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LOS ANGELES
ORANGE COUNTY
SAN DIEGO
SAN FRANCISCO
SANTA BARBARA
WESTLAKE VILLAGE

June 14, 2016

VIA HAND DELIVERY

Mr. David Belmer, City Planning Director
Anaheim City Hall
200 South Anaheim Boulevard
Anaheim, CA 92805

With Copies To:
Mr. Paul Emery, City Manager
Ms. Kristine A Ridge, Assistant City Manager
Ted Reynolds, Esq., Assistant City Attorney

Re: **Preliminary Study on Just Compensation:**
Implications of Banning Existing Short-Term Rentals in Anaheim

Dear Mr. Belmer:

On behalf of the Anaheim Rental Alliance, we enclose a Preliminary Study for your use as you evaluate the length of a lawful amortization period in connection with an ordinance proposing to extinguish the fundamental vested rights of Anaheim short-term rental (STR) permit holders.

The study relies on actual data provided by 54 distinct STRs. The study is conservative; it excluded data from properties with exceptional circumstances. The report concludes that a ban of STRs would result in $60,000,000.00 of unrecoverable losses to existing STR permit holders. An amortization period of 10 years would allow two-thirds of the STR permit holders to recoup this unrecoverable investment. An amortization period of 12 years would allow recoupment for three-fourths of the STR permit holders, while 15 years would cover 85% of the properties.

Please do not hesitate to contact me if you have questions.

Very truly yours,

Jane Ellison Usher
for MUSICK, PEELER & GARRETT LLP

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RGL Forensics

Discovering & Defining Financial Value

Implications of Banning Existing Short-Term Rentals in Anaheim: Just Compensation

Preliminary Study Prepared for Anaheim Rental Alliance

June 14, 2016

Study Objective:

The Anaheim City Council is to consider an ordinance that would ban existing permitted Short-Term Rentals (STRs). Such a ban would require the City to provide "just compensation" prior to extinguishing the fundamental vested rights of permitted owners to operate their STRs. Legal precedent also suggests that provision of an amortization period, over which existing STR owners could continue to operate their STRs, may satisfy the City's responsibility to provide just compensation. This preliminary study was designed to utilize accepted methodologies to estimate a satisfactory amortization period should the City propose such a period to offset their duty to provide just compensation.

Conclusion:

RGL's analysis indicates that, should a ban be enacted, an amortization period of ~10 years would likely allow ~2/3 of existing STR properties to recover the owners' unrecoupable investments. Alternatively, an amortization period of ~12 years would cover ~3/4 of the STR properties and ~15 years would cover ~85% of the STR properties.

RGL STUDY PROTOCOLS & METHODOLOGIES

Schedule 1

Background:

- ☐ Anaheim currently has ~370 permitted STRs, ~1/3 of which are condominiums and ~2/3 single family residences (SFR).
- ☐ The City Council enacted an ordinance allowing for STRs on May 13, 2014, with a permit application deadline of July 31, 2014.
- ☐ Given the recent permitting, most STRs owners have not yet earned back their sizable investments (see Schedule 4).
- ☐ Similarly, many STRs have not yet achieved full earnings potential due to the necessary maturation period (see Schedule 3).

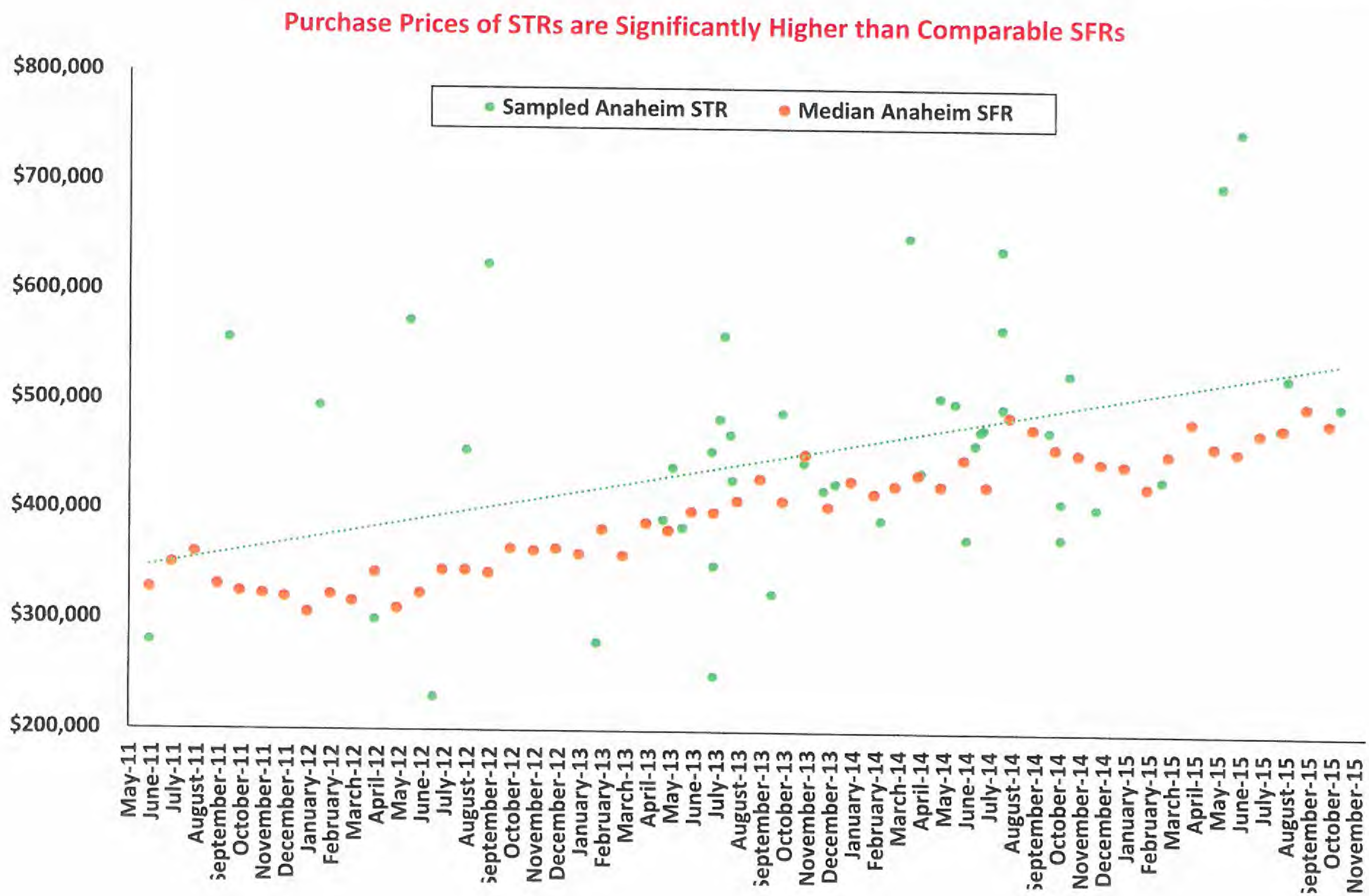
Study Protocols:

- ☐ RGL obtained detailed statistics from well over a dozen Anaheim STR owners for key information regarding their STR properties.
- ☐ We received survey responses covering 54 STR properties, representing ~15% of the total permitted STR population.
- ☐ Dataset excludes over a dozen extreme outliers that have post-purchase startup costs exceeding ~$600k per property.
- ☐ Resulting statistics detailing actual investments into the properties and their resulting profitability were analyzed.
- ☐ Three different methods were used to determine the average amortization period needed to provide just compensation.

Methodologies Utilized:	**_Median Amortization Period_**
Fair Market Value Method: Determined by subtracting the value of the land and building sold on the open market without the STR permit from the value of the property if sold with existing STR permit. Unrecoupable value is then divided by annual net income.	**9.7 Years**
Investment by Owner Method: Determined by subtracting the value of the land and building if sold at market without the STR permit from the total owner investment into the property. Unrecoupable investment is then divided by annual net income.	**9.2 Years**
Replacement Cost Method: Determined by establishing the cost of moving the STR to another suitable location and then subtracting the value of the land and building that remains if sold at market without the STR permit. Unrecoupable replacement value is then divided by annual net income.	**12.4 Years**
OVERALL AVERAGE AMORTIZATION PERIOD	10.5 Years

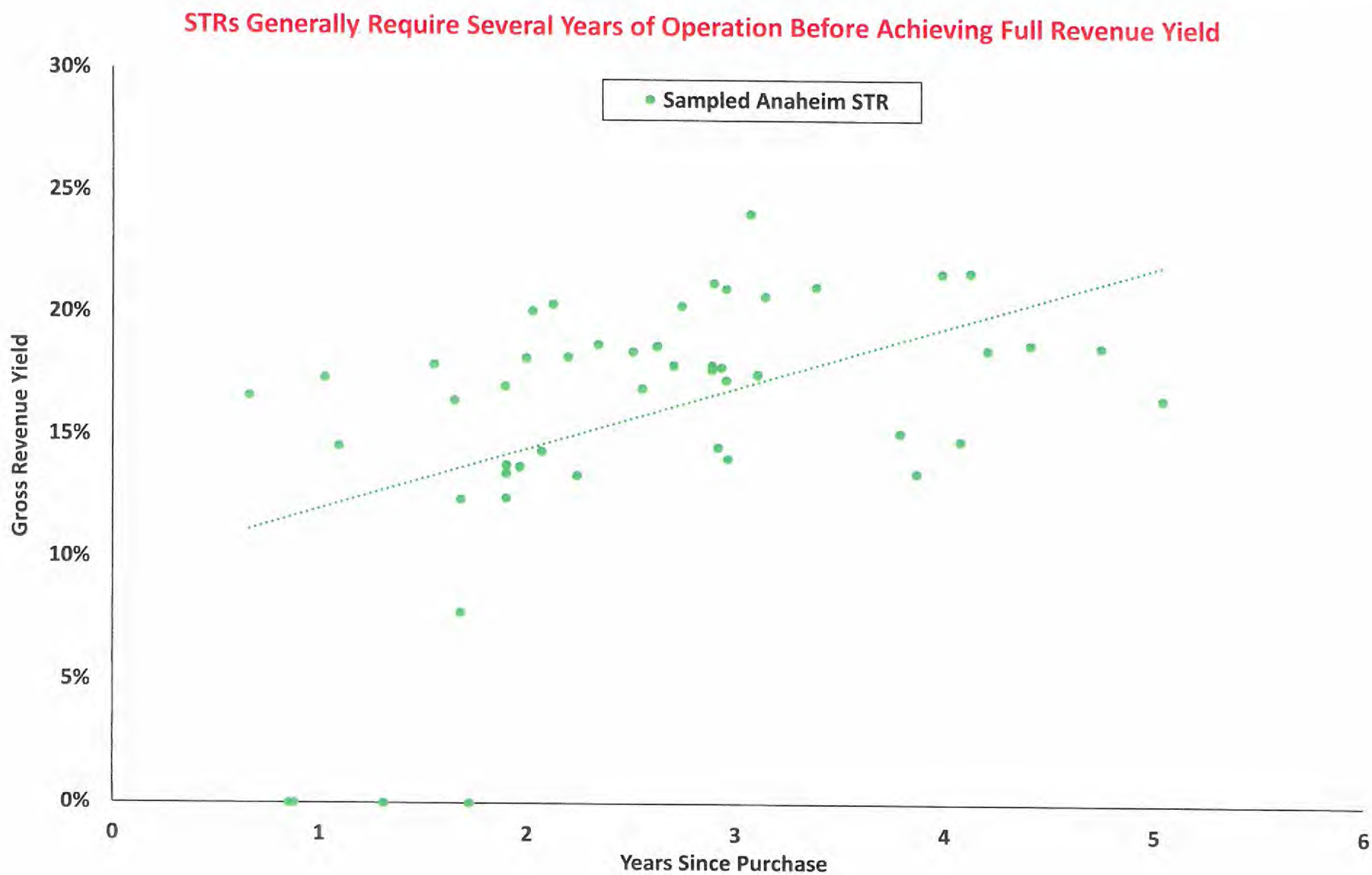
PURCHASE PRICES OF SAMPLED STRs VS. MEDIAN ANAHEIM SFRs OVER TIME

Schedule 2



SIMILAR TO STARTUP BUSINESSES SAMPLED STRs REQUIRED A MATURATION PERIOD

Schedule 3



OVERVIEW OF SAMPLED ANAHEIM STR DATA

Schedule 4

RGL calculated metrics, excluding clear outliers.

Description	Sampled Properties		
	20th Percentile	Median	80th Percentile
Purchase Price	$ 376,640	$ 458,750	$ 538,397
Original Loan Amount (Standard or Commercial Loans)	242,968	375,000	427,247
Estimated Current Market Price	474,606	550,000	600,000
Additional Purchase, Startup & Marketing Costs	21,095	32,518	45,773
Improvements & Furnishings	75,432	116,956	210,543
Negative Cash Flow Until Break-Even	7,500	20,753	35,893
Years Since Purchase Before First Monthly Break-Even	0.4	0.7	1.4
RGL Calculated Unrecoupable Investment	$ 66,814	$ 153,862	$ 221,341

Description	Sampled Properties		
	20th Percentile	Median	80th Percentile
Annual Revenue (Normalized for Mature Operations)	$ 80,432	$ 97,496	$ 115,570
Operating Expenses	32,393	43,404	68,033
Maintenance Expenses	4,696	7,392	8,899
Replacement of Furniture & Furnishings	-	2,250	5,000
Management Expenses	8,192	13,165	27,193
Accounting, Legal, Consulting Fees	555	1,000	3,923
General Business, Insurance & Travel Expenses	1,152	5,700	9,691
RGL Calculated Annual Net Profit	$ 9,116	$ 14,124	$ 24,610

COMMON-SIZED ANALYSIS OF SAMPLED ANAHEIM STRs

Schedule 5

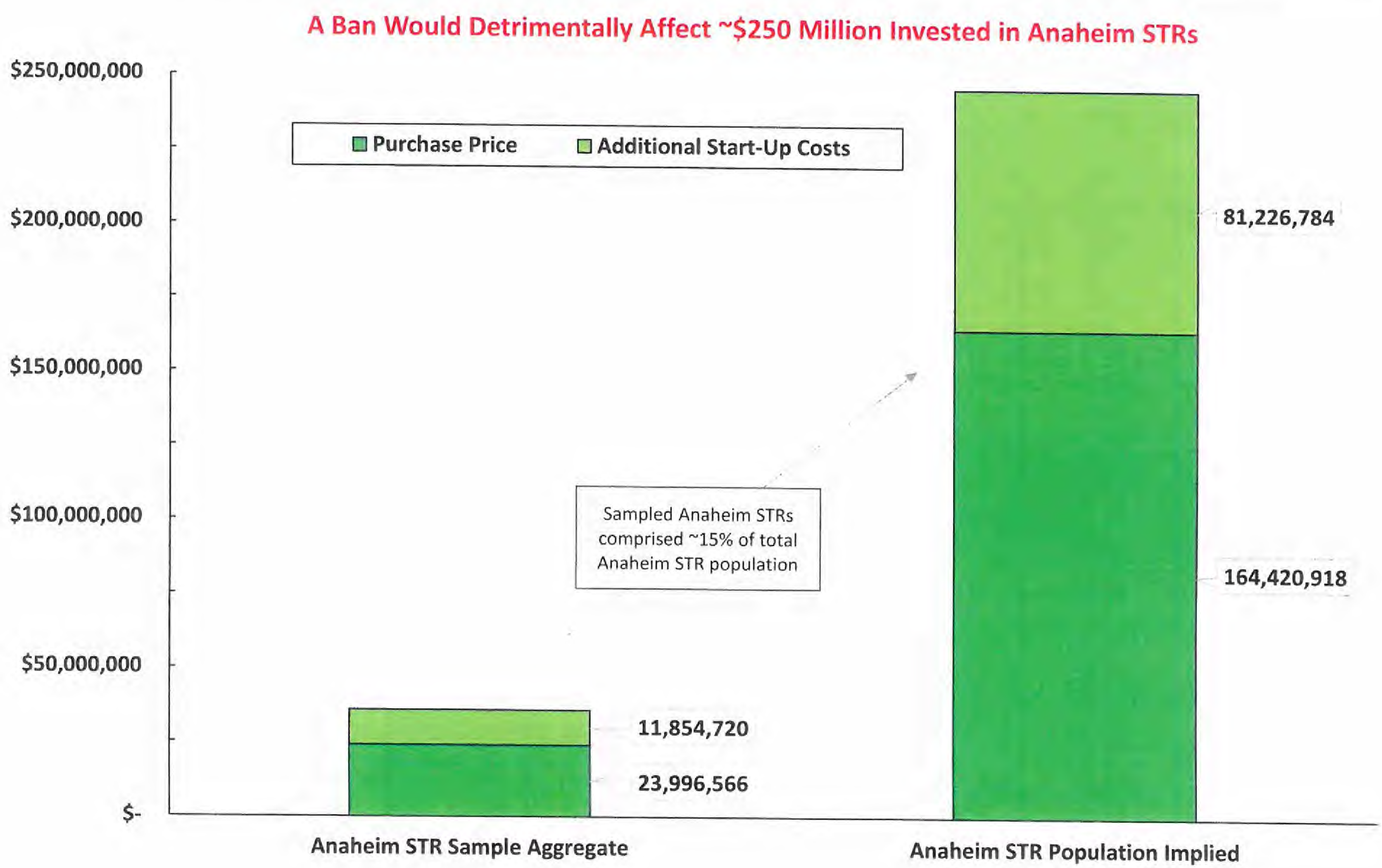
RGL calculated metrics, excluding clear outliers.

Description	As % of Purchase Price		
	20th Percentile	Median	80th Percentile
Purchase Price	100%	100%	100%
Original Loan Amount (Standard or Commercial Loans)	67.7%	75.0%	100.0%
Estimated Current Market Price	106.0%	117.3%	146.2%
Additional Purchase, Startup & Marketing Costs	4.4%	6.6%	11.4%
Improvements & Furnishings	17.3%	30.2%	55.9%
Negative Cash Flow Until Break-Even	2.2%	5.0%	7.4%
RGL Calculated Unrecoupable Investment	19.9%	32.7%	43.5%

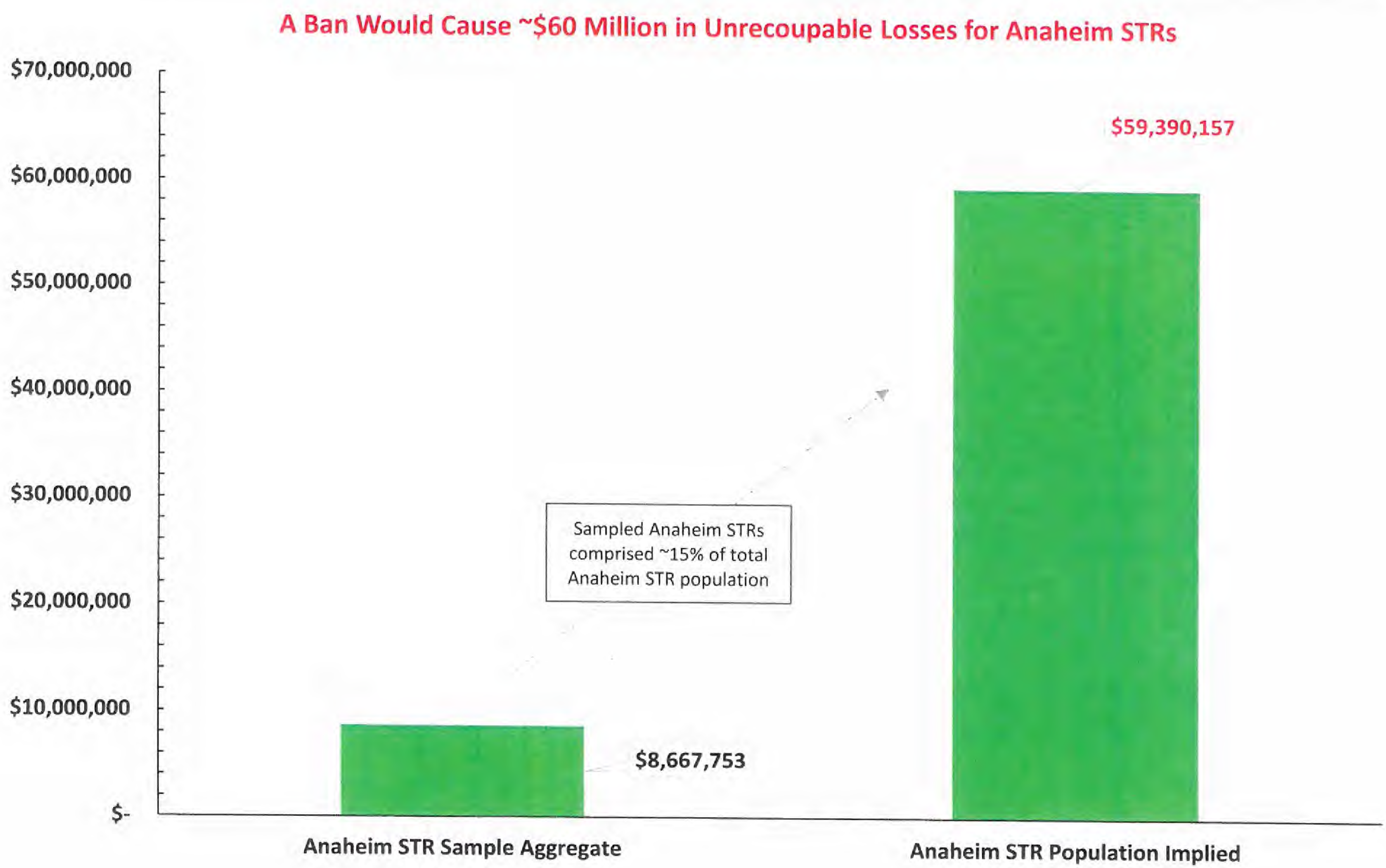
Description	As % of Annual Revenue		
	20th Percentile	Median	80th Percentile
Annual Revenue (Normalized for Mature Operations)	100%	100%	100%
Operating Expenses	35.7%	46.9%	61.7%
Maintenance Expenses	5.3%	6.7%	9.7%
Replacement of Furniture & Furnishings	0.0%	2.4%	5.2%
Management Expenses	10.0%	12.8%	29.9%
Accounting, Legal, Consulting Fees	0.5%	1.1%	4.2%
General Business, Insurance & Travel Expenses	1.1%	6.1%	10.2%
RGL Calculated Annual Net Profit	9.6%	15.3%	25.0%

TOTAL AMOUNTS INVESTED IN ANAHEIM STRs

Schedule 6



TOTAL ESTIMATED UNRECOUPABLE LOSS TO ANAHEIM STRs IF BAN IS ENACTED (Median of Three Methods) *Schedule 7*



DETAILED DESCRIPTION OF CALCULATIONS & ASSUMPTIONS

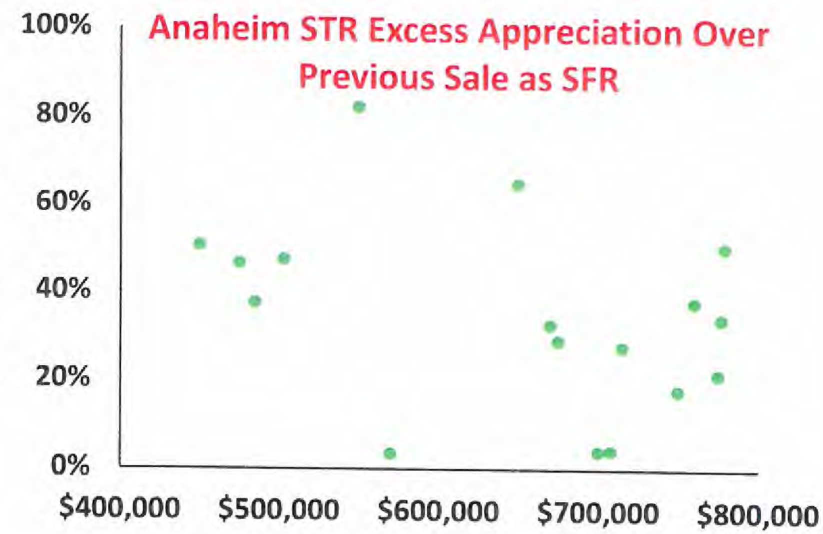
Schedule 8

(For All Methods) Amortization Period = Unrecoupable Loss/Net Profit

Fair Market Value Method - See Schedule 9

□ Determined STR value "premium" by comparing excess price appreciation of 21 Anaheim properties recently sold as STRs versus the same properties' previous sales as SFRs (see adjacent graph).

□ Results indicated a median STR premium of 34%, corresponding to an implied 25% decline in values for STR properties should their permit rights be denied. As such, unrecoupable loss was calculated assuming a 25% decline in STR property values after a ban.



Investment by Owner Method - See Schedule 10

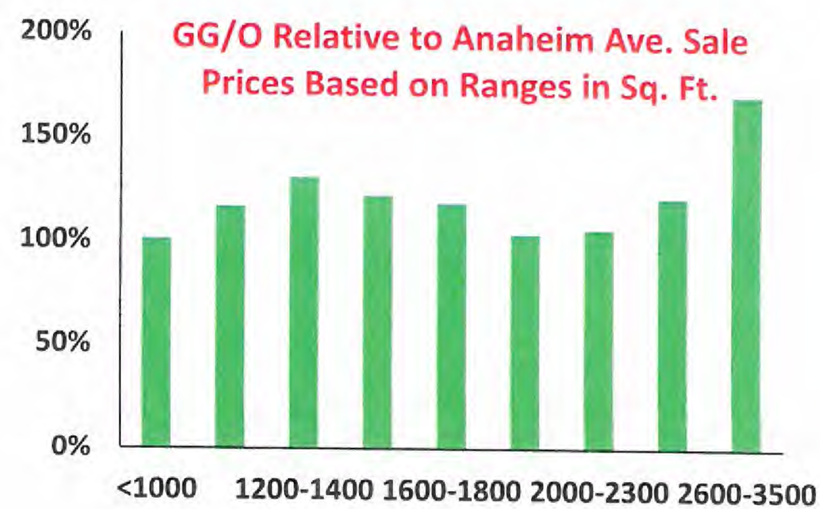
□ Unrecoupable loss calculated as the difference between total initial investment and current estimated fair market value for each property without an STR permit.

□ Total initial investment includes purchase price and all start-up costs.

Replacement Cost Method - See Schedule 11

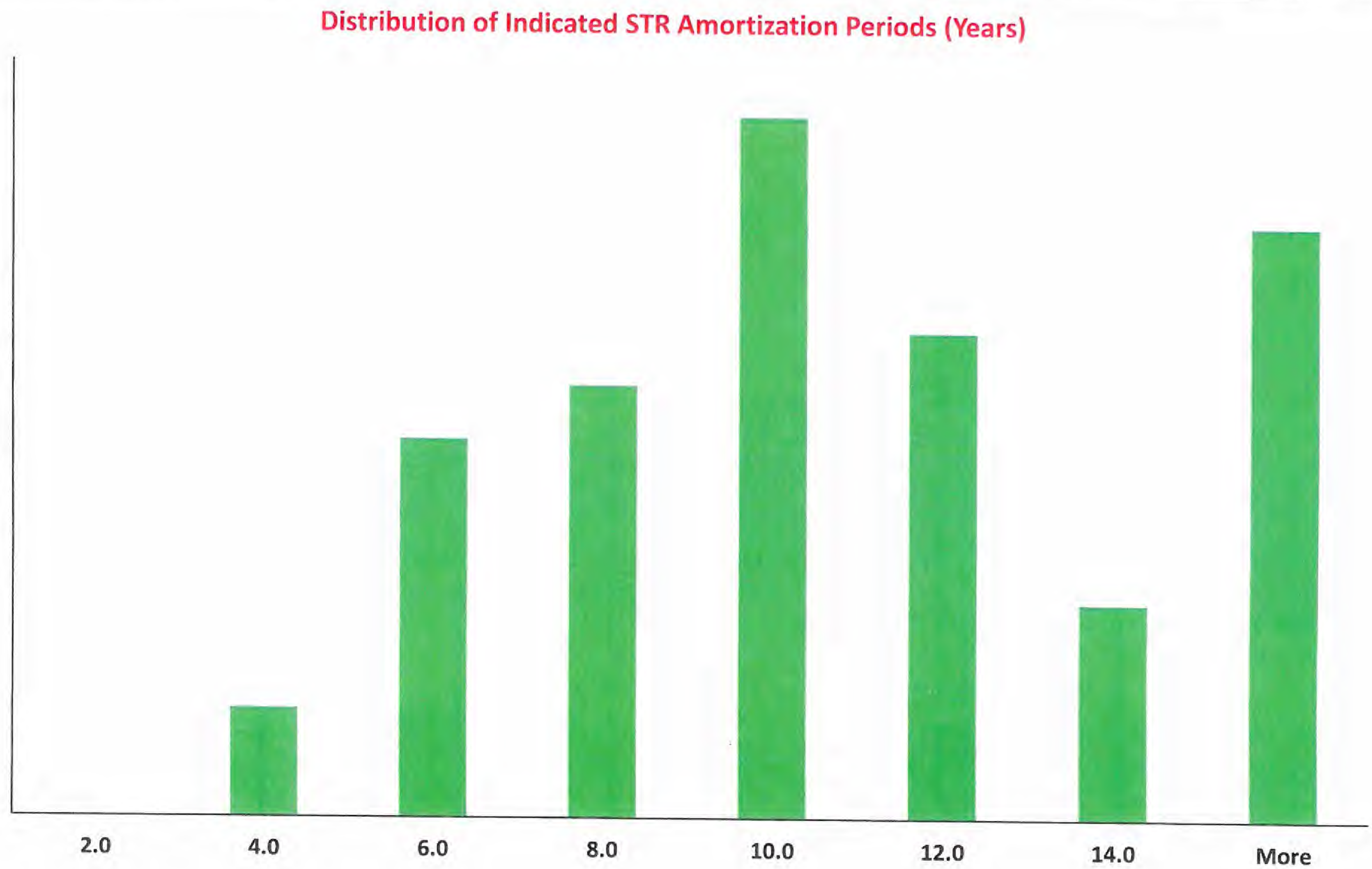
□ Determined cost to buy equivalent replacement property in nearby Garden Grove or Orange by comparing relative median prices for various size properties (see adjacent graph).

□ Unrecoupable cost includes median net property premium of 15% for similar properties in Garden Grove and Orange plus non-transferable start-up costs.



FAIR MARKET VALUE METHOD ASSUMING 25% DECLINE IN STR PROPERTY VALUES DUE TO BAN

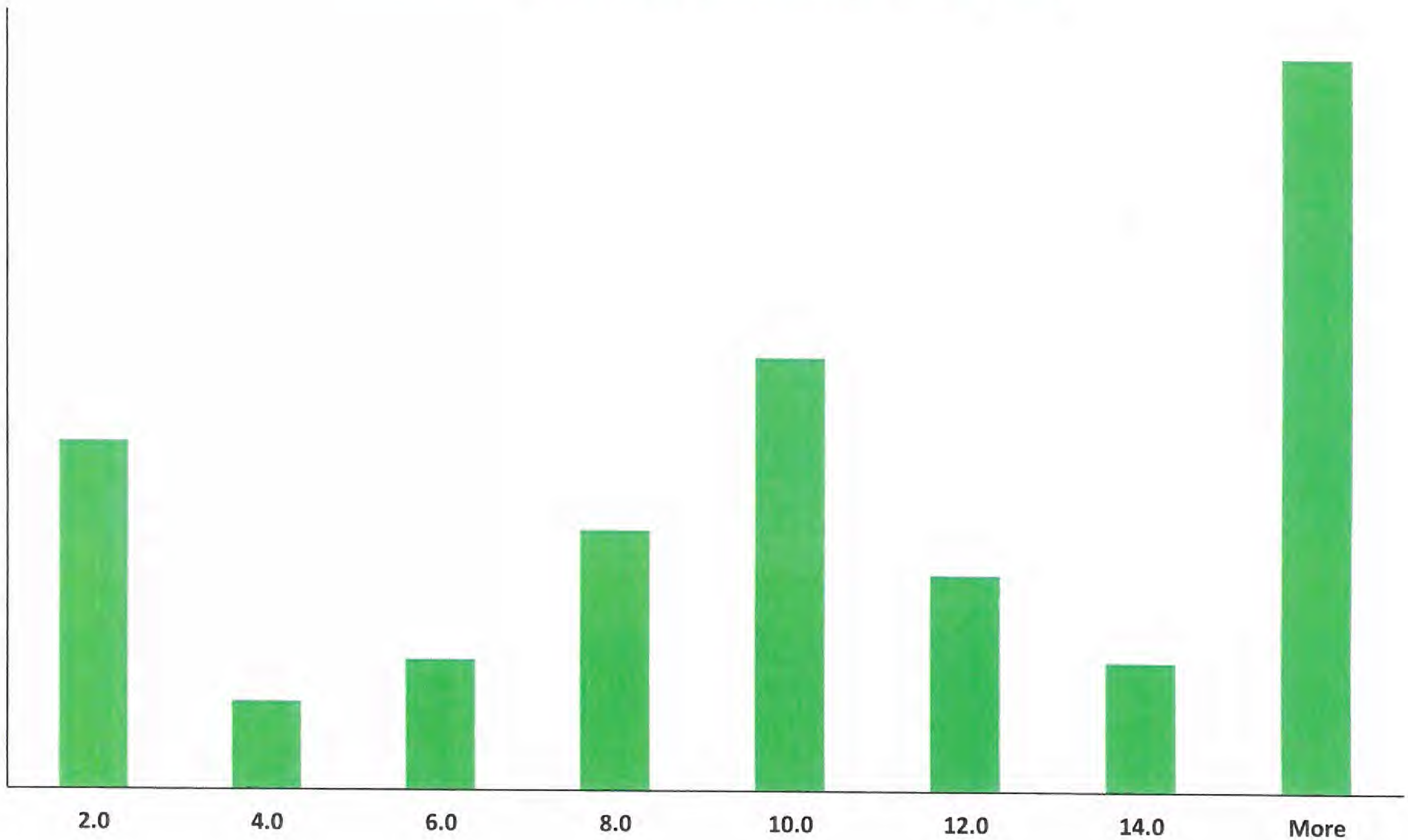
Schedule 9



INVESTMENT BY OWNER METHOD

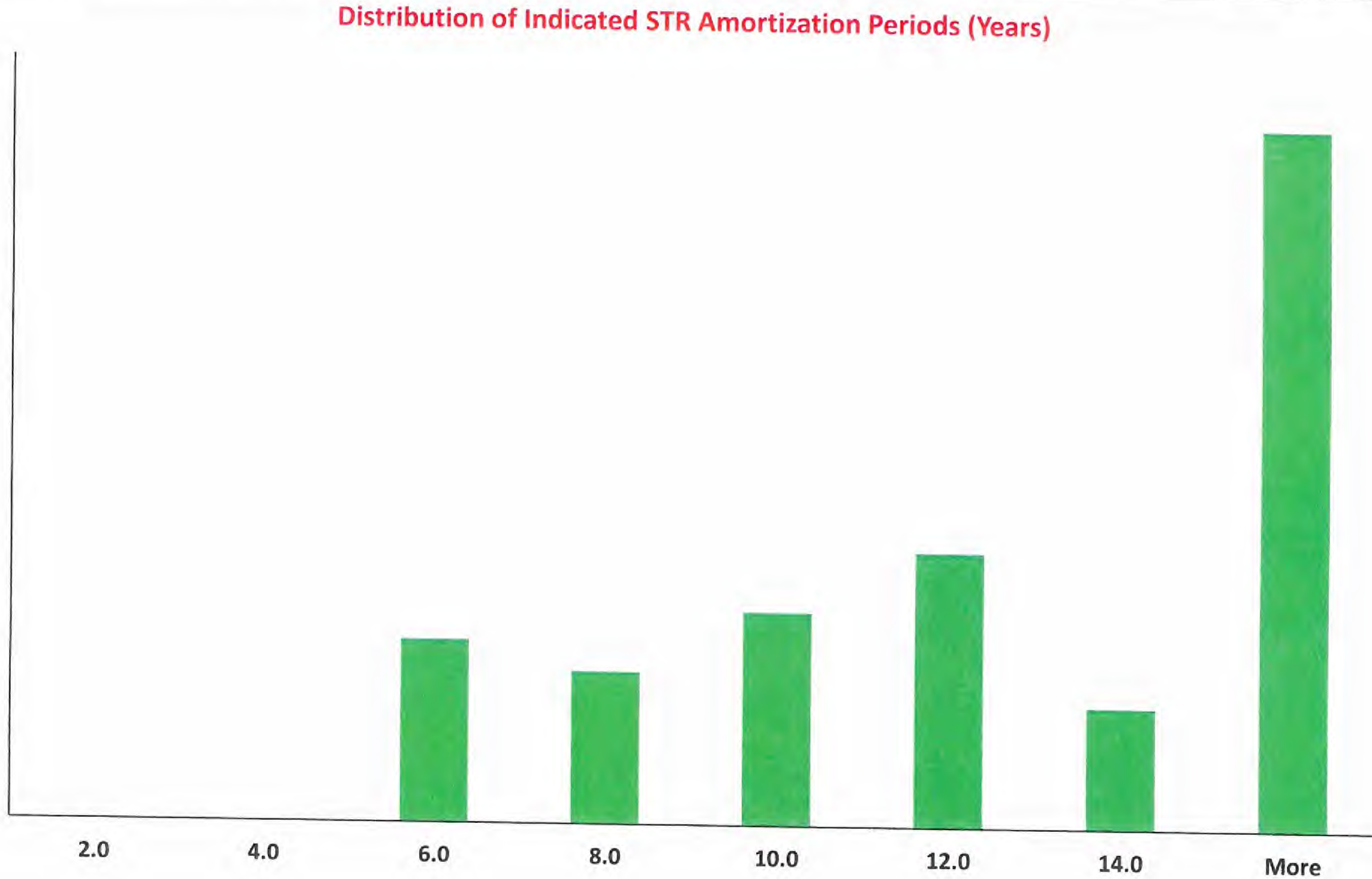
Schedule 10

Distribution of Indicated STR Amortization Periods (Years)



REPLACEMENT COST METHOD ASSUMING MOVE TO GARDEN GROVE/ORANGE

Schedule 11



APPENDIX - LIMITING CONDITIONS

Schedule 12

- □ This report has been prepared for the specific purpose of assessing an appropriate amortization period to compensate owners should STRs be banned in Anaheim. It is intended for no other purpose. Possession of this report, or a copy thereof, does not carry with it the right of publication of all or part of it. It may not be used for any purpose other than the purpose indicated above by any person other than the client to whom it is addressed without written consent of RGL, and in any event, only with the proper written qualifications and only in its entirety.

- □ None of the contents of this report shall be conveyed to any third party or to the public through any means without the express written consent of RGL other than for the stated purpose appearing above.

- □ All facts and data set forth in the report are true and accurate to the best of RGL's knowledge and belief. No investigation of title to property or underlying claims by any individuals or company has been undertaken. Our report is based upon information provided to us. Had we audited or reviewed the underlying data, information may have come to our attention which would have resulted in our using amounts which differ from those provided. Accordingly, we take no responsibility for the underlying data presented or relied upon in this report.

- □ RGL assumes responsible ownership and competent management with respect to the subject assets, properties, or business interests. RGL assumes that there is full compliance with all applicable federal, state, and local regulations and laws unless the lack of compliance is stated, defined, and considered in the report. RGL also assumes that all required licenses, certificates, of occupancy, consents, or legislative or administrative authority from any local, state, or national government, or private entity or organization have been or can be obtained or reviewed for any use on which the opinion contained in the report is based.

- □ No opinion is intended to be expressed for matters that require legal or other specialized expertise, investigation or knowledge beyond that customarily employed by consultants.

- □ Public information and industry and statistical information have been obtained from sources we believe to be reliable. However, we make no representation as to the accuracy or completeness of such information and have performed no procedures to corroborate the information.

- □ We do not provide assurance on the achievability of the results forecasted under the methodologies herein because events and circumstances frequently do not occur as expected; differences between actual and expected results may be material; and achievement of the forecasted results is dependent on actions, plans, and assumptions underlying the analysis.

APPENDIX - OUR BACKGROUND

Schedule 13

RGL Forensics
Discovering & Defining Financial Value

RGL Forensics is a multidisciplinary forensic accounting and consulting firm that delivers accurate and reliable financial analysis in critical situations. Our team spans 25 offices on five continents, with one goal: to provide complete, accurate financial analysis. We serve multinational corporations, global insurance companies, leading law firms and government entities.

For the past 25 years, Hank Kahrs (CPA, ABV, CFF, CFE, CMA, CM) has practiced as a forensic accountant and fraud examiner quantifying economic damages in complex commercial, civil and criminal cases. His career has seen him quantifying IP damages related to images of 1950s Hollywood royalty, working with rock stars in contract disputes, and valuing assets and businesses in diverse industries. Hank has been named as an expert in hundreds of cases and has testified in trial, arbitration and in depositions. He has been retained by over 140 law firms in cases that involve loss of profits, shareholder disputes, real estate, business valuation, lost earnings, fraud, bankruptcy, construction, contract disputes, corporate & partnership dissolution, marital dissolution, asset tracing, workers compensation insurance, embezzlement and intellectual property damages. Hank leads RGL's operations in Southern California. He serves on the Board of Directors of the Coastline Community College Foundation and currently serves as the CFO for the Boys & Girls Club of Tustin in Tustin, California.

Garrett Wilson (CFA, CVA) specializes in the field of business, securities and intellectual property valuation wherein he applies financial, economic and valuation principles to meet a variety of client needs. The scope of his work includes: valuation analyses for financial reporting, tax compliance, asset backed lending, corporate planning and dispute resolution purposes; advisory services including due diligence and financial opinions for mergers, acquisitions and other corporate transactions; litigation support for matters involving securities class actions, commercial damages, marital dissolution, illiquid securities and investment suitability; corporate strategy including benchmarking, strategic alternatives and predictive customer analytics. Garrett began his career at BGI in Kirkland, Washington, where he worked as one of a handful of Investment Specialists managing global investments on behalf of the Bill & Melinda Gates Foundation and Bill Gates, personally. Garrett graduated summa cum laude from Claremont McKenna College with degrees in Economics/Accounting.