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Rent Control - Is the Cure Worse Than the Disease?

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POLICY BRIEF

Rent Control—Is the Cure Worse Than the Disease?

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BRIEF HIGHLIGHTS

- *Rent control is common in coastal cities, but can take many complex forms.*
- *Evictions from rent-controlled apartments tend to rise in booms and fall in busts.*
- *Research shows that rent control incentivizes landlords to at least temporarily withdraw housing in response to price increases—the opposite of what policymakers intend.*
- *Rent control is unlikely to be a standalone solution to the underlying problem plaguing expensive cities: chronic undersupply of housing.*

For additional details, see the working paper, "Do Rent Increases Reduce the Housing Supply under Rent Control? Evidence from Evictions in San Francisco," published by the Upjohn Institute. https://doi.org/10.17848/wp19-296.

After a long period of neglect, a new generation of policymakers and activists has embraced rent control as a solution to the housing affordability crisis plaguing America's booming coastal cities. The national median rent for a one-bedroom apartment is $1,209 a month, but for some metro areas it is considerably higher. Urban residents suffering from the highest rents are mostly in wealthy, coastal cities, such as San Francisco ($3,500), New York City ($2,860), San Jose ($2,480), Los Angeles ($2,360), Oakland ($2,100), and Washington, D.C. ($2,160). In addition to sharing astronomically high rents, these cities also share another feature: rent control.

Rent-control regimes have operated in these six cities for the better part of 30 years, and they exist also in a host of smaller cities, chiefly in California, Maryland, and New Jersey. Undergraduate Economics 101 would have you think that rent control is essentially a rent freeze, but the reality is that rent control as practiced today has evolved into a far more complex system. The vast majority of today's rent controls were instituted in the 1970s and early 1980s in response to the stagflation crisis, and are often referred to as rent stabilization, tenancy rent control, or second-generation rent control to distinguish themselves from their much-maligned predecessor. Since these modern forms are really the only game in town, I refer to them herein as just rent control.

Policymakers claim that rent control can allow low- to moderate-wage workers to live close to jobs in expensive cities. They also claim that these rent-control policies would prevent families from being displaced by high rents into substandard housing. Even for families who stayed, the rent controls would mean that they could more easily afford other necessities, like food and health care. This concern applies particularly to low-income or fixed-income households, such as the elderly and disabled. For example, Oakland's rent control ordinance claims to address a "severe housing affordability crisis," in which "60 percent of . . . residents are renters, who would not be able to locate affordable housing within the city if displaced."

The regimes share four prominent features:

1) The city grants landlords and tenants some freedom to negotiate a starting rent, and then caps subsequent rent increases according to agency decree or prescribed formula. This process, called vacancy decontrol, ranges from restrained in New York City and Washington, D.C., to completely unrestricted in California.
2) There is automatic lease renewal for existing tenants, and landlords usually require "just-cause" to evict a tenant. In practice, this means that landlords must prove to a rent board or court that tenants are being evicted for one of a predetermined list of reasons. This prevents landlords from turning over tenants at will and locking in new base rents in response to market shifts.
3) New buildings are exempt from rent control unless the landlord opts in. Policymakers fear discouraging new supply, so the rules control only existing buildings and commit to not extending controls further.

Economics 101 would have you think that rent control is essentially a rent freeze, but the reality is that rent control as practiced today has evolved into a far more complex system.

4) There are a series of landlord hardship provisions, where landlords may petition to pass certain operating expenses on to tenants in order to cover costs with reasonable profit.

Table 1 shows how the details vary across cities, but it also underscores how these systems share more policy similarities than differences.

These measures were largely intended to be temporary, but like many so-called temporary regimes, rent control is the answer to an emergency situation that never seems to end. One reason for rent control's persistence is that it redistributes benefits from future tenants to present ones. One influential study found that, after rent control was expanded to a new set of apartments in 1994 in San Francisco, tenants in affected buildings were 10–20 percent more likely to remain at their 1994 address compared to tenants in the control group. Since rent increases are capped at less than the rate of inflation, these tenants were (and in some cases still are) effectively being subsidized to live in their controlled apartments for as long as they like. This creates a powerful pro-rent-control constituency that can be difficult for reform-minded policymakers to overcome.

This de facto subsidy to stay in place affects tenants' labor market outcomes. One study shows that tenants absorb longer commutes instead of yielding their rent-controlled apartments, suggesting that keeping the subsidized housing is more valuable to them than moving closer to a new job or switching job markets altogether. Another study concluded that the stronger the local rent-control ordinance, the more likely a person was to limit their job search to local jobs. While rent control may allow workers to stay close to high-wage jobs in dense urban areas, it is not altogether clear that this is in the best interests of tenants or the economy in the long run.

Table 1 Major City Rent Control and Evictions Policies, October 2016

City	Subject to controls if the building is...	Max annual allowable rent increase	Vacancy decontrol?	Just-cause evictions?	Rental stock coverage (%)
Los Angeles	Built before 10/1/1978 and has 2 or more units	Regional CPI rate, bounded within 3–8%	Yes	Yes	85
Oakland	Built before 1/1/1983 and has 4 or more units	Regional CPI rate, max of 10%	Yes	Yes	66
New York City	Built before 1/1/1974 and has 6 or more units	Set by NYC rent guidelines board annually	No, rent increase for new base rent capped at 20%[a]	Yes	47
San José	All rental units built before 9/7/1979	Previously 8% 6/2016-: 5%	Yes	No, city-mandated arbitration instead	33
Washington, DC	An apartment building built before 1/1/1976	CPI + 2%, max of 10%	No, rent increase for new base rent capped at 10%	Yes	66
San Francisco	Built before 6/13/1979 and has 2 or more units	60% of CPI, max of 7%	Yes	Yes	72

a In both cities, landlords can appeal for a rent increase on new base rents of up to 30% if rents in comparable units are shown to be higher.

NOTE: See Asquith (forthcoming) for detailed sources.

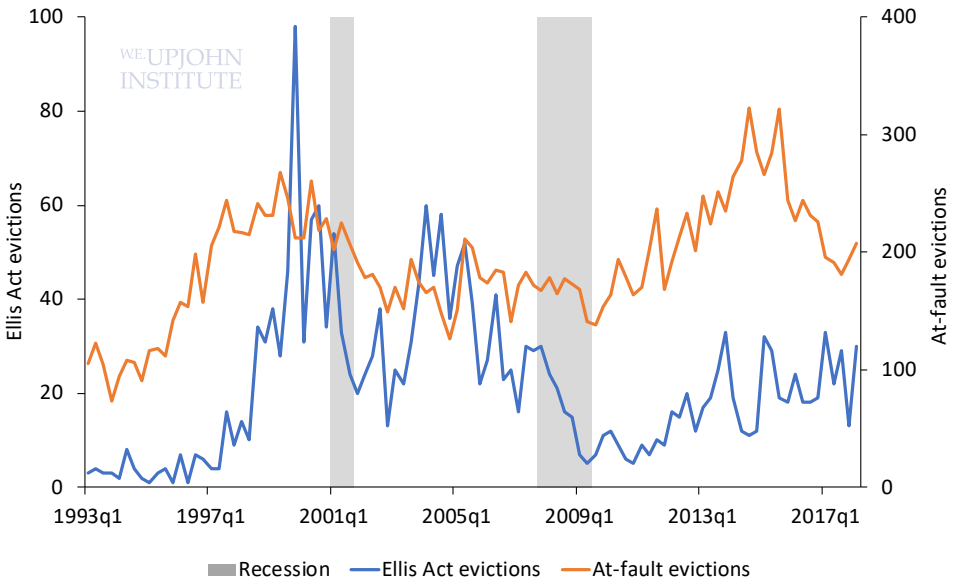
The evidence suggests that landlords of rent-controlled apartments are *less* likely to turn over their tenants when prices rise.

Rent control's distortionary effects also extend into housing supply. The policies in Table 1 collectively dampen landlords' profits in the controlled market. In the case of San Francisco, landlords actually lose money since rent increases are capped at 60 percent of the inflation rate. In growing markets, the gap between what a landlord receives from a controlled apartment and from one that allows increases at the market rate compounds over time. Because tenants in this situation have strong incentives to stay longer under rent control, landlords in turn try to avoid tenants they suspect will be "long-stayers."

My own research asks: How do landlords of rent-controlled properties change their housing supply when prices rise? Do they bring more units to market? Or, in San Francisco, at least, have policymakers imposed such burdens on landlords that they actually remove properties from the market? To motivate this question, Figure 1 shows evictions by quarter in San Francisco. The left axis shows Ellis Act evictions, by which landlords evict all tenants and withdraw an entire building from the market. Ostensibly, this occurs when landlords no longer want to operate their buildings, and so one might expect these evictions to rise when the economy slumps and vice versa. Instead, Ellis Act evictions spike during booms and fall during recessions. The right axis shows "just-cause" at-fault evictions, mostly tenants being evicted for delinquent rent. Since tenants in the controlled market are insulated from price increases during booms, one might expect this type of eviction to rise during recessions as tenants' ability to pay falls. Instead, like Ellis Act evictions (albeit less sharply), at-fault evictions seem to rise in boom periods and level off in recessions.

These relationships suggest that landlords try to evade rent control restrictions when it would be especially profitable to do so, such as by converting rental units to condominiums. To test this hypothesis more definitively, I examine how two outcomes respond to market price increases that affected San Francisco neighborhoods differentially between 2003 and 2013. The first outcome is whether landlords tactically evict individual tenants to try to lock in higher rents from new tenants. More specifically, do landlords use just-cause evictions to expel long-standing but lower-paying tenants? In spite of the pattern in the graph, I find no statistically significant evidence that landlords do this. Instead the evidence suggests that landlords of rent-controlled apartments are *less* likely to turn over their tenants when prices rise.

Figure 1 Evictions in San Francisco, 1993Q1–2018Q1



SOURCE: Author's calculations from data provided by the San Francisco Rent Board and Kate Pennington, University of California, Berkeley.

The other outcome is whether controlled landlords outright exit the market in response to a price increase. I find that landlords do in fact respond to rising prices by withdrawing from the rental market via Ellis Act evictions (or, in smaller buildings, by withdrawing one unit from the market by claiming a relative needs to move in). This is a serious response, because by law the landlords must pay relocation fees and leave these units vacant (or filled by a family member) for at least three years or be subject to sanctions.

The two results confirm that the controlled market is distorted compared to "normal" housing markets. Landlords apparently expect to make such little money on the controlled market that they conclude it's better to exit the market entirely, at least for a few years. If these landlords are thus incentivized to *reduce* supply as prices rise, it is hard to see how rent control improves housing market dynamics in these cities.

So, if existing evidence is that rent control is distortionary, why not abolish it? We have some evidence on what happens when rent control is repealed, and the result is generally salutary (see, for example, Autor, Palmer, and Pathak 2017). In January 1995, a Massachusetts law banned rent controls, mostly affecting units in Boston, Cambridge, and Brookline. Property values in both decontrolled and never-controlled units rose, while property crime fell, especially in areas with the highest concentration of controlled units. Additionally, segregation may have decreased.

However, the evidence is not clear on whether low- and middle-income tenants in fact would have been better off without rent control. So, what are other remedies to help these groups with housing costs? Government programs have included Section 8 housing subsidies, low-income housing tax credits to finance new housing, and more recently, affordable housing mandates. These programs offer some help, particularly to poorer renters, but generally do little to address the housing needs of middle-income residents facing excessive rent burdens in expensive cities. Rent control's lack of means testing is thus a political strength, because it can claim to be the rare policy that helps middle-income renters as well.

Despite popular demands for government intervention on rents, economists typically advocate for increasing the housing supply. Frustratingly, there is little empirical evidence on what happens to rent prices when the number of housing units in a neighborhood rises, with one study suggesting prices may not move much. Upjohn Institute economist Evan Mast, Philadelphia Fed economist Davin Reed, and I are currently studying this issue using data on unit-level migrations, rents, and building openings.

Irrespective of the ultimate answer, rent control is here to stay. The current beneficiaries are well-organized, numerous, and know what they stand to lose from its repeal. The return of rent control to the scholarly agenda is thus propitiously timed to caution policymakers and a frustrated public that while soaring rent burdens are indeed approaching crisis levels in some places, rent control is a policy that has yet to deliver on its promise: affordable rents for all, not just for the few lucky enough to score a controlled apartment.

NOTE

1. Oakland rent control ordinance. https://oakland.legistar.com/LegislationDetail.aspx?ID=2680738&GUID=BAED7BF3-ED56-4A16-A876-37717D4E01D6&Options=&Search= (accessed January 11, 2019).

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