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IS RENT CONTROL GOOD SOCIAL POLICY?

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Rent control has been a major type of governmental housing regulation throughout the world for many years.[1] In the United States, it has been the exception rather than the rule. It existed throughout the country during and immediately after the Second World War, but by the early 1950s it had been abandoned almost everywhere. During the remainder of the 1950s and 1960s, it existed only in a few cities in the State of New York, most notably New York City. There was a resurgence of rent control during the 1970s and early 1980s when rates of inflation were high. Over 200 localities in the United States currently have some form of rent regulation, and more than ten percent of all rental units are subject to rent control. Controls now exist in six states (California, Connecticut, Maryland, Massachusetts, New Jersey, and New York) and the District of Columbia. New York City accounts for thirty-nine percent of all rent controlled units; Los Angeles, seventeen percent; San Francisco, seven percent; and Washington, D.C., four percent.[2]

Sound housing policy requires an understanding of the consequences of any phenomenon which affects so much of the American housing stock and so many individual housing markets. The purpose of this paper is to consider whether rent control is good social policy based in part on the best available evidence concerning its justifications and effects.

It is important to recognize at the outset that different rent control ordinances have different provisions and these differences can lead to dif-

* Professor of Economics, University of Virginia. Tulane University, B.A., 1963; Rice University, Ph.D., 1968. I want to thank Bob Ellickson for encouraging me to read some of the legal literature on rent control and for providing me with excellent references. Although Epstein (1988, 1989) has done a superb job of conveying some of the main economic insights concerning the desirability of rent control, Ellickson correctly perceived that someone with a more detailed knowledge of the technical economic aspects of housing markets and the effects of rent control would be able to fill a gap in the legal literature. Time constraints have limited the extent of my reading of the legal decisions and writings on rent control. However, I suspect that the papers that I have read contain the most common arguments and that this paper does bring what economists know to bear on these arguments.

1. For a description of rent control ordinances outside of the United States, see STEPHEN MALPEZZI & GWENDOLYN BALL, RENT CONTROL IN DEVELOPING COUNTRIES (World Bank, 1991) DISCUSSION PAPER 129.

2. U.S. DEP'T OF HOUS. & URB. DEV., OFF. OF POLICY ANALYSIS & RES. REPORT TO CONGRESS ON RENT CONTROL, GPO Document number 312-228/41023. Table 2 (1991) [hereinafter HUD].

ferent results.[3] For example, almost all jurisdictions automatically increase the ceiling rent each year, some by a fixed percentage and others by a fraction of the increase in the Consumer Price Index. However, these percentages and fractions differ greatly across localities. Los Angeles allows one hundred percent of the increase in the CPI; Berkeley only sixty-two percent. Some jurisdictions with rent control allow rents to be increased for new tenants without limit, others limit the increase, and still others allow no increase. If landlords are allowed to set rents freely when units turn over, it is to be expected that rent control will not lead to any substantial transfer of wealth from owners of rental housing to their tenants. Instead it will lead to higher initial rents and a slower rate of increase in rents for sitting tenants. Thus the transfers will be from tenants who move frequently to those who seldom move. The Los Angeles ordinance has this feature, and the major studies of it support this conjecture.[4] The best estimate of the more recent study is that rent control has lowered the mean rent in Los Angeles by seven dollars per month but that it has increased the mean rent of those who have been living in their apartment one or two years by twenty-eight dollars per month.[5]

The available evidence suggests that the majority of ordinances in the United States today have little effect on rents and hence do not, to any great extent, have the ill effects often attributed to rent control.[6] There is little to be said for such ordinances. An administrative cost is incurred to produce a small amount of haphazard redistribution. Since proponents of rent control usually argue that these ordinances should be made more stringent in order to have the effects that they desire, this paper will focus on the desirability of more restrictive laws.

Attempts to justify rent control in the legal literature leave much to

3. For a description of some of the ordinances in the United States, see Kenneth K. Baar, *Guidelines for Drafting Rent Control Laws: Lessons of a Decade*, 35 RUTGERS L. REV. 723, 756-841 (1983); HUD, *supra* note 2, at 43-63.

4. C. PETER RYDELL ET AL., THE IMPACT OF RENT CONTROL ON THE LOS ANGELES HOUSING MARKET (1981); Hamilton et al., The Los Angeles Rent Stabilization System: Impacts and Alternatives (April, 1985) (prepared for the Rent Stabilization Division of the Community Development Department of the City of Los Angeles).

5. Hamilton et al., *supra* note 4, at Exhibits 2-12.

6. Richard P. Appelbaum & John I. Gilderbloom, *The Redistributional Impact of Modern Rent Control*, 22 ENV'T & PLAN. A. 601 (1990). ANTHONY DOWNS, RESIDENTIAL RENT CONTROL: AN EVALUATION (1988). John I. Gilderbloom, *Moderate Rent Control: Its Impact on the Quality and Quantity of the Housing Stock*, 17 URB. AFF. Q. 123 (1981). John I. Gilderbloom, *The Impact of Moderate Rent Control in New Jersey: An Empirical Study of 26 Rent Controlled Cities*, 7 URB. ANALYSIS 135 (1983); John I. Gilderbloom, *The Impact of Rent Control on Rent in New Jersey Communities*, 71 SOC. & SOC. RES. 11 (1986); Hamilton et al., *supra* note 4; C. PETER RYDELL ET AL., *supra* note 4. For a critical analysis of these and other studies of rent control, see Edgar O. Olsen, *What is Known about the Effects of Rent Control?* (September 1990) (prepared for the Office of Policy Development and Research of the U.S. Dept. of Housing and Urban Development).

be desired. Keating[7] asserts that housing is a fundamental right, but he does not tell us to what type of housing people have a right and why. He also offers the usual popular arguments for housing subsidies to low-income households, namely "the declining stock of affordable housing and the increasing number of tenants, millions, mostly poor, living in substandard housing and paying very high proportions of their income for rent."[8] Since existing studies suggest that housing subsidies to low-income households and rent control have the exact opposite effect on consumption patterns, it is difficult to understand how they can have the same justifications.[9] Furthermore, it is not clear why all of the phenomena mentioned are considered problems. If low-income households decided to place a higher value on housing (that is, to spend a higher proportion of their income on it), the housing stock would be upgraded and the stock of affordable housing as usually measured would decline. Keating does not explain why this would be bad. Dobkin says that "[r]ent controls are necessary to protect people who through no fault of their own would otherwise be priced out of decent housing."[10] There are several problems with this argument. First, rent control is not limited to people who are priced out of decent housing. The majority of renters are not poor, and the majority of low-income renters live in adequate housing.[11] Second, rent control is not necessary to attain this end since it could also be achieved by providing households that are priced out of decent housing with housing subsidies financed by broad-based taxes. Finally, we might ask why people should be protected from this outcome.

If what underlies the preceding arguments for rent control is simply a concern about the well-being of certain people, this should be stated. Since the appropriate policy response to this concern depends on whether the concerned believe that the objects of their concern know what is good for themselves, it is important to take a stand on this issue. If we believe that others are the best judges of their own well-being, then unrestricted

7. Dennis W. Keating, *Commentary on Rent Control and the Theory of Efficient Regulation*, 54 BROOK. L. REV. 1223, 1226 (1989).

8. *Id.* at 1224 (citing NATIONAL HOUS. TASK FORCE, A DECENT PLACE TO LIVE (1988)).

9. Housing subsidies such as public housing and Section 8 typically induce participants to occupy better housing than they would choose if given equally costly cash grants. *See, e.g.*, Edgar O. Olsen & David M. Barton, *The Benefits and Costs of Public Housing in New York City*, 20 J. PUB. ECON. 1983; William J. Reeder, *The Benefits and Costs of the Section 8 Existing Program*, 26 J. PUB. ECON. 349 (1985). Occupants of controlled units typically live in worse housing than they would choose if given equally costly cash grants. Edgar O. Olsen, *An Econometric Analysis of Rent Control*, 80 J. POL. ECON. 1081 (1972).

10. Stephen Dobkin, *Confiscating reality: The Illusion of Controls in the Big Apple*, 54 BROOK. L. REV. 1249, 1249 (1988).

11. Kathryn P. Nelson & Jill Khadduri, *To Whom Should Limited Housing Resources Be Directed?*, 3 HOUS. POL'Y DEBATE, Table 1 (1992).

cash grants should replace other types of transfers such as rent control.[12] Housing subsidies are appropriate if some altruists believe that the objects of their concern undervalue housing and none believe that they overvalue it.[13]

In stark contrast with the many superficial attempts to justify rent control is Radin's detailed analysis.[14] It is impossible to convey the richness of her arguments here. However, the essence of her justification for rent control might be summarized as follows. People care about the identities of their neighbors, and they feel a loss when a long-time neighbor moves. In the jargon of economics, an externality is involved here. According to her argument, rent control is justified because it reduces mobility and hence ameliorates the externality.

One might question the importance of this explanation regarding the existence of rent control ordinances. If this justification is important, the residents of New York City must surely be the most neighborly in the country since they adopted rent control long before other cities. More fundamentally, Radin does not explain why rent control is superior to obvious alternative policies. For example, why is it better than imposing a tax on those who move each year and distributing the proceeds to those who stay? This will reduce mobility without the ill effects of rent control.

The failure to consider alternative means to a desirable end, such as helping the poor, is a persistent shortcoming of arguments for rent control in the scholarly literature. If everyone would prefer some other program to rent control, then it can hardly be argued that rent control is good social policy. To concede, as proponents of rent control usually do, that rent control involves inefficiencies is to concede that it leads to an inefficient allocation of resources.[15] By definition, an allocation is inefficient if and only if there exists a *feasible* alternative allocation preferred by everyone. This means that there exists an alternative program that everyone would prefer to rent control. Specifically, we could have imposed a proportional tax on the value of rental property owned on the date to which rents were initially rolled back under rent control. The tax rate could have been set so that the tax paid by each landlord is slightly less than the reduction in the market value of his rental property result-

12. Edgar O. Olsen, *The Simple Analytics of the Externality Argument for Redistribution, in* 2 ECONOMIC PERSPECTIVES: AN ANNUAL SURVEY OF ECONOMICS 156-59 (M.B. Ballabon ed., 1981).

13. *Id.* at 159-70.

14. Margaret J. Radin, *Residential Rent Control*, 15 PHIL. & PUB. AFF. 350 (1986).

15. In economic terminology, an allocation of resources does not simply refer to how much of each input is used to produce each good and service. It refers to how much of each good and service is consumed by each person and how much of each good or service is supplied by each person.

ing from rent control. The proceeds of the tax on each building could have been distributed among the tenants in proportion to their rents at that time. The general principle here is that we never want to adopt a program when we can easily think of an alternative program that is better for everyone.

To justify a government program, it is not enough to explain why selected effects are desirable, for example, why we should help some of the people who benefit from it. To justify a government program, you must be able to justify all of its effects. It is necessary to explain why money should be taken from those who bear its costs and why it should be given to those who directly benefit. It is necessary to justify the distribution of the benefits and costs of the program, that is, who gets large and who gets small benefits and who bears large and who bears small burdens. Finally, it is necessary to justify the form of the taxes and subsidies. This paper addresses each of theses issues.

1. Why Should Benefits to Tenants Be Financed by an Implicit Tax on Landlords?

The burden of rent control is borne primarily by those who own rental housing at the time that it becomes widely known that a rent control law will be adopted or modified in a way unfavorable to landlords.[16] This will be reflected in a decline in the prices for which affected rental units can be sold. The primary beneficiaries are tenants who occupy units at the times when these changes occur.[17]

Why should benefits to tenants be financed by an implicit tax on landlords? It is clear that some people who do not expect to occupy controlled housing support rent control because they believe that owners of

16. Landlords who buy rental property after rent control is adopted do not bear a burden unless the ordinance is *unexpectedly* changed to their disadvantage.

17. It is less clear whether tenants who move into these units later benefit because they often pay bribes and incur extra search costs to obtain possession of the unit. With one exception, attempts to estimate the benefits of rent control to such tenants ignore both as well as tenant expenditures on maintenance and improvements. *See* Richard Ault & Richard Saba, *The Economic Effects of Long-term Rent Control: The Case of New York City*, 3 J. REAL EST. FIN. & ECON. 25 (1990); Joseph Gyourko & Peter Linneman, *Equity and Efficiency Aspects of Rent Control: An Empirical Study of New York City*, 26 J. URB. ECON. 54 (1989); Peter Linneman, *The Effects of Rent Control on the Distribution of Income Among New York City Renters*, 22 J. URB. ECON. 14 (1987); Olsen, *supra* note 9; Edgar O. Olsen & Kathy A. York, *The Effect of Different Measures of Benefit on Estimates of the Distributive Consequences of Government Programs*, *in* ECONOMIC TRANSFERS IN THE UNITED STATES (Marilyn Moon ed., 1984). In a study of Cairo, Egypt, Malpezzi estimates that the average controlled rent is sixty-two percent below the average market rent of controlled units. However, when side payments and tenant maintenance and improvements are added to the controlled rent, the discount is only thirty percent. MALPEZZI & BALL, *supra* note 1, at 41-42.

rental housing make excess profits and they view rent control as a way of returning these excess profits to tenants.

The discussion of this issue often fails to distinguish between two very different situations. Most commonly, the discussion concerns a situation in which a large unexpected increase in demand for housing in an area results in higher rents and excess profits.[18] This can happen even if the housing market is perfectly competitive. If the housing market is perfectly competitive, excess profits during some periods will be offset by deficient profits in others. Over their entire lives, some buildings will yield higher returns than others due to mistaken expectations on the part of their owners. However, the typical project will earn a competitive rate of return. Such fluctuations in returns provide no good argument for rent control. On the contrary, we want more housing to be provided in this area and the excess profit that can be earned in the short-run provides the incentive for suppliers to do it. If we prevent excess profits by instituting rent control, will anyone have an incentive to provide more housing in the area?

The situation is quite different if excess profits are due to a monopolized housing market. If suppliers of rental housing successfully collude to set prices and prevent entry, they will consistently earn excess profits. If monopoly power is substantial enough, then the government with all its imperfections might be able to improve the situation using rent control.

The belief that landlords make excessive profits is not supported by any systematic evidence and few economists share this view.[19] The majority of economists believe that easy entry into the rental housing business precludes a greater than competitive rate of return on the typical investment.

Two empirical regularities well-known to housing economists argue against certain extreme views concerning the monopoly power of landlords. First, it is well documented that if the rents of units of all types

18. In this situation, the goal of rent control is sometimes described as protecting tenants from opportunistic exploitation by landlords. This characterization of the response to an unexpected increase in demand is an obvious attempt to persuade people to support a particular government policy by the use of loaded words rather than by a serious analysis of the situation. Would proponents of rent control who use this argument agree that landlords are being opportunistically exploited by tenants when rents fall in response to a precipitous decrease in demand resulting from the closing of a military base in a small town?

19. Some advocates of rent control argue explicitly that housing markets are not competitive, and some cite an empirical study by two sociologists in support of this proposition. Keating, *supra* note 7, at 1228-29 (citing JOHN I. GILDERBLOOM & RICHARD P. APPELBAUM, RETHINKING RENTAL HOUSING 57-67 (1988)). It remains to be seen whether this study can withstand the scrutiny of economists.

were increased by the same percentage from prevailing levels, renters would ultimately occupy less desirable units and would spend more on housing.[20] If landlords could collude to set rents, they would have charged higher rents because this would have resulted in greater revenue along with less expenditure on maintenance. Second, it is equally well documented that sitting tenants pay lower rents than new tenants for identical units.[21] This argues against the widespread belief that landlords have market power over sitting tenants due to the out-of-pocket and psychic costs of moving.

Housing economists have made few attempts to calculate rates of return on rental housing and to compare them with returns on other types of investment, but they have provided indirect evidence in support of their views by deriving and testing implications of models of competitive housing markets.[22] Generally speaking, the empirical evidence supports the view that housing markets are competitive. One problem with this type of evidence is that it is extremely difficult to convey to a nontechnical audience. Direct evidence would be more persuasive provided that the underlying data could be collected in a way which casts little doubt on its credibility.

A superficially appealing explanation of why benefits to tenants should be financed by an implicit tax on landlords is that the average income of landlords exceeds that of their tenants and therefore these transfers have the same justifications as other redistributive programs such as public housing, food stamps, medicaid, and AFDC.

The only available information on the distribution of income among owners of controlled units comes from Arthur D. Little's survey of the 1984 incomes of owners of rent stabilized units in New York City.[23] Table 1 reports the results. This table should be compared with Table 2, which shows the distribution of income among occupants of stabilized apartments. This evidence supports the view that the median income of owners exceeds that of their tenants but also shows that there is consider-

20. Steven K. Mayo, *Theory and Estimation in the Economics of Housing Demand*, 10 J. URB. ECON. 95 (1981).

21. C. LANCE BARNETT, USING HEDONIC INDICES TO MEASURE HOUSING QUALITY (1979); JAMES R. FOLLAIN & STEPHEN MALPEZZI, DISSECTING HOUSING VALUE AND RENT: ESTIMATES OF HEDONIC INDICES FOR THIRTY-NINE LARGE SMA'S (1980); SALLY R. MERRILL, HEDONIC INDICES AS A MEASURE OF HOUSING QUALITY (1980); CHARLES W. NOLAND, ASSESSING HEDONIC INDICES FOR HOUSING (1980); Allen C. Goodman & Mashiro Kawai, *Length-of-Residence Discounts and Rental Housing Demand: Theory and Evidence*, 61 LAND ECON. 93 (1985).

22. *See, e.g.*, RICHARD F. MUTH, CITIES AND HOUSING (1969).

23. ARTHUR D. LITTLE, INC., THE OWNERS OF NEW YORK'S RENTAL HOUSING: A PROFILE (1981).

able overlap between the two distributions. There are many low-income owners and many high-income occupants of rent stabilized housing.

Does a difference in average income between two groups justify income transfers from all members of one group to all members of the other? The mean income of Jews in the United States exceeds that of others. Does this justify taxing Jews to provide subsidies to others? Should we tax Chinese-Americans to subsidize others for this reason? Should the food stamp program be financed by a tax on farmers? Few would answer these questions positively because it is not considered appropriate to finance government programs by a tax based on characteristics such as religion, ethnicity, or occupation. Instead, the majority favor taxes that impose the same burden on equally wealthy people. The primary programs for helping low-income households in the United States are financed by broad-based taxes.

It is often said that local governments cannot afford to provide help to the needy through explicit subsidies such as housing allowances, but that they can provide benefits to some needy people via rent control.[24] This argument is difficult to understand. In order to provide benefits, rent control must impose costs on some people. These people are primarily those who own rental housing before rent control goes into effect. If these people can be implicitly taxed via rent control, it is not at all clear why they cannot be explicitly taxed to the same extent. Specifically, the tax would be a proportional tax on the assessed value of rental property owned at a date immediately prior to any public discussion of the tax. Landlords would thus have no incentive to work harder to oppose the explicit rather than the implicit tax.

Even if one could produce a satisfactory justification for transfers from owners of rental housing to their tenants, one would be hard pressed to justify the pattern of costs and benefits of existing rent control ordinances and the nature of the subsidies and implicit taxes.

2. The Distribution of Benefits of Rent Control

In discussing the distribution of benefits, it is important to distinguish between the distribution among tenants living in the units when controls are adopted and those who move into these units later. The distribution of benefits among the first group is fairly clear without any study. The typical rent control ordinance rolls rents back to levels that prevailed at a date prior to serious consideration of the ordinance. This

24. Keating, *supra* note 7, at 1225.

would normally be about a year before its enactment. The percentage reduction in rents will be approximately the same at all rent levels and so the absolute reduction in rent will be greater at higher rent levels. The benefit to each tenant will be roughly equal to the absolute reduction in rent. Since average expenditure on housing is larger for richer households, average benefits are larger for these households. Since the majority of renters are middle and upper income by any reasonable definition, they surely receive the bulk of the benefits in the years immediately after the imposition of controls. Over time, the distribution of benefits depends upon how long these households stay in their controlled units.[25] However, the small differences in mobility rates across income classes could not possibly change the preceding conclusions.[26]

As mentioned earlier, it is not clear whether tenants who move into controlled units after the adoption of rent control actually benefit, because they pay key money and incur extra search costs in order to obtain possession of the unit and may spend more on its maintenance than they would in an uncontrolled unit. It is clear that all studies of rent control in the United States have overestimated benefits by ignoring these costs.

For what they are worth, studies of rent control ordinances that have been in existence for a while are unanimous in concluding that the variance in annual benefits is quite large among households with the same characteristics.[27] For example, Ault and Saba estimate that the mean benefit of rent control to occupants of controlled units in New York City in 1968 was $233 but that the standard deviation of benefits among households with the same income and size and the same race and age of the head was $737.[28] When consideration is expanded to all occupants of rental housing (that was not publicly subsidized) and a benefit of zero is assigned to households living in the uncontrolled sector, they estimate that the mean benefit was $151 and that the standard deviation of benefits among households that were the same with respect to the aforementioned characteristics was $537.[29] Findings such as these have led all investigators to conclude that equals are not treated at all equally under mature rent control ordinances.

25. If households who move into controlled units after the enactment of rent control receive benefits or if households who live in uncontrolled housing incur losses, we would also have to take into account how many years households spend in each sector to determine the distribution of benefits over time.

26. Hamilton et al., *supra* note 4, at Exhibits 2-14.

27. *See, e.g.*, Ault & Saba, *supra* note 17; Peter Linneman, *The Effects of Rent Control on the Distribution of Income Among New York City Renters*, 22 J. URB. ECON. 14 (1987); Olsen, *supra* note 9; Olsen & York, *supra* note 17.

28. Ault & Saba, *supra* note 17.

29. *Id.*

These studies have produced conflicting results concerning differences in average benefits among different types of households. For example, Ault and Saba estimate that the mean benefit is larger for richer rather than for poorer households living in controlled units, although they are the same with respect to other characteristics.[30] Ault and Saba also estimate that non-whites receive smaller benefits than similarly situated whites.[31] However, using identical data, Olsen obtains opposite results.[32]

In short, the distribution of benefits of rent control among renters in the jurisdiction at the time that controls are imposed is perverse under the usual arguments for income redistribution, and the distribution among those who come later is haphazard.

3. The Distribution of the Costs of Rent Control

While there is no evidence on the distribution of the cost of rent control, the following propositions are almost certainly true. The majority of families at each wealth level do not own rental housing. The cost of rent control is borne overwhelmingly by people who own rental housing at the time that it is adopted. Equally wealthy owners of rental property do not bear the same cost because they hold different proportions of their assets in this form.

These propositions lead to two questions. Why should rent control, which allegedly serves a public purpose, be financed by an implicit tax on such a small proportion of the population, and why should the magnitude of this tax on equally wealthy people depend upon the proportion of their assets held in the form of rental housing?

Even the meager evidence available makes clear that rent control has no merit as a redistributive device. It is much inferior to programs such as food stamps, housing vouchers, and AFDC that provide benefits to the poorest households funded by broad-based taxes. These programs provide the largest benefits to the poorest households and impose the largest taxes on the wealthiest taxpayers.

4. The Efficiency of Rent Control

The shortcomings of rent control ordinances are not limited to their unjustifiable patterns of benefits and costs. They are also highly inefficient redistributive devices. They lead to higher costs of producing hous-

30. *Id.*
31. *Id.*
32. Olsen, *supra* note 9, at 1095.

ing services in both the controlled and uncontrolled sectors and to haphazard changes in consumption patterns by occupants of controlled units.

A consistent finding of empirical studies of mature rent control ordinances is that their benefits to tenants are much less than their costs to landlords.[33] For example, Olsen estimates that the total benefit of rent control in New York City in 1968 to tenants was $270 million while its cost to landlords was $514 million.[34] Such a difference is not the inevitable consequence of a program of transfers from landlords to tenants. If an explicit tax had been imposed on landlords in proportion to the market value of the rental housing that they owned prior to any discussion of the tax and if the proceeds had been distributed to tenants in the form of cash grants, there would have been no differences between these numbers. The reason that there is a difference is that some occupants of controlled units live in more desirable apartments and spend less on other goods than they would have chosen if they had been given cash grants with the same costs to their landlords, while others live in less desirable apartments and spend more on other goods. If other members of society care about these households but think that they undervalue some goods (for example, housing) and overvalue other goods, it is good social policy to induce these households to choose more of the former and less of the latter than they would choose if given cash grants. However, this is not a persuasive argument for the changes in consumption patterns brought about by rent control.

The empirical evidence indicates that the majority of occupants of controlled units occupy less desirable housing and consume more of other goods than they would choose if given a cash grant. To justify this outcome, it would have to be argued that others believe that these households overvalue housing. The evidence also suggests that a substantial minority occupy better housing. To justify this outcome, it would have to be argued that others believe that these households undervalue housing. While some people may well feel that some overvalue housing and others undervalue it, there is no reason to believe that rent control changes consumption patterns in the desired directions for these two groups.

All published estimates of the benefits of rent control to tenants implicitly assume that each occupant of a controlled unit lives in an apartment with his preferred combination of characteristics such as space,

33. Ault & Saba, *supra* note 17; Olsen, *supra* note 9; Olsen & York, *supra* note 17.
34. Olsen, *supra* note 9, at 1094.

amenities, and location among units with the same market rent as the controlled unit. It has long been suggested that the difficulty of finding a controlled unit leads many of their occupants to live in units that are not well-suited to their current circumstances.[35] In a preliminary study of this issue based on one and two-person households headed by white males under 40 years old living in Manhattan in 1965, Olsen estimates that the magnitude of this distortion is large.[36] When he accounts for preferences for particular attributes of housing, he finds that estimated benefits are only one-fourth as large as benefits estimated using the standard approach that assumes that households are living in units with their preferred combinations of characteristics.

Economists have long argued that rent control will lead to less maintenance of the controlled stock. For an ordinance which places a ceiling on the rent of each apartment that is independent of its condition, it is usually argued that landlords will not maintain controlled apartments at all because maintenance adds something to cost but nothing to revenue. A more careful analysis of this type of ordinance reveals that a profit-maximizing landlord will spend some money on maintenance if this is needed to prevent the market rent of the apartment from falling below its controlled rent.[37] Even in this case the landlord will spend less on maintenance than in the absence of rent control.

The problem with the usual analysis is that it ignores a common feature of rent control ordinances and a likely response to them. Rent control laws typically allow higher rents for units that are improved and impose lower ceilings on units that are allowed to deteriorate.[38] It has been shown that as a theoretical proposition rent control ordinances that increase the ceiling rent on an apartment generously when it is upgraded and decrease it severely when it is allowed to deteriorate will lead to greater landlord maintenance of the unit.[39] Furthermore, even ordinances that reduce landlord maintenance to zero can lead to offsetting maintenance by the tenant.[40]

Since the effect of rent control on the maintenance of the controlled stock is ambiguous on theoretical grounds, empirical research is neces-

35. Olsen, *supra* note 9, at 1096-97.

36. Edgar O. Olsen, Bias in Estimating the Benefits of Government Programs Due to Misapplication of Composite Commodity Theorems: Estimates for Major U.S. Housing Programs (August 1990) (Unpublished Discussion Paper 927-90, Institute for Research on Poverty, University of Wisconsin).

37. Edgar O. Olsen, *What do Economists Know About the Effect of Rent Control on Housing Maintenance?*, 1 J. REAL EST. FIN. & ECON. 295, 296-98 (1988).

38. Baar, *supra* note 3, at 781-826, 830-32.

39. Olsen, *supra* note 37, at 298-300.

40. *Id.* at 300-02.

sary to determine the direction as well as the magnitude of this effect. Unfortunately, the sparse empirical literature contains no compelling evidence.[41] However, it is important to realize that rent control leads to inefficient production of housing services whether it increases or decreases the flow of services from controlled units. In the uncontrolled sector, landlords will maintain units to the point where the last dollar spent on maintenance will increase the value of the housing stock by a dollar. If rent control leads to less maintenance of a controlled unit, the last dollar spent on maintenance will increase the value of the housing stock by more than a dollar. If it leads to more maintenance, the last dollar spent on maintenance will increase the value of the housing stock by less than a dollar. Efficient production of housing stock requires that the last dollar spent on the maintenance of each dwelling increase the value of the stock by the same amount. If this condition is violated, it is possible to have a housing stock of the same value for a lower total cost. Furthermore, rent control leads to inefficient production of housing services to the extent that tenant maintenance replaces landlord maintenance and tenants are less efficient providers of this maintenance than their landlords.

Rent control creates incentives for owners of controlled units to move these units into the owner-occupied sector. Furthermore, although rent control ordinances typically exempt from controls housing built after their adoption, it seems plausible that owners of uncontrolled units in a locality with rent control will require a higher risk premium than they would in the absence of the ordinance. Therefore, it is reasonable to expect the price of housing service in the uncontrolled sector to be higher than it would have been in the absence of rent control. For both of these reasons, it is to be expected that rent control will lead more households to be homeowners. The meager evidence available supports this view.[42]

Contrary to the views of many social commentators, there is no

41. For a critical analysis of two of the three best empirical studies of this issue, see *id.* at 295. In a more recent study, Gyourko and Linneman attempt to estimate the effect of rent control and the magnitude of the rent control subsidy on the number of units that are in sound condition, accounting for the influence of a few other variables, namely the borough in which the unit is located, the year that the building was built, and whether the unit is in a structure with more than six floors. Joseph Gyourko & Peter Linneman, *Rent Controls and Rental Housing Quality: A Note on the Effects of New York City's Old Controls*, 27 J. URB. ECON. 398 (1990). The primary shortcoming of the study is that uncontrolled units are likely to differ substantially from controlled units with respect to unobserved characteristics. As a result, the error term in their statistical relationship is correlated with the rent control variables and their estimators are biased. For example, about two-thirds of the units decontrolled between 1947 and 1965 were in one and two family houses. RENT CONTROL: MYTHS & REALITIES 118 (Walter Block & Edgar O. Olsen eds., 1981).

42. Gyourko & Linneman, *supra* note 17 at 66-73; Lawrence B. Smith, *An Economic Assessment of Rent Controls: The Ontario Experience*, 1 J. REAL. EST. FIN. & ECON. 217, Table 2 (1988).

good reason to believe that it is desirable for more households to be homeowners. A homeowner must sell his house every time he moves. This involves real cost. So it makes sense for people who expect to move frequently to be renters. Furthermore, home ownership typically involves holding a large proportion of one's wealth in the form of one asset, thus exposing these households to more risk. To justify government action to increase the home ownership rate, it must be shown that people other than the new homeowners benefit. Some arguments of this sort have been offered, but none are supported by empirical evidence. Furthermore, we already have massive implicit subsidies through the income tax system that has induced many households who would otherwise rent to be homeowners.[43] Rent control exacerbates a bad situation with respect to tenure choice.

The other frequently mentioned efficiency effects of rent control are neither supported nor refuted by empirical evidence. These include the increase in the risks facing providers of rental housing, the greater search costs incurred by tenants, and the effect of rent control in one political jurisdiction in an urban area on the location of new construction in the area.

5. Conclusion

Despite the gaps in our knowledge of the effects of rent control, the case against this type of government action is fairly strong. No compelling justification has been offered for financing benefits to tenants by an implicit tax on landlords. There is no satisfactory explanation of why the magnitude of this tax on equally wealthy people should depend on the proportion of their assets held in the form of rental housing. The pattern of benefits is equally indefensible. Among households living in controlled units when rent control is enacted, the richest households receive the largest benefits. Among households who move into controlled housing later, there is no discernible relationship between benefit and household characteristics and the variance in benefit among similar households is large. In short, rent control is a poorly focused redistributive device.

It is also highly inefficient. The benefits of a mature rent control ordinance to tenants is far less than its cost to landlords because it leads to distortions in the consumption patterns of tenants and the production decisions of landlords. The majority of tenants occupy a unit whose overall desirability is less than that of the unit that they would occupy if

43. Harvey S. Rosen, *Housing Subsidies: Effects on Housing Decisions, Efficiency and Equity, in* 1 Handbook of Public Economics (Alan J. Auerbach & Martin Feldstein eds., 1985).

given a cash grant by their landlord, while a significant minority occupy a better unit. Furthermore, many tenants live in units whose particular characteristics are not well suited to their current circumstances. That is, rent control leads to haphazard changes in consumption patterns. Finally, theoretical reasoning suggests that rent control leads to higher costs of producing housing services in both the controlled and uncontrolled sectors. It induces some units to be undermaintained and (perhaps) others to be overmaintained. It induces too many people to be homeowners, imposes greater search costs on tenants, increases the risks facing providers of housing services, and affects the location of new construction in an urban area.

TABLE 1

DISTRIBUTION OF INCOME AMONG OWNERS OF RENT STABILIZED UNITS IN NEW YORK CITY IN 1984

Annual Income Class	Percentage of Owners
Under $10,000	9
10,000 - 19,999	21
20,000 - 39,999	24
40,000 - 74,999	33
75,000 or more	13

Source: Arthur D. Little, Inc., *supra* note 23, at 3.

TABLE 2

DISTRIBUTION OF INCOME AMONG OCCUPANTS OF RENT STABILIZED UNITS IN NEW YORK CITY IN 1983

Annual Income Class	Percentage of Tenants
Under $10,000	36
10,000 - 14,999	15
15,000 - 19,999	13
20,000 - 24,999	10
25,000 - 34,999	12
35,000 or more	14

Source: 1984 New York City Housing and Vacancy Survey