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## RENT CONTROL: A COMMENT ON OLSEN

ROBERT C. ELLICKSON\*

In his contribution to this symposium,<sup>1</sup> Edgar Olsen, a leading authority on the economics of rent control in the United States, concisely reviews much of the empirical and theoretical literature on the subject.<sup>2</sup> Olsen's title reveals, however, that his central mission is normative, not positive. His basic conclusions, which square with those of most American economists,<sup>3</sup> are that rent control is inefficient, distributionally capricious, and inferior to other policy instruments that might be employed in behalf of low-income tenants. While remaining comfortably within his profession's mainstream, Olsen does challenge a few orthodoxies, such as the notion that rent control invariably leads to undermaintenance of housing.

Economists are prone to underestimating the constraining effects of both transaction costs and law. Although Olsen is usually attentive to transaction costs, at places he fails to give them their due. For example, his assertion that cash housing allowances are invariably superior to rent control implicitly assumes that the administrative costs of housing-allowance programs aren't prohibitively high. While plausible, this assumption should at least be made explicit. When responding to an assertion that rent control may help preserve social networks, Olsen suggests that a city would be wiser to tax those who move, and distribute the tax's revenues to those who stay. A tax on moving could pose federal constitutional issues,<sup>4</sup> and might be barred under state law.<sup>5</sup>

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1. Edgar O. Olsen, *Is Rent Control Good Social Policy?*, 67 CHI.-KENT L. REV. 931 (1991).

2. Some valuable sources not cited by Olsen are Richard Arnott, *Rent Control: The International Experience*, 1 J. REAL EST. FIN. & ECON. 203 (1988) (and the symposium that follows), and Michael P. Murray et al., *Analyzing Rent Control: The Case of Los Angeles*, 29 ECON. INQUIRY 601 (1991).

3. The obligatory citation is Bruno S. Frey et al., *Consensus and Dissension Among Economists: An Empirical Inquiry*, 74 AM. ECON. REV. 986, 988, 991 (1984) (Only 1.9% of U.S. economists "generally disagree" with the statement that "[a] ceiling on rents reduces the quantity and quality of housing available.").

4. In *Nordlinger v. Hahn*, 112 S. Ct. 2326 (1992), the Supreme Court considered several federal constitutional challenges to California's Proposition 13, which skews property tax assessments in favor of stayers and against movers. In rejecting a challenge based on the equal protection clause, the Court identified two plausible purposes for this tax policy: (1) protecting a sitting owner's reliance interest against higher out-of-pocket costs; and (2) maintaining the continuity and stability of neighborhoods. These two rationales are essentially those that Radin invokes in defense of rent

Moving beyond these quibbles, in the first portion of this comment I describe ways in which economists' analyses of rent control tend to be incomplete. The second part evaluates the justifications for rent control recently put forward by Margaret Jane Radin, William H. Simon, and other legal scholars who are relatively hostile to letting people coordinate through markets.

## I. TOWARD A FULLER ECONOMIC ANALYSIS OF RENT CONTROL

Olsen focuses on rent control's effects on *housing* markets. Although he observes that a tenant's savings in rent may be largely offset by losses the tenant sustains in other markets, Olsen devotes little space to these sorts of second-order consequences. A thoroughgoing normative assessment of rent control requires consideration of its indirect effects, many (but not necessarily all) of which are likely to be baneful.

First, by reducing the mobility of tenant households, rent control may create inefficiencies in labor markets.<sup>6</sup> To retain the benefits of a controlled rent, a worker might decline to switch to a geographically distant job that he would otherwise take.

Second and relatedly, rent control tends to increase commuting costs. A worker who does switch jobs may continue to reside in his old apartment simply because its rent is controlled. These lock-in effects can increase the commuting costs of others. For instance, rent controls in Berkeley, Cambridge, and other university towns hamper incoming students' chances of finding apartments within walking distance of campus. Many new students may experience longer commutes, while the near-campus apartments they covet are inhabited by ex-students who commute away from the university.

Third, rent control tends to reduce levels of cooperation, certainly between landlord and tenant, and, more speculatively, in society at large. The Rand Corporation's work in and around Green Bay, Wisconsin—one of the best empirical studies of a rental housing market—supports the proposition that landlord-tenant relationships tend to be cooperative in the absence of rent control.<sup>7</sup> Both the tenant and the landlord typi-

control. The Court also held that the challenger did not have standing to assert a violation of freedom of travel.

5. For a review of legal constraints on municipal taxation systems, see DANIEL R. MANDELKER ET AL., *STATE AND LOCAL GOVERNMENT IN A FEDERAL SYSTEM* 195-307 (3d ed. 1990).

6. Rent-control ordinances will be discussed as if they had real teeth, which, as Olsen stresses, is often not the case.

7. "Generally, dealings between landlords and tenants in Brown County appear to be relaxed and comfortable. Twenty-five percent of the rental properties had resident landlords and thirteen

cally recognize that their inputs into maintaining the premises are sufficiently interdependent to enable either party to use tit-for-tat sanctions to punish the other's misconduct.<sup>8</sup> If thoroughly offended, either can also soon effect an exit from the relationship, either by refusing to renew a term-of-years lease, or by giving notice to terminate a periodic tenancy.

Rent control, by contrast, tends to lock landlords and tenants into continuing uncooperative relationships. The landlord, denied the usual means for ending a tenant's occupancy and feeling unjustly deprived of rental income, is likely to try to skimp on maintenance of the premises. This understandably aggravates the tenant, who, reluctant to relinquish a scarce low-rent dwelling, must fight back through unresponsive city bureaucracies. By keeping mutual antagonists in the same cage, rent control breeds nastiness in landlord-tenant interactions. A breakdown in one type of social relationship may infect others. My casual empiricism in Santa Monica and East Palo Alto, California, suggests that rent control in both places led to a general drop in civility. This, at any rate, is a hypothesis for why life in New York City seems more brutish than elsewhere.

Fourth, other housing programs predictably follow in the train of mature rent-control ordinances.<sup>9</sup> When the threat of rent control crimped construction of new rental housing in New York City, the city and state implemented a wide variety of project-subsidy programs—traditional public housing, Mitchell-Lama, and 421a and J-51 tax abatements—to make up for the shortfalls in the unsubsidized sector. An assessment of rent control should include the net effects of these predictable derivatives. An optimist might see them as salutary responses to the second-best world of rent control. A pessimist might note that the first-best solution—repeal of rent control—would be preferable, and that government housing-production programs may add to a city's woes. Among other drawbacks, subsidized housing projects cost about 25% to 50% more to build than comparable private projects do.<sup>10</sup>

Fifth, rent control may broadly transform a municipality's politics. In an uncontrolled city, tenants have smaller stakes than homeowners do and are less likely to vote. Events in the California cities of East Palo Alto, Santa Monica, and West Hollywood support the proposition that

percent had one or more tenants who were related to the landlord." RAND, THE SECOND ANNUAL REPORT OF THE HOUSING ASSISTANCE SUPPLY EXPERIMENT 69 (No. R-1959-HUD, May 1976).

8. See generally ROBERT AXELROD, *THE EVOLUTION OF COOPERATION* (1984).

9. Arnott, *supra* note 2, at 210, calls this the "old lady who swallowed the fly" syndrome.

10. See sources cited in John C. Weicher, *The Voucher/Production Debate*, in BUILDING FOUNDATIONS: HOUSING AND FEDERAL POLICY 263, 284-86 (Denise DiPasquale & Langley C. Keyes eds., 1990).

rent control increases tenants' stakes and political participation. Some proponents of rent control are attracted to the program partly because it helps mobilize a relatively passive part of the electorate. Others are less sanguine about an explosion of rentseeking at the municipal level.<sup>11</sup> In any event, economists should alert themselves to the second-order political fallout of rent control.

## II. RECENT DEFENSES OF RENT CONTROL

Olsen touches on some defenses of rent control that Margaret Jane Radin and others have advanced. I will seize this opportunity to join the debate. To a great extent, the battle has been epistemological. The economists and lawyers who criticize rent control tend to be positivists oriented toward empirical analysis. The critics tend to be less empirically inclined and informed. Radin, for example, conjures up situations—such as a landlord cartel or a perfectly inelastic long-run supply curve—under which rent control would indeed be theoretically justified; the rub is that in urban areas of the United States, these scenarios are utterly far-fetched.<sup>12</sup> The defenders of rent control also tend to articulate goals, such as personhood and community, that are hard to pin down, much less quantify.

In her thoughtful effort to rehabilitate rent control, Radin articulates and circumscribes a pair of justifications for it. Although Radin is to be commended for creativity, her arguments are not as weighty as she supposes.

### A. *Rent Control as a Device for Protecting the Home*

Radin first argues that the home is a special form of property, and that rent control may serve to insulate tenants from rising real rents that could dispossess them.<sup>13</sup> Although no one will contest that a sitting ten-

11. For a spectrum of opinion on the political implications of rent control, see Timothy J. Brennan, *Rights, Market Failure, and Rent Control: A Comment on Radin*, 17 PHIL. & PUB. AFF. 66, 76-79 (1988) ("The improvements in the performance of local political institutions have to be weighed against the inefficiency resulting from the imposition of a form of price and contract control on the rental market."); Robert C. Ellickson, *Cities and Homeowners Associations*, 130 U. PA. L. REV. 1519, 1545-54 (1982) (small local governments should have leeway to choose among electoral systems that vary in their propensity to involve tenants in politics); William H. Simon, *Social-Republican Property*, 38 UCLA L. REV. 1335, 1356-61 (1991) (praising rent control's potential for involving tenants in local politics).

12. Margaret J. Radin, *Residential Rent Control*, 15 PHIL. & PUB. AFF. 350, 351-52 (1986).

13. *Id.* at 359-68. Radin appears to be concerned about increases in real, as opposed to nominal, rents. See *id.* at 353, 359, 366. This objective is more explicitly identified in Note, *Reassessing Rent Control: Its Economic Impact in a Gentrifying Housing Market*, 101 HARV. L. REV. 1835, 1841 (1988) (policy goal should be to allow "poor tenants to stay in their units at approximately the current real rent").

ant may be traumatized by dislocation, Radin exaggerates the significance of this reality.<sup>14</sup> Rent control protects tenants' roots much less often than she implies, and, from a dynamic perspective, tends to frustrate households' aggregate prospects of residential security.

Contrary to their unsavory reputations, residential landlords are not apt to jack up the real rents charged sitting tenants.<sup>15</sup> Olsen cites five studies that indicate that longtime tenants tend to pay *lower* rents than do more recently arrived tenants who move into comparable housing units.<sup>16</sup> Rather than opportunistically exploiting tenants who have put down roots, landlords instead seem to give them price breaks. A residential tenant could also stave off the risk of a rent increase by negotiating a long-term lease; in practice, however, residential landlords, not tenants, typically push to lengthen leases.

Rent-control advocates identify households in gentrifying neighborhoods as the ones most likely to suffer from rising real rents.<sup>17</sup> Is gentrification common enough to justify the collateral mischief that citywide rent control causes? Contrary to what some advocates imply, gentrification of urban neighborhoods is uncommon, and is predicted to become even less frequent with the graying of the Babyboom generation.<sup>18</sup> Using citywide rent control to protect a small fraction of sitting tenants against rising real rents is like using hand grenades to kill dandelions in a lawn.

The other basic shortcoming of Radin's roots-protection argument is its generally static (*ex post*) character. She views tenants as already in place, and sees the basic issue to be how to protect them. Because housing markets are dynamic, however, this sort of analysis is shortsighted.<sup>19</sup>

14. Prospect theory, which is just now being incorporated into economic analysis, supports Radin's intuition that it is usually more harmful to oust a sitting tenant than to frustrate an incoming move by a would-be tenant. For an introduction to the theory, see Amos Tversky & Daniel Kahneman, *Rational Choice and the Framing of Decisions*, 59 J. BUS. S251 (1986). Prospect theory does not, however, support the notion that losses and gains cannot be measured by the same metric.

15. In Oliver Williamson's terminology, a landlord would appear able to exploit a sitting tenant's "asset-specific" investment. For a Williamsonian analysis of the landlord-tenant relationship, see Brennan, *supra* note 11, at 73-76.

16. See also William A. Clark & Allan D. Heskin, *The Impact of Rent Control on Tenure Discounts and Residential Mobility*, 58 LAND ECON. 109 (1982); but see J. Luis Guasch & Robert C. Marshall, *A Theoretical and Empirical Analysis of the Length of Residency Discount in the Rental Housing Market*, 22 J. URB. ECON. 291 (1987) (unable to verify discounts).

17. This is the central theme of *Reassessing Rent Control*, *supra* note 13.

18. RICHARD P. TAUB ET AL., *PATHS OF NEIGHBORHOOD CHANGE* 10 n.1 (1984) ("Taken as some proportion of total urban housing, [gentrification's] impact appears to be quite small."); JAMES W. HUGHES & GEORGE STERNLIEB, *THE DYNAMICS OF AMERICA'S HOUSING* 213 (1987) (predicting less gentrification in the future).

19. Radin is aware that protecting tenants from rent increases will have adverse dynamic consequences, but thinks that rent control is justified in certain situations. Because the discussion is general, one cannot be certain how much of, say, New York City's program she would be willing to repeal. Radin, *supra* note 12, at 361, 371.

Viewed *ex ante*, policies that stunt housing supply and mismatch households with dwelling units are detrimental to households' aspirations for homes. From a dynamic perspective, the notion that greater decommodification of housing markets will somehow serve the general cause of "personhood" is a triumph of hope over experience.<sup>20</sup> By reducing vacancy rates, rent controls frustrate, among others, immigrants seeking a new life, adult children seeking to establish households apart from their parents, and former tenants of housing that rent control propelled into abandonment.

The Soviet Union, the nation that most systematically decommodified its housing, suffered from a staggering housing shortage. The U.S. housing system has succeeded in delivering about five times more floor space per capita than the Soviet system did.<sup>21</sup> In Russia there are many more households than housing units; individuality and selfhood are hardly served when one must share the kitchen sink with a stranger.<sup>22</sup> Might there not be a lesson in the fact that the nations of the former Communist Bloc are now busily recommodifying their housing markets?<sup>23</sup>

#### *B. Rent Control as a Device for Cementing Community*

All scholars agree that rent control lessens tenant mobility. Critics regard this as one of the drawbacks of the policy. In their view, sticky housing markets deprive households of locational options and misallocate labor and dwellings. Radin and other defenders of rent control, by contrast, applaud certain government policies that restrict mobility.<sup>24</sup> They plausibly anticipate that a household considering moving from a neighborhood may not sufficiently weigh the damage its move will inflict on the neighborhood's social fabric. When a baseball player considers exercising free agency, the management of his current club will, in its bids to retain him, take into account his effect on the club's chemistry.

20. Radin does not make clear how much decommodification of housing she favors.

21. For this calculation, and sources on housing conditions in the Soviet Union, see Robert C. Ellickson, *The Untenable Case for an Unconditional Right to Shelter*, 15 HARV. J.L. & PUB. POL'Y 17, 25-26 (1992).

22. "Communal apartments, where several [often unrelated] families share the same kitchen, bathrooms, toilets and corridors, are still prevalent, especially in cities with an old housing stock such as Leningrad, where 36 percent of the population was still living in such apartments in 1986." 3 INTERNATIONAL MONETARY FUND ET AL., A STUDY OF THE SOVIET ECONOMY 323 (1991).

23. To start a phase-out of rent control, rents in Eastern Germany were tripled on October 1, 1991. BRUCE A. HARRIS, AFFORDABLE HOUSING POLICY IN UNIFIED GERMANY 36 (unpublished manuscript, on file with author). Partly to encourage the sale of housing units, Russia has entitled sitting tenants to claim ownership of the government housing units they have been occupying. Louis Uchitelle, *New Niche for Moscow Entrepreneurs: Real Estate*, N.Y. TIMES, Feb. 28, 1992, at A10.

24. See Radin, *supra* note 12, at 368-71; Simon, *supra* note 11, at 1356-61.

When a household considers leaving a neighborhood, by contrast, transaction costs are likely to prevent the appearance of an agent who can fully represent the interests of those who are staying put. Hence, Radin's argument concludes, rent control may be a defensible method for keeping some households from moving when they should not.

This defense, like the roots-protection defense, rests on tenuous premises and identifies a remedy that is not closely linked to the problem identified. First, the overall desirability of keeping people in their current places is not obvious. Commentators are prone to romanticize life in the peasant village, small town, or urban enclave. Sinclair Lewis' *Main Street* is a reminder that while stable communities can provide mutual support, they can also be stultifying. Unsullied rights to enter into and exit from residential communities may both deter group abuses and assure a household the freedom of a fresh start.

Moreover, in what might be described as "replenishing communities," mobility constraints may lock in stale households and lock out the fresh entrants the community most needs to retain its vitality. To invoke a prior example, in university towns rent control perpetuates residency by former students, to the detriment of the communitarian prospects of incoming students. An anti-move policy may also impede adaptive en masse relocations of social networks to new locations. For example, New York City's rent control may have made it more difficult for Brooklyn retirees to transplant their communities to Miami Beach.

Assuming for the sake of argument that households should be deterred from moving, Olsen observes (as was mentioned above) that a tax on those who move would be a better tailored policy response.<sup>25</sup> Surely Olsen is right to regard rent control as an imprecise cure for excessive mobility. Rent control does little or nothing to deter moves by the many households who are owner-occupiers, or reside in rental units exempt from rent control. Taxes wreak less ancillary damage than controls do.

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In sum, Radin and her allies only succeed in identifying small weights that might be placed on one side of a set of scales that slants heavily downward to the other side. It is anachronistic for the current generation of anti-market legal scholars to be toiling to spin out arm-

25. Instead of taxing movers, a municipality might experiment with property tax abatements for longtime residents. Cf. the lock-in effects of California's Proposition 13, described *supra* note 4. Similarly, Congress could repeal, in the name of community, Internal Revenue Code § 1034, which enables a home seller with a capital gain to avoid its realization by buying an equally expensive home within two years.



chair rationalizations for Old-Left programs. Olsen rightly skewers the defenders of rent control for devoting themselves to prolonging the life of a misguided policy, instead of to the design of programs that would better advance their objectives.