Washington Research Council

Special Report

February 29, 2016 SR 16-03

Rent Control

Briefly

Rent control in a city:

- Discourages construction of new rental housing,
- Discourages maintenance of existing rental housing,
- Encourages the conversion of rental housing to owner-occupied housing,
- Reduces tenant mobility,
- Generates mismatch between units and tenants,
- Increases commute times and congestion,
- Reduces the city's property tax base,
- Shifts the burden of city property taxes away from rental housing and onto owner-occupied housing,
- Shifts the burden of regional and state-wide property taxes onto property owners outside of the city.

> *Rent control has in certain western countries constituted, maybe, the worst example of poor planning by governments lacking courage and vision.*

This statement by Nobel laureate Gunnar Myrdal (quoted in Rydenfelt 1971) captures the predominant opinion towards rent control of economists across a broad spectrum of diverse ideological perspectives.

Economists have identified a number of negative effects stemming from rent control. Residential rent control reduces the supply of rental housing by discouraging new construction and encouraging the conversion of rental units to owner occupancy. It discourages maintenance of rental housing, causing housing stocks to deteriorate. It reduces the property tax base. It lowers tenant mobility, generating mismatches between units and tenants. It discourages densification and lengthens commute times.

Within rent controlled cities, local property taxes are shifted away from rental housing onto owner-occupied housing and commercial and industrial properties. Regional and state-wide property taxes are shifted onto property owners outside of the city.

Policymakers have tended to agree. With rare exceptions, rent control has only been enacted in the economic dislocation suffered during 20th century wars or their aftermath.

History

During World War I, rent control in the U.S. was local and mainly of an informal nature. While two rent control bills were introduced in the U.S. House of Representatives in 1918, no action was taken on either of these bills. The federal Bureau of Industrial Housing and Transportation set up "Fair Rent" committees in 82 cities. With membership representing

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landlords, tenants, organized labor, and the general public,

> *for the most part [these committees] had no legal powers and acted through arbitration, conciliation and the use of publicity; but profiteering landlords were also threatened with tax increases, expulsion from real estate boards, enforcement of health and building laws, and even with shutting off of fuel supplies in one city (Willis 1950, p. 69).*

Most of these committees disbanded following the end of the war.

In October 1919, as the nation's economy experienced a turbulent transition from war to peace, the Congress passed the Ball Rent Act establishing a commission to set fair rents in the District of Columbia. This law expired in 1925.

During this same period, the New York State Legislature passed emergency rent control laws for New York City, effective April 1920, which were subsequently strengthened and extended to Albany, Troy, and Schenectady. These laws were narrowed in 1926 and 1928, and finally expired in 1929.

Rent control returned with the economic disruptions occurring shortly after the U.S. entered World War II: President Roosevelt signed the Emergency Price Control Act on January 30, 1942. This act allowed the Office of Price Control to regulate rents in a large number of specified "defense rental areas." The first of these came under control in July of 1942. By January 1945, every city with population greater than 100,000 except for Scranton, Pennsylvania was under control, as well as all but 6 cities with population between 50,000 and 100,000 (Willis 1950). Following the end of the war, most price controls were terminated. Under the Federal Housing and Rent Act of 1947, federal rent controls expired on February 29, 1948 (Willis 1947).

By the early 1950s, New York City was the only local jurisdiction to control rents.

Rent control has in certain western countries constituted, maybe, the worst example of poor planning by governments lacking courage and vision.

—Gunnar Myrdal

The third rent-control wave came in the Vietnam War-related inflation of the 1970s. During this period controls were introduced in Los Angeles, San Francisco, Boston and Washington, D.C. as well as a number of smaller cities in California, Connecticut, Massachusetts, New Jersey and New York. Cities in Washington were spared.

Richard Arnott observes the rent control laws in this third wave differ somewhat from those of World War II:

> *They have been termed variously "soft" rent control, "second-generation" rent control, rent review, and rent regulation. They entail a complex set of regulations governing not only allowable rent increases, but also conversion, maintenance, and landlord-tenant relations. (Arnott 1995)*

In 1977 Seattle did enact an ordinance regulating the rental of moorage space to the owners of houseboats.

In November 1980, Seattle voters resoundingly defeated Initiative 24 (80,587 to 163,140), which would have rolled rents in the city back to their July 1979 levels and then allowed an annual increase tied to inflation. The initiative also would have restricted condominium conversions and made it harder to demolish housing (Gilmore 1980a).

Sharon Feigon, the I-24 campaign coordinator, said on election night, "We will regroup and come out stronger" (Gilmore 1980b). This threat had consequences. Ronald M. Davis of the real estate firm Coldwell Banker was quoted in the Seattle Times the following January,

> *We expect fewer units in 1981 because of high land costs, fear of rent control (despite the 2-to-1 defeat in November, the issue is expected to be back on future ballots), unavailable financing and no economic return for investors because of low rents. (Lane 1981)*

Soon thereafter the state acted, removing the authority of local governments to regulate rents. Substitute House Bill 264 preempting local rent control moved out of the Senate on April 16. It passed the House on April 20 and was signed by Gov. Spellman on May 6.

The governor apparently threatened to veto the bill unless it exempted Seattle's houseboat ordinance (Larsen 1981).

Negative Effects

In a 1946 paper on the post-war housing shortage, Milton Friedman and George Stigler reasoned that rent control reduced the supply of rental housing as the demand for housing boomed in both the rental and owner-occupied markets:

> *The selling price of houses is rising as the large and increasing demand encounters the relatively fixed supply. Consequently, many a landlord is deciding that it is better to sell at the inflated market price than to rent at a fixed ceiling price.*

> *The ceiling on rents, therefore, means that an increasing fraction of all housing is being put on the market for owner-occupation, and that rentals are becoming almost impossible to find, at least at the legal rents. (Friedman and Stigler 1946)*

A recent paper by economist Daniel Fetter documents the effect of rent control on the home ownership during World War II. Looking at a sample of 51 cities, Fetter finds that

> *cities in which rent control was more severe at the time of control (as measured by the degree to which control was meant to lower rents) had greater increases in home ownership ... The estimates suggest that rent control may explain 65 percent of the [7.7 percentage point] urban increase in home ownership over the early 1940's. (Fetter 2013)*

Economists Joseph Gyourko and Peter Linneman found that 7 percent of rent controlled units in New York City were judged to be dilapidated, compared to less than 1 percent of uncontrolled units, and 24 percent of controlled units were judged to be dilapidated, compared to 3 to 4 percent of uncontrolled units.

Gyourko and Linnemen found that New York City families living in rent controlled units had a lower propensity to move (and hence longer tenancy) than families living in uncontrolled units.

Similarly, in a study of rent control in New Jersey, Robert Krol and Shirly Svornoy found that workers living in rent-control cities were less likely to have moved recently than workers living in uncontrolled cities (Krol and Svornoy 2005).

Krol and Svornoy found the workers who commute by car and live in cities with rent controls are more likely to commute longer than 45 minutes than similar workers who live in cities without rent controls. Conversely, those living in rent-controlled cities were less likely to have commuted shorter than 25 minutes than those living in uncontrolled cities.

Gyourko and Linnemen found that New York City's rent controls did not disproportionally benefit the poor.

> *Rent controls in New York City had little if any distributional impact due to the ineffective targeting of benefits. Thus, while many poor families were aided by the rent controls, the same was also true for middle and upper income families. (Gyourko and Linneman 1989)*

David Sims concluded that rent control reduced the economic diversity of Cambridge, Massachusetts:

> *average residents [were] wealthier and less likely to have incomes below the poverty line under rent control (Sims 2009).*

Peter Navaro reports that in Cambridge, Massachusetts the share of housing units that were renter-occupied rather than owner-occupied fell by 9 percentage points from 1970, prior to rent control, to 1980 (Navaro 1985).

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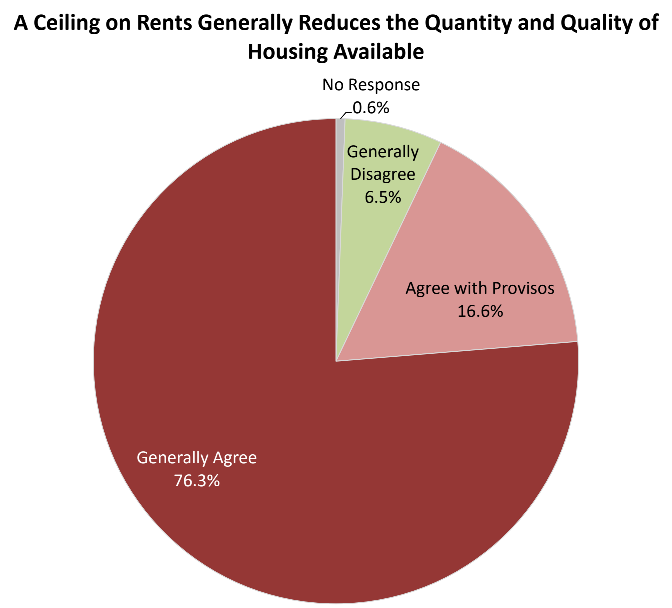
Sims estimated that Boston, Brookline and Cambridge experienced a 6 percentage point increase in the share of housing units that were in the rental market following the end of rent control in Massachusetts (Sims 2007).

A paper by economists David Autor, Christopher Palmer and Parag Pathak demonstrates that rent control can reduce the value of nearby houses that are not subject to rent control. The reason for this is that rent controls reduce the incentive for landlords to maintain and improve their properties. This reduces the attractiveness of neighborhoods with large numbers of rent controlled houses and the market values of uncontrolled houses in these neighborhoods. Autor, Palmer and Pathak estimate that decontrol of rents in Cambridge Massachusetts increased the value of decontrolled houses by 18 to 25 percent and never-controlled houses by 12 percent, adding \$1.8 billion to the market value of Cambridge's residential housing stock in 2004.

Economist Edward Glaeser notes the implication of this for a city's ability to fund services for its residents:

Rent control also has possible impacts on municipal finances, which depend heavily on property taxes. By reducing the value of rental properties, rent control would seem to reduce the tax revenues of the community. Of course, the city could offset this with an increase in tax rates, but that may be difficult for institutional or political reasons. (Glaeser 2012)

Chart 1: Poll Published in the 1992 American Economic Review



Surveys of Economists

Economists are remarkably unified in their opposition to rent control. The breadth of agreement is captured by three surveys.

In 1992 the American Economic Review published the results of a 1990 survey designed to measure the extent to which there is a consensus among economists on issues of theory and policy (Alston et al. 1992). A total of 464 economists participated this survey. The survey presented 40 statements and asked participants to indicate whether they (1) generally agreed, (2) agreed with provisos, or (3) generally disagreed with each.

One of the 40 statements concerned rent control:

A ceiling on rents reduces the quantity and quality of housing available.

This statement elicited a greater degree of agreement from the respondents than any other on the list, with 354 (76.3 percent) generally agreeing and 77 (16.6 percent) agreeing with provisos. (Chart 1.)

The Initiative on Global Markets at the University of Chicago Booth School of Business regularly surveys a national panel of academic economists. In 2012 the IGM panel was presented with this statement:

Local ordinances that limit rent increases for some rental housing units, such as in New York and San Francisco, have had a positive impact over the past three decades on the amount and quality of broadly affordable rental housing in cities that have used them.

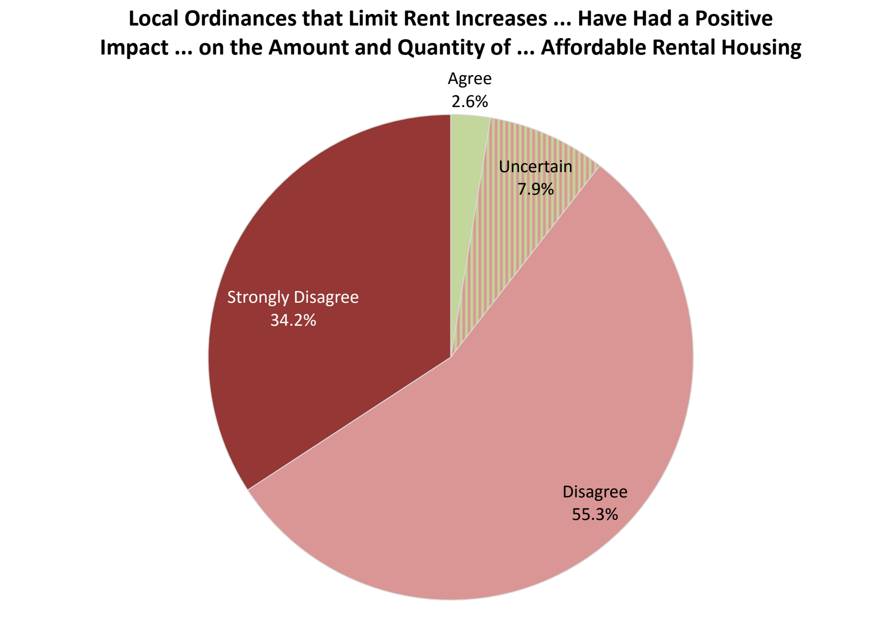


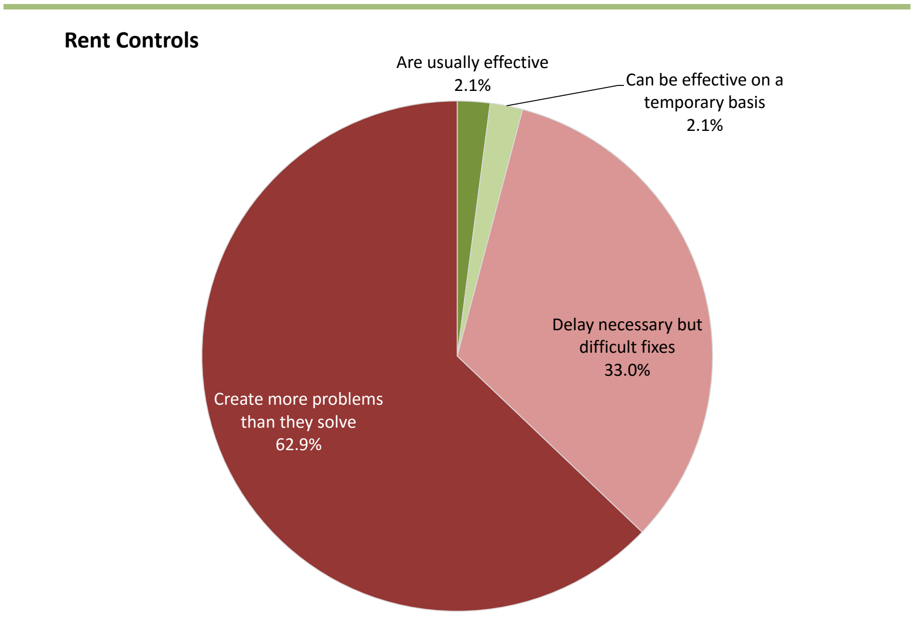
Chart 2: 2012 Poll of IGM Panel

Participants were asked whether they strongly agreed, agreed, were uncertain, disagreed or strongly disagreed. Of the 38 economists who offered an opinion, 21 disagreed (55.3 percent) and 13 (34.2 percent) strongly disagreed. (See Chart 2)

University of Chicago economist Richard Thayer, who disagreed with the statement, added the comment "Next question: does the sun revolve around the earth?"

In the summer of 2015, a survey of economists by Zillow asked panelists to choose among four statements regarding the effectiveness of rent control,

Chart 3: 2015 Zillow Poll



1) *Rent controls are government intrusions into the marketplace that, however well-intentioned, always create more problems than they solve*
2) *Rent control might be effective in resolving an urgent crisis, but should always be a last resort because they serve to delay necessary but difficult fixes to failed urban planning policies*
3) *Rent control can be effective and should be enacted without delay when local government leaders deem them necessary –but strictly on a temporary basis to help resolve an urgent crisis*
4) *Rent controls are usually effective, so they should be a permanent component of any city's overall housing strategy*

Of the 93 respondents expressing an opinion, 61 (63 percent) picked the first statement; 31 (33 percent) picked the second; 2 (2 percent) picked the third and 2 (2 percent) picked the fourth. (See Chart 3.)

Does the Prohibition on Local Rent Control Extend to Commercial Rents?

Substitute House Bill 264, which was enacted in 1981 added sections preempting local enactment of rent controls both to Title 35 (Cities and Towns) and to Title 36 (Counties) of the Revised Code of Washington. The section added to Title 35 (35.21.830) reads:

> *The imposition of controls on rent is of statewide significance and is preempted by the state. No city or town of any class may enact, maintain, or enforce ordinances or other provisions which regulate the amount of rent to be charged for single-family or multiple-unit residential rental structures or sites other than properties in public ownership, under*

> *public management, or properties providing low-income rental housing under joint public-private agreements for the financing or provision of such low-income rental housing. This section shall not be construed as prohibiting any city or town from entering into agreements with private persons which regulate or control the amount of rent to be charged for rental properties.*

The section added to Title 36 (36.01.150) is identical except that "county" replaces "city or town."

The question is whether these sections prohibit cities and counties regulating the rents on commercial properties as well as the rents on residential properties. While commercial properties are not specifically mentioned, the first sentence ("the imposition of controls on rent ... is preempted by the state.") suggests that the prohibition on rent control is general.

In the current edition of the RCW, the sections preempting local rent control in Title 35 and Title 36 are both preceded by the caption:

> *Controls on rent for residential structures – Prohibited – Exceptions*

Seattle Councilwoman Kshama Sawant is a high profile advocate of establishing residential rent control in the city and has advocated that the city lobby the legislature to allow this. Frustrated by the state prohibition, in October Councilwoman Sawant proposed that the city establish rent controls on commercial property, which she claimed is not prohibited by the state law quoted above. At Sawant's behest, the 2016 city budget update adopted by the city council in November included a statement of legislative intent that the city's Office of Economic Development study the feasibility of commercial rent control.

In a post to her blog, Councilwoman Sawant cites the caption, which she incorrectly terms a title, as evidence that the state ban on local rent control does not extend to commercial property.

> *The statewide ban on residential rent control – while undemocratic and exploitative – is so explicit in its focus that it's literally titled "Controls on rent for residential structures – Prohibited – Exceptions." (Sawant 2015)*

However, the caption did not appear in the bill that passed the Legislature as reflected in the volume of Session Laws compiled after the 1981 legislative session. It was written by the Code Reviser (as required by RCW 1.08.015) at the time the sections were folded into the RCW. The caption is not a title, and is not dispositive as to the meaning of the section.

Statewide Significance

Councilwoman Sawant's characterization that the state's preemption of local governments' ability to impose rent control as "undemocratic" is not literally true, of course. The legislators who voted for SHB 264 and the governor who signed this bill were democratically elected. Perhaps what she meant to say is that the costs and benefits of rent control are localized and that therefore local government is the appropriate forum for democratic decision-making about it. However, the Legislature's statement in SHB 264 that local rent controls have statewide significance is a finding that the costs of rent control do extend beyond a locality.

Edward Glaeser notes that the majority of states have laws, like Washington's, precluding local governments from enacting rent control and that an "economic explanation for this state intervention is that rent control imposes costs on people outside the jurisdiction." Glaeser specifically identifies the impact on people "who might want to move to the community but are prevented by the lack of supply of available housing." Under the Growth Management Act it is state policy to concentrate growth in existing urban areas and to allow people to live close to where they work. By reducing the supply of rental property in a city, rent control works against these goals.

Rent Control Shifts the Property Tax Burden

Shifting property tax burdens is another way that rent control may put costs on people outside of the rent controlled market. In many instances a taxing district is allowed to raise a fixed amount of money from its property tax: For example, the amounts of money that cities, counties and the state can raise each year through their regular property tax levy are fixed by the Initiative 747 revenue limit. The tax rate is in these cases is set by local assessors, based on the total value of property to be taxed, so as to raise the specified amount of money. In these cases a reduction in the value of one set of properties will increase the amount of taxes paid by the remaining properties. Thus, when residential rent control reduces the value of rental properties in a city, the effect is (1) to raise the share of city taxes borne by owner occupied homes and commercial properties in the city, (2) to raise the share of county taxes paid by properties in the areas of the county outside of the city, and (3) to raise the amount of state property tax paid by property in areas of the state outside of the city.

Comment

Downtown Seattle is being reborn as a major job center of the 21st century knowledge economy. Rising demand from people working in these high–paying jobs has increased rents and sales prices of nearby housing, disrupting neighborhoods and forcing some lower income residents into long commutes or out-migration. The current housing demand shock, nevertheless, is much less severe those the region experienced during World Wars I and II.

New voices calling for increased government intervention in many sectors of the economy have added the quick fix of rent control as their solution to the growing problem of housing affordability. But rent control is a Band-Aid, not a solution. If the affordability problem is to be solved, the increase in demand must be met by an increase in supply. As rent controls would discourage the construction of new rental housing, they would make the affordability problem worse in the longer term.

Policymakers, taking heed to the vast majority of economists and the basic nature of market behavior, have resisted the call for rent controls. They would be wise to look to policies that would remove unnecessary regulatory impediments to an increase in the supply of housing, to counter balance the demand pressures driving up rents and property values.

Policymakers should also carefully consider allowing cities to provide property tax exemptions for private landlords who commit to income and rent restrictions in existing buildings, as recommended by Seattle Mayor Ed Murray's HALA Advisory Committee (HALA 2015). Voluntary agreements of this sort are not prohibited by RCW 35.21.830.

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