increase

This law tightens up the requirements for a landlord to terminate a tenancy under the Tenant Protection Act (i.e., California statewide rent cap and just cause eviction law) for no-fault evictions based upon owner move-in or substantial remodeling.

Additionally, an owner who violates the TPA by improperly terminating a tenancy or by raising rent beyond the maximum amount is liable for actual damages, reasonable attorney's fees and costs (at the discretion of the judge), up to three times actual damages for willful violations and punitive damages. The Attorney General et al is authorized to seek injunctive relief. Effective April 1, 2024.

#3 – Competitive Vendor Pricing:
We screen all of our third-party vendors annually on pricing, quality of work, and timeliness. We will continue to ensure we receive competitive pricing as we benefit from both our internal economies of scale, and a loosening in the labor market.

We do believe the long-term outlook for real estate investors is positive and we remain committed to the principle that when property management is performed with integrity, both the property owner AND the resident benefit. We are committed to serving both our owners and our residents by providing clean, safe, and fair priced housing.

Operational Updates For 2024
The above referenced laws require us to make several significant changes to our business including the applicant screening process, the rent collection process, the lease renewal process, and the eviction process. Below are a few of the changes that may impact you or your property:

1. We are required by law to lower the processing standards on all applicants. Although we are no longer allowed to process or consider the credit report on subsidized applicants, we are still processing our rental applications to the full extent of the law in an effort to screen out high risk tenants. Our current monthly rent collection averages 90% of all rents due. This is primarily due to our applicant screening process and we are committed to only placing properly vetted and highly qualified residents in our rental properties.
2. We are required by law to accept tenant provided background reports. When this happens, we will ensure the accuracy of these reports.
3. The legal eviction process has been significantly complicated and delayed. The average time it now takes to evict a non-paying tenant is 120 days. Although evictions are rare, when this happens, we are experienced in overseeing this process in a timely and fair manner.

The necessity of regular interior property inspections, while tenant occupied, has never been more important. In the past, we have not charged a fee for this service. Effective 1/1/24, we will be implementing a fee charged at the completion of the full lease renewal and/or review process of $125 and will be used to help recover the additional costs associated with these walkthroughs and subsequent review after each inspection. This is not a monthly fee and will only be charged near the anniversary of your tenants' lease should we choose to renew them. If they submit a 30-Day Notice, this fee will not be charged.

Christina Wade, Broker/Owner
Wellspring Property Management