

RENT CONTROL AND THE AVAILABILITY  
OF AFFORDABLE HOUSING  
IN THE DISTRICT OF COLUMBIA:

A Delicate Balance

by

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## PREFACE

In March 1987, the District of Columbia's Department of Consumer and Regulatory Affairs (DCRA) contracted with The Urban Institute to conduct a study of rent control in the District. This study was mandated by Section 220 of the Rental Housing Act of 1985 (D.C. Law 6-10). Its purpose is to provide a factual basis for determining the continued need for rent stabilization in the District of Columbia.

The content of the study was originally defined by nine specific items delineated by the City Council:

- I. The number of new or renovated units placed on the District's rental market after May 1, 1985.
- II. The number of new or renovated units projected to be placed on the District's rental market through 1996.
- III. An assessment of the effectiveness of the Tenant Assistance Program (TAP), and the projected cost of TAP in the absence of rent control.
- IV. The impact of rent control on the cost and supply of rental housing.
- V. An assessment of the present rent control program in terms of its ability to be understood, and its efficiency, economy, equity, and flexibility.
- VI. The impact of rent control on small housing providers.
- VII. The number of District residents living in substandard housing and their location.
- VIII. An assessment of the impact of the Civil Infractions Act on the enforcement of the District's housing code regulations.
- IX. An assessment of the impact on both the rental housing market and the rent stabilization program of vacancy decontrol, luxury decontrol, increasing the small landlord exemption from 4 to 10 rental units, and using the percentage of family income available for rent as a component of a rent control formula.

To address these nine specific questions effectively, a more comprehensive analysis of the workings of the District's rental housing market was required. In addition, since the Civil Infractions program was not implemented during the study's data collection phase, a base-line analysis of the District's housing code enforcement process was substituted for study item number VIII.

The expanded study scope is organized around four major study components: 1) the D.C. rental housing market -- conditions and trends; 2) D.C. government programs that intervene in the housing market; 3) impacts of rent control on market outcomes; and 4) possibilities for the future. This final research report addresses each of these four study components in turn, while Annex A presents our conclusions regarding each of the original nine study items.

Because the issues addressed in this study are many and complex, this final report does not provide all of the methodological or empirical details involved in the study as a whole. These details are presented in a Technical Supplement, in which individual chapters focus on specific study issues and empirical methods. The contents of this Technical Supplement are listed in Annex C of this report.

Urban Institute staff members who played major roles in the collection and analysis of data for this study, and who have contributed chapters to the Technical Supplement, include:

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The **Mayor's Tenant-Provider Advisory Committee**, participated in questionnaire development, provided advice on data collection and analysis, and reviewed the study design. In addition, we are particularly grateful to those members who contributed their time for informal, one-on-one interviews on study issues. The Committee membership included:

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Despite the help of these many individuals and organizations, all errors and ambiguities are, of course, the responsibility of the author.





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## INTRODUCTION AND SUMMARY

The District of Columbia's current system of rent stabilization has evolved over more than a decade of experience and debate, and reflects an ambitious set of objectives. According to the Rental Housing Act of 1985, the District's overall housing policy is intended to protect low and moderate income tenants from excessive housing costs; to encourage the construction of new units and the rehabilitation of vacant units; to provide administrative mechanisms for the resolution of disputes between housing providers and tenants; to protect the existing supply of rental housing from conversion to other uses; and to allow housing providers and developers a reasonable rate of return on their investments.

Approximately two thirds of the District's rental stock -- about 101,100 units -- are subject to controls, with five important categories of rental units receiving exemptions: 1) units owned by small providers (individuals with fewer than four D.C. rental units in all); 2) new and substantially renovated units (those added to the stock after 1975); 3) units in vacant buildings (if the buildings were continuously vacant since 1985); 4) co-op units; and 5) subsidized units (except those subsidized through the D.C. Tenant Assistance Program).

The existing system of controls regulates both the frequency and the amount of rent increases. For units that are properly licensed and registered and that comply with the District's housing code, rents can increase annually by the previous year's Consumer Price Index (CPI). And when a unit is vacated, its rent can be increased by 12% or up to the rent ceiling for a comparable unit in the same property, whichever is higher. In addition, providers can petition to increase rent ceilings to reflect the cost increases associated with capital improvements, substantial rehabilitation, or changes in services and facilities. For properties in financial hardship, rent increases can be approved to generate a 12% cash return on equity. And finally, housing providers can negotiate voluntary agreements with their tenants to increase rent ceilings.

The complexity of these exemption and rent adjustment provisions reflects the District's effort to balance the goal of reducing housing costs for the city's renters against the need to ensure that rental housing is sufficiently profitable to attract investment so that the supply of good quality rental units is sustained.

This report presents the results of a comprehensive study of the impacts of rent control on the availability, adequacy, and affordability of rental housing in D.C. This study -- which was mandated by the Rental Housing Act of 1985 -- provides an objective basis for assessing how well the existing rent control system has achieved its statutory goals, and for developing rental housing policies that will meet the District's needs for the remainder of this century.

## Data Sources and Study Structure

In order to effectively address the City Council's mandate to conduct a comprehensive analysis of the impacts of rent control in the District of Columbia, The Urban Institute compiled an extensive data base that includes up-to-date information about renter households and their housing circumstances, housing providers and the physical and financial condition of their properties, stock losses and additions, and the operation of the rent control program, housing code enforcement and the Tenant Assistance Program. Existing data compiled by city agencies and by the U.S. Census provided a starting point, but the results presented in this report are based on the analysis of eight major sources, all but one of which constitute new data collected specifically for this effort:

**The American Housing Survey (AHS).** The U.S. Census Bureau conducts regular surveys of households and housing units for 59 metropolitan areas, including the District of Columbia and its suburbs. Our analysis makes extensive use of the 1974 AHS data for the Washington metropolitan area, as well as key indicators for 1977 and 1981. The AHS was most recently conducted in the Washington metropolitan area in 1985, and we have obtained counts of rental households and housing units from this survey. However, since the 1985 AHS was not released by the Census until the end of the study period, we were not able to analyze individual household observations. Finally, we refer at numerous points throughout this report to published AHS data for other central cities -- with and without rent control -- in the Northeast and mid-Atlantic states.

**1987 Survey of Renter Households.** During the summer of 1987, The Urban Institute, with the help of Lawrence Johnson and Associates, conducted telephone interviews with 3,000 D.C. renters and 600 renters in nearby suburban jurisdictions. These interviews provide data on household characteristics, housing conditions, rent levels, and attitudes toward the rent control program. Household responses regarding the control status of their units were verified against data in DCRA registration files.

**Financial Statements for Controlled Properties.** For a sample of 814 controlled rental properties, 1985 financial statements were collected from DCRA's registration files. These financial statements were verified by comparing summary tabulations of income and expense items to tabulations of Department of Finance and Revenue (DFR) data for the same properties. Confidentiality restrictions prevented The Urban Institute from obtaining direct access to DFR financial data for individual properties.

**1987 Survey of D.C. Housing Providers.** The owners and/or managers of the 814 controlled rental properties for which financial statements were obtained were asked to provide additional factual and attitudinal data on a mail-back questionnaire. Providers of a representative sample of 244 controlled rental properties responded to this questionnaire.

**Inventory of Stock Losses and Additions.** Drawing from D.C. Certificates of Occupancy, Tenant Eviction Petitions, and Condominium Conversion Registrations, The Urban Institute constructed an inventory of all additions to and losses from the District's rental housing stock from May 1, 1985 through April 31, 1987. In addition, telephone interviews were conducted with the housing providers responsible for a subset of these additions and losses.

**Housing Code Enforcement Histories.** For a sub-sample of 319 controlled rental properties, a year's history of housing code enforcement activity was recorded from the records of DCRA's Housing Inspections Division.

**Rent Control Petitions Records.** The volume and case-by-case disposition of 1985-1987 housing provider and tenant petitions were gathered from DCRA records.

**Tenant Assistance Program Participation.** Staff of ICF Inc., a sub-contractor to The Urban Institute, collected and coded data on a representative sample of TAP applicants and program participants as of January 1988.

Information provided by these structured and objective data sources has been supplemented by numerous personal interviews conducted with tenant advocates, housing providers, developers, and public officials. In these interviews, Urban Institute research staff members sought to understand the subjective perspectives of key actors in the D.C. rental housing market, and to interpret the implications of the study's empirical results.

The original mandate for this study identified nine specific items for analysis (see Annex A). To address these nine issues effectively, however, a broader analysis of the workings of the District's rental housing market was required. Exhibit 1 outlines the scope and organization of our study, which consists of four major components. The first component describes the District's rental housing market, focusing on the availability, adequacy, and affordability of rental housing and on the factors that shape these outcomes. Next, we review the operation of three District programs designed to intervene in the workings of the rental housing market -- the rent control program itself, housing code enforcement, and the Tenant Assistance Program (TAP). The study's third component analyzes the impacts of the existing rent control program on the housing market, estimating how key market outcomes would differ in the absence of controls. And finally, the study explores possible future market outcomes, under a variety of regulatory scenarios.

## EXHIBIT 1

### STRUCTURE OF THE RENT CONTROL STUDY

- 1.0 THE D.C. RENTAL HOUSING MARKET
  - 1.1 Current Conditions and Recent Trends--What's Been Happening
  - 1.2 Changes in the Rental Inventory--How it Happened
  - 1.3 Rental Housing Market Dynamics--Why it Happened
- 2.0 GOVERNMENT PROGRAMS
  - 2.1 Operation of the Rent Control Program
  - 2.2 Housing Code Enforcement
  - 2.3 The Tenant Assistance Program
- 3.0 IMPACTS OF RENT CONTROL ON MARKET OUTCOMES
  - 3.1 Impacts on Rents and Affordability
  - 3.2 Impacts on Household Decisions--Mobility, Tenure, and Location
  - 3.3 Impacts on Provider Profits and Property Value
  - 3.4 Impacts on Investment Decisions and the Rental Housing Inventory
- 4.0 POSSIBILITIES FOR THE FUTURE
  - 4.1 Forecasting Inventory Change
  - 4.2 Alternatives to the Existing System of Controls
    - Vacancy Decontrol
    - Luxury Decontrol
    - Expanded Small-Owner Exemption
    - Household Affordability as a Factor in Determining Rent Adjustments
  - 4.3 Expanded Tenant Assistance Program as an Alternative or Supplement to Rent Control



The next four chapters of this report focus in turn on the study components outlined in Exhibit 1. The remainder of this introductory chapter, however, provides an overview of our central findings regarding the impacts of rent control on the availability, adequacy, and affordability of rental housing in the District of Columbia.

Annex A presents our findings regarding each of the nine study items originally mandated by D.C. Law 6-10, and Annex B describes the sampling and survey methods employed to assemble the data upon which our analysis is based. For additional methodological and empirical details, see the Technical Supplement to this final report, the contents of which are listed in Annex C.

### Impacts of Rent Control on the D.C. Rental Market

The most severe and widespread problem confronting D.C. renters today is a shortage of units that are affordable for households with low and moderate incomes. Rent control is neither the cause nor the complete solution for the problem of housing affordability. The existing system of controls achieves its objective of reducing rents for the majority of D.C. units, but it has by no means eliminated the problem of excessive housing cost burdens. On the other hand, while there is a legitimate cause for concern that an excessively restrictive policy of rent control might ultimately limit the supply of rental housing, the empirical evidence does not indicate that the District's rent control program has had a significant adverse impact on housing supply. In fact, the quality of the District's housing stock is better today than in was in 1974, and changes in the overall size of the rental inventory appear to be much more sensitive to nationwide demographic and economic forces than to the local regulatory environment.

We estimate that, in the absence of controls, the rent for the average D.C. unit would be between \$95 and \$100 per month higher, and roughly three quarters of D.C. renters would be paying higher rents than they do today. The District's existing system of controls has moderated increases in rent levels for most households, particularly those who remain in their units for more than a year or two. By reducing prevailing rent levels, the existing system of controls makes rental housing in the District more affordable than it otherwise would be, so that the share of renters devoting more than 30% of their income toward housing is lower in D.C. than in other U.S. central cities.

However, not all D.C. renters benefit directly from controls. Because the District's rent control program allows larger rent increases when units change occupancy, the rent savings attributable to controls are greatest for households who remain in the same controlled units for more than a year or two. Recent movers pay as much -- and possibly even more -- than they would in the absence of controls, since many housing providers raise rents to the highest allowable levels at the time of turnover.

By targetting benefits to long-term stayers, rent control tends to provide the greatest rent savings to lower income renters, to elderly households, and to families with children. However, affluent renters, as well as young singles and groups of young adults also obtain direct benefits whenever they remain in controlled units for an extended number of years. And poor households who move are likely to pay rents that are just as high, or perhaps higher, as those that would prevail in an uncontrolled market.

During the 1980s the rate of rent increases has generally kept pace with increases in operating costs, even for units that have been continuously occupied. Although rent levels in the District today are lower on average than they would be in the absence of controls, the District's system of automatic rent adjustments appears to have compensated most housing providers adequately for increases in operating costs. This may not have been true during the 1970s, when utility costs rose sharply, and annual rent adjustments were limited to 10% even when the CPI was higher. During this period, the revenues of some providers may have been eroded as a result of controls.

The majority of controlled units in the District generate relatively low cash returns. In fact, most providers do not realize a 12% cash return on their equity. However, after accounting for appreciation gains and tax benefits, the profitability of investment in D.C. rental housing today appears to compare favorably to alternative investment opportunities.

The evidence is mixed when it comes to determining whether rent control is responsible for housing deficiencies in the District's rental stock. A significant minority of D.C. rental units -- about one in five -- are physically deficient.<sup>1</sup> On one hand, we estimate that the higher rent levels that would prevail in the absence of controls would increase providers' rent revenues by about 33% on average. Many providers indicate that they would use higher revenues to improve building maintenance or to address deferred maintenance problems, and the increased revenue that would be realized in the absence of controls would probably be sufficient to improve maintenance substantially in at least half of the existing stock. On the other hand, however, the share of D.C. rental units that are physically deficient has actually declined from 26% to 20% since the implementation of rent control in the District of Columbia, and the rate of deficiencies is higher among exempt units today than among units that are subject to controls.

Even in the absence of controls, the District's rental stock would have experienced a precipitous decline during the 1970s. The newly imposed system of local rent controls may have been a

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1. See Definitions for the criteria used to identify physically deficient units.

factor in the decisions of some housing providers to remove properties from use or to convert them to owner-occupancy. However, since many uncontrolled central cities in the U.S. experienced the same pattern of decline, we conclude that widespread demographic and economic conditions were more important sources of the shrinkage in the District's rental inventory. Specifically, the relative attractiveness of homeownership, the expansion of suburban housing opportunities for minorities, and the basic costs of rental housing production appear to be the critical determinants of the number of units added to and lost from the District's rental housing stock.

In more recent years, the supply of rental housing in the District has begun to respond to renewed demand pressures, confirming that rent control is not the determining factor in investment decision-making. Starting in the early 1980s, demand for rental housing in the District began to stabilize, in part because rising interest rates, lower inflation, and reductions in marginal tax rates have all contributed to make homeownership much less affordable relative to rental housing. At first, the supply of rental units continued its decline, and the result was a dramatic drop in the rental vacancy rate from 6.2% in 1981 to 2.5% in 1985. More recently, the District's rental stock has started to grow in size, increasing by about 1,600 units between 1985 and 1987. This turn-around represents a lagged market response to renewed levels of effective demand.

Despite the renewed level of rental housing production, the District faces a persistent shortage of units that low and moderate income households can afford. Today, fewer units are being removed from the inventory than in the 1970s and early 1980s, and more units are being added through substantial renovation and the conversion of non-residential properties. However, these additions respond to a heightened level of demand from relatively affluent city renters; most do not significantly expand the availability of housing that is affordable for poor and moderate income renters in D.C. In fact, a substantial share of the units added to the rental stock in recent years were developed as condominiums and are being rented rather than owner-occupied for the time-being. These units, which currently supplement the stock of rental housing, could easily be converted to owner-occupancy if and when demand pressures swing back in that direction.

The availability of low-cost rental housing is much more sensitive to the number of units lost from the stock each year than to the number of units added. Again, rent control, along with other aspects of the local regulatory environment, may play a role in the decisions of some providers who remove properties from rental use. However, the current system of rent control is a balanced one, which -- at least in recent years -- has allowed rent revenues to rise along with operating costs, and which -- in principle -- offers opportunities for providers to obtain greater rent increases if they are experiencing financial hardship or if they choose to invest in capital improvements.

The units that are at greatest risk of being removed from the stock -- units with very low rents and chronic code violations -- qualify for hardship rent increases but have not applied for them. Rent control is by no means the primary constraint preventing the owners of these units from raising rents and making property improvements. The administrative and financial burden of the hardship petition process may present a difficult hurdle for these providers, but their primary problem is that the tenants who occupy their buildings are simply too poor to pay the rent levels required.

While rent control has not caused the problems of housing availability and affordability in the District of Columbia, it certainly has not eliminated these problems either -- nor can it be expected to. Despite the rent reductions attributable to the existing system of controls, 43% of all renters in the District pay more than 30% of their income for housing, and about 10% pay more than three quarters of their income for housing, placing them seriously at risk of homelessness. And although rent control significantly reduces rent levels for those who remain in their apartments for several years, we estimate that recent movers pay rents as high or possibly even higher than they would in the absence of controls. As a result, poor households who move as well as newly forming households with low incomes have great difficulty finding affordable rental housing in the District.

#### Possibilities for the Future

Marginal modifications to the existing system of rent control -- such as luxury decontrol -- would have minimal effects on market outcomes. Fewer than 10% of controlled rental units appear to qualify as "luxury" apartments, and these units already charge close to market rents, since most of them are occupied by affluent recent movers.

An expanded small-owner exemption (making owners of up to ten D.C. units exempt from controls) would have more significant market impacts. Approximately 16% of the District's controlled units would qualify for an expanded small-owner exemption. These units are typically in good condition and charge below average rents, but their owners appear to have considerable difficulty understanding the District's complex rent stabilization program. While it is unlikely that making rental housing investment more profitable and less administratively burdensome for small investors would substantially expand the level of housing production in the District, it might avoid the potentially harmful effects of the Tax Reform Act of 1986 on small providers and their tenants.

While it may be tempting to strengthen the impact of rent control by limiting rent adjustments on the basis of household affordability, such an initiative would almost certainly result

in increased evictions, discrimination against low income renters, deterioration of low rent units, and removal of these units from the housing stock. Rent control, per se, cannot be expected to eliminate the problem of housing affordability in the District. While rent control may play an important role in moderating rent levels, housing affordability for low and moderate income households can only be guaranteed through a systematic program of direct assistance, low cost housing production, and preservation of the existing stock.

Within the existing system of controls, we have identified two key areas for improvement or fine-tuning. First, the District needs to develop a comprehensive information system for monitoring the rental housing stock. Such a system would enable DCRA to more effectively enforce the coverage of the existing rent control program, to monitor trends in the costs of operating rental property in the District so as to ensure that the increase of general applicability keeps pace with provider costs, and to forge a more effective information and enforcement linkage between housing inspections and the rent adjustments.

In addition, the District should streamline the hardship, substantial rehab, and capital improvements petition processes, so that they work more effectively from the perspectives of both housing providers and tenants. These provisions of the existing rent stabilization program effectively balance the moderating impact on rents by allowing providers to obtain rent increases in order to earn an adequate return on investment or to finance property improvements. But both property owners and lenders are discouraged from investing in property improvements when delays and uncertainty cloud their revenue projections. This is not to suggest that providers should not be required to document their revenues, expenses, and planned improvements, or that tenants should not have an opportunity to challenge proposed rent increases. Instead, we recommend that the standards of documentation for hardship, substantial rehab, and capital improvements petitions should be rigorous and clearly specified. Then, for providers who supply adequate documentation, the review and approval process should be prompt and predictable.

Rent control alone cannot ensure the availability of decent and affordable rental housing for all of the District's residents. A comprehensive rental housing strategy for D.C. requires more direct measures, including programs to supplement the rents low and moderate income tenants can afford to pay, to preserve existing low-rent properties, and to induce the production of additional, low and moderate cost rental units.

Public housing, federally subsidized housing projects, and the local Tenant Assistance Program (TAP) all provide direct remedies to the problem of housing affordability for low income renters in the District of Columbia. But, at current funding levels, these programs can only serve a fraction of the households in need. Currently, 28,300 D.C. renter households receive direct housing assistance, but a total of 53,000 additional households are

eligible for assistance, according to TAP standards. If TAP allocated all of its current funding, it could serve 2,300 more households, and if the public housing program completed its modernization program and achieved full occupancy of its inventory, another 2,300 needy households could be accommodated in public housing units.

Even if both TAP and the public housing program were working at full capacity, at least 48,000 low and moderate households would still live in deficient, overcrowded, or unaffordable rental units. In the absence of rent control, the number of eligible households would be closer to 55,000, because a much larger share of low and moderate income households would be paying excessive rent burdens. The District has designed and implemented several creative programs for addressing local housing needs, and these programs can be expected to significantly expand the availability of affordable rental housing and the capacity of low income renters to pay for adequate units. But the annual cost of serving all of the District's needy households would exceed \$200 million. Clearly, housing programs of this scope are beyond the capacity of the District government. The answer to the District's housing problems does not lie in the enactment of new programs, but in the more effective implementation of existing programs for housing assistance, preservation, and direct construction. Moreover, only through collaboration with the federal government and neighboring suburban jurisdictions can decent and affordable rental housing be ensured for all.

A key element of an overall strategy for expanding the availability of low cost rental housing in the District should be the preservation of the existing stock. In particular, priority should be given to properties that currently serve low and moderate income households, particularly those that are physically and financially distressed. By intervening to help these projects address their deferred maintenance problems and regain sound financial footing, the District can reduce the number of low cost rental units that drop out of the housing inventory, thereby contributing to the availability of affordable housing. In some cases, rent increases will be necessary to enable these properties to survive. While these increases may be painful for tenants, if they are moderate and if they are accompanied by significant improvements in building conditions, they will probably be tolerable for most tenants. Those who cannot afford the increased rents should be directly assisted through the TAP program. Finally, while preservation is the most cost-effective way of contributing to the availability of affordable rental housing, the stock of low and moderate cost housing also needs to be supplemented through subsidized new construction and substantial rehabilitation.

## 1. THE D.C. RENTAL HOUSING MARKET

This chapter sets the stage for a thorough examination of the impacts of rent control, by examining key conditions and trends in the District's rental housing market. We begin by focusing on the demand side of the housing market -- what types of households make up the renter population in D.C., and what problems to these households face? Next, we focus on the rental stock itself, and how it has changed in response to the changing demand conditions of the last decade and a half. And finally, we focus on financial and ownership characteristics of the rental inventory -- what types of owners provide rental housing in D.C., and what are the financial characteristics of their investments?

### Renter Households and Housing Problems

The District's renter population consists of about 157,900 households, of whom 18% receive federal or local rent subsidies.<sup>1</sup> Our analysis focuses for the most part on the characteristics of the approximately 129,600 D.C. renter households who are unassisted.<sup>2</sup> The majority of these households (62%) are black, and half have annual incomes under \$20,000. In fact, 40% of D.C. renter households are poor (annual incomes under \$15,000), and only about 6% earn more than \$50,000 annually.

However, the D.C. renter population is by no means a homogeneous group. Exhibit 2 illustrates the relative size of six distinct groups of unassisted renter households: 1) non-elderly singles; 2) groups of unrelated adults; 3) elderly singles and couples; 4) non-elderly couples without children; 5) husband-wife families with children; and 6) female-headed families with children. These groups differ sharply with respect to household

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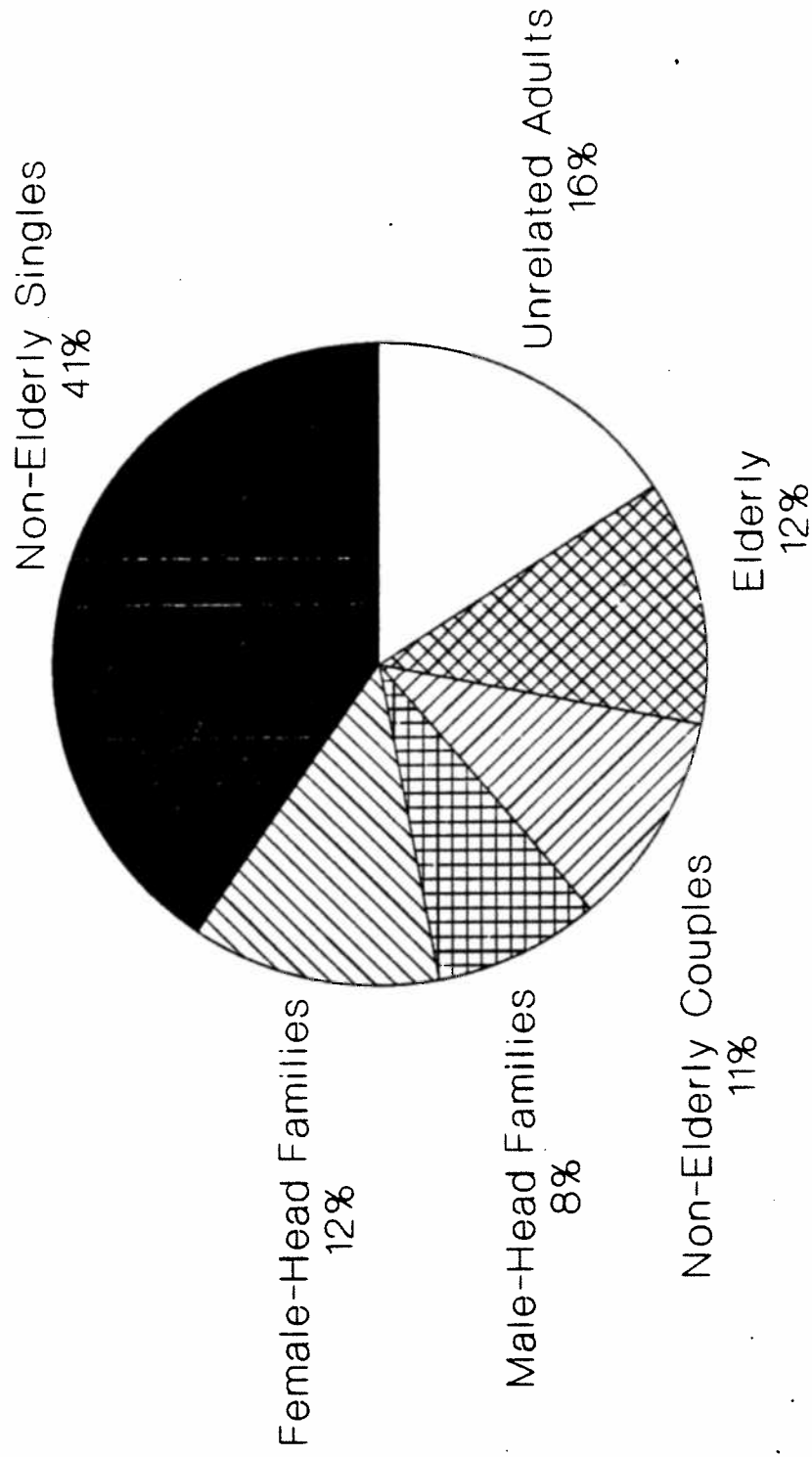
1. Our estimate of the total number of renter households in the District is derived as follows: The American Housing Survey (conducted by the Bureau of Census, estimates that there were 160,400 rental units in D.C. in 1985. Our inventory of additions and losses to the rental stock between 1985 and 1987 yields about 1600 additions by 1987, to yield a 1987 total of 162,000 rental units. According to the AHS, the rental vacancy rate (units vacant for rent divided by total renter occupied and vacant for rent) for D.C. was 2.51% in 1985. We have assumed that this rate remained essentially the same between 1985 and 1987, for a total of 157,900 D.C. renter households.

2. The analysis presented in the section is based on our survey of 3,600 unassisted renter households in D.C. and the surrounding suburbs. Both our household survey and our analysis focus on unassisted households, since it is these renters whose housing circumstances are most likely to be affected by rent control. See Annex B for more details on sampling and survey methodology.

EXHIBIT 2

# D.C. RENTER HOUSEHOLDS

## Life Cycle Groups, 1987



SOURCE: 1987 U.I. Tenant Survey



composition, life-cycle status, and socio-economic circumstances; and, consequently, they face very different housing opportunities and housing problems.

Non-elderly singles and groups of unrelated adults -- who account for about 57% of all D.C. households -- form an ethnically diverse and relatively affluent group, many of whom are relative newcomers to the D.C. area who participate only temporarily in the District's rental market. In contrast, families and elderly households who rent housing in the District are predominantly black, generally poorer<sup>1</sup>, and much more likely to be long-term residents of the city.

	<u>Median Income</u>	<u>% Black</u>	<u>% Newcomers to D.C.</u>
Non-Elderly Singles	\$20,000	52.2%	36.9%
Adult Groups	30,000	41.3	52.3
Elderly	13,000	64.9	2.9
Non-Elderly Couples	22,000	75.7	23.7
Husb-Wife Families	23,000	83.9	20.7
Female-Hd Families	15,000	91.2	10.5

The presence of these very different segments in the D.C. rental housing market is largely explained by the widespread U.S. preference for homeownership. Almost all households who do not view their current living situation as temporary want to become homeowners if they can afford it. Thus, owner-occupancy rates among families and elderly people are very high, and households who remain renters either choose to do so because they expect to change their living arrangements relatively soon, or are forced to do so because they cannot afford homeownership. As a result, in Washington -- as in other central cities throughout the U.S. -- the majority of renters have low to moderate incomes,<sup>2</sup> with the exception of the young singles and groups of unrelated adults, who are relative short-timers in the local rental housing market.

Excessive costs constitute the most widespread housing problem for D.C. renters. More than two out of every five D.C. renters (43%) spend over 30% of their income for housing, and more than 10% pay over three quarters of their income for rent (including

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1. See Section I of the Technical Supplement for more information about the racial composition, income levels, and mobility patterns of the six life-cycle groups.

2. For purposes of this analysis, we have defined the following income categories, based on 1987 annual incomes: less than \$15,000 -- low income or poor; between \$15,000 and \$25,000 -- moderate income; between \$25,000 and \$35,000 -- lower-middle income; between \$35,000 and \$50,000 -- upper-middle income; and over \$50,000 -- high income or affluent.

utilities). The problem of housing affordability is particularly severe for those who are poor. As shown in Exhibit 3, poor and moderate income households are the most likely to pay excessive housing costs. Only a small minority of those with annual incomes over \$25,000 spend more than 30% of their income on housing, while among those who are poor, the majority pay more than 30% of income for housing and about one in four pays more than three quarters of income for rent and utilities.

While problems of housing affordability affect the largest number of D.C. renters, the problems of physically deficient and overcrowded housing cannot be ignored. Roughly one in five D.C. rental units is physically deficient, and deficiencies seem to plague all groups to roughly the same degree -- regardless of location, income, rent, or household composition. Overcrowding, on the other hand, is clearly a problem faced only by large households -- primarily families with children. Only about 5% of all D.C. renters, but 15 to 20% of families with children live in overcrowded units.

	<u>% living in deficient units</u>	<u>% living in overcrowded units</u>
Non-Elderly Singles	20.2%	0.0%
Adult Groups	16.9	6.2
Elderly	22.6	0.4
Non-Elderly Couples	28.7	6.0
Husb-Wife Families	22.3	20.7
Female-Hd Families	21.7	15.5

#### Recent Trends in Renter Households and Housing Problems

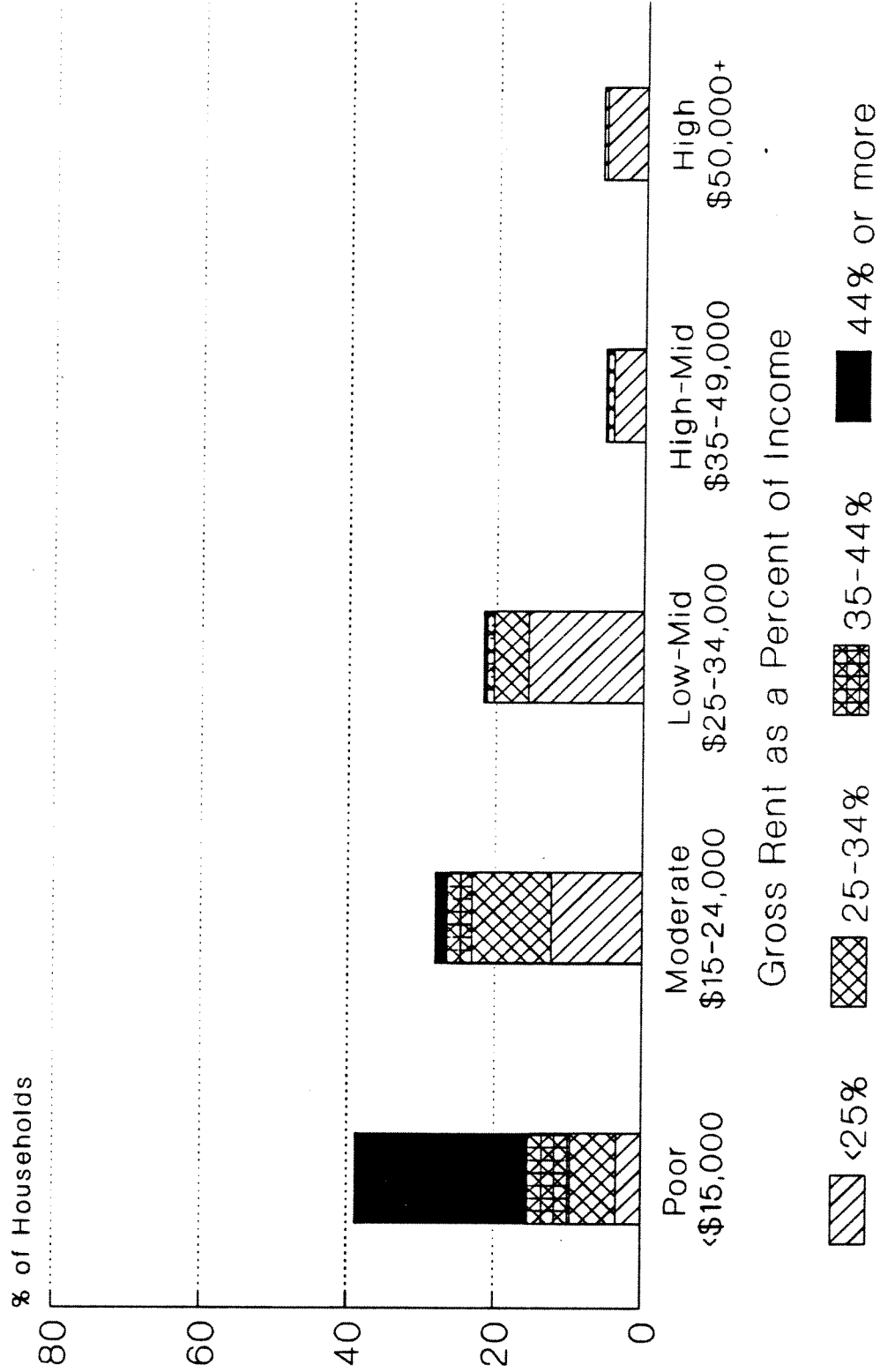
The District's renter population declined substantially in size during the second half of the 1970s, and this decline appears to have continued -- though at a less dramatic rate -- into the early 1980s. The decline in the size of the D.C. renter population occurred at the same time that the number of homeowners in the District was increasing and, as a result, the

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1. See Definitions, in this report, for the criteria used to identify physically deficient and overcrowded rental units. In addition, Section I of the Technical Supplement provides more extensive documentation of the incidence of these problems among D.C. renters.

# D.C. RENTER HOUSEHOLDS

## Rent Burden by Income Group - 1987



SOURCE: 1987 U.I. Tenant Survey

share of D.C. households who rent dropped precipitously from 70% in 1974 to about 62% today.<sup>1</sup>

At the same time that the District's renter population shrank in size, its composition shifted significantly, to include more young singles and adult groups and fewer families with children (see Exhibit 4).<sup>2</sup> Specifically, the share of non-elderly singles and groups of young adults increased from 42% to 57% between 1974 and 1987, while the share of families with children declined from 33% to 20%. Moreover, as Exhibit 5 illustrates, real incomes (adjusted for inflation) grew among singles and adult groups, but declined among all other types of renter households. In other words, the most affluent segments of the D.C. renter population became larger and even more affluent, while the more permanent core of elderly and family renters became smaller and poorer.

This shift resulted from two important trends, neither of which has been unique to the District of Columbia. First, the number of relatively affluent singles living alone or in groups of unrelated adults increased in urban areas throughout the U.S.; and second, middle-income families achieved homeownership and/or suburbanization at a high rate. Thus, the District's renter population -- like that of U.S. cities generally -- is increasingly composed of poor families and elderly people, who cannot afford to become homeowners, along with more affluent singles and adult groups, who are not yet ready to buy permanent homes.

The incidence of both physical deficiencies and crowding in the D.C. rental stock declined during the 1970s and 1980s, but affordability problems worsened:

<u>Percent of D.C. renters</u>	<u>1974</u>	<u>1987</u>
with excessive rent burdens	27.2%	42.4%
in physically deficient units	26.6	20.5
in overcrowded units	6.6	5.3

Because real incomes declined for most segments of the D.C. renter population between 1974 and 1987, prevailing rent levels

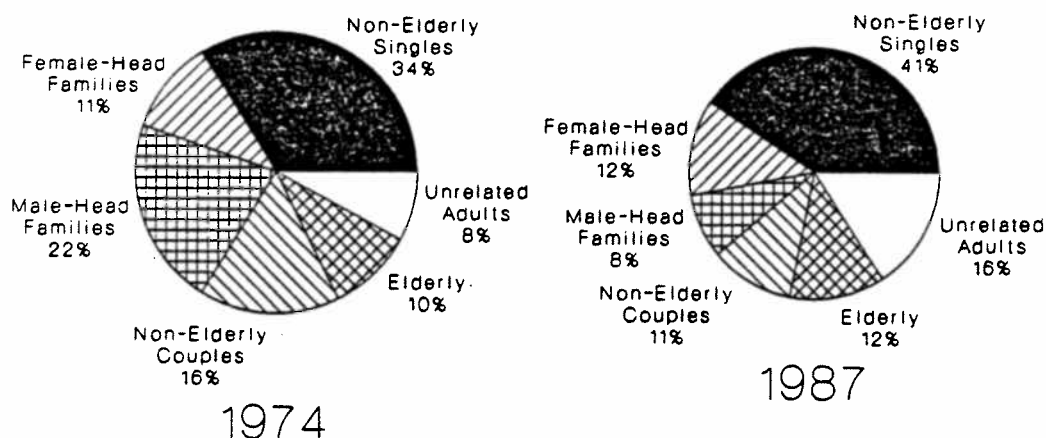
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1. Trends in the size of the D.C. renter population are obtained from published AHS data, which indicate that the number of D.C. renters declined from 180,000 in 1974 to 174,900 in 1977 and 159,900 in 1981. At the same time, the number of homeowners in the District increased from 77,700 in 1974, to 81,600 in 1977 and to 92,600 in 1981.

2. Using data on magnetic tape from the 1974 AHS for the Washington metropolitan area, we were able to classify households and their housing conditions in 1974 using the same definitions applied to our 1987 survey data.

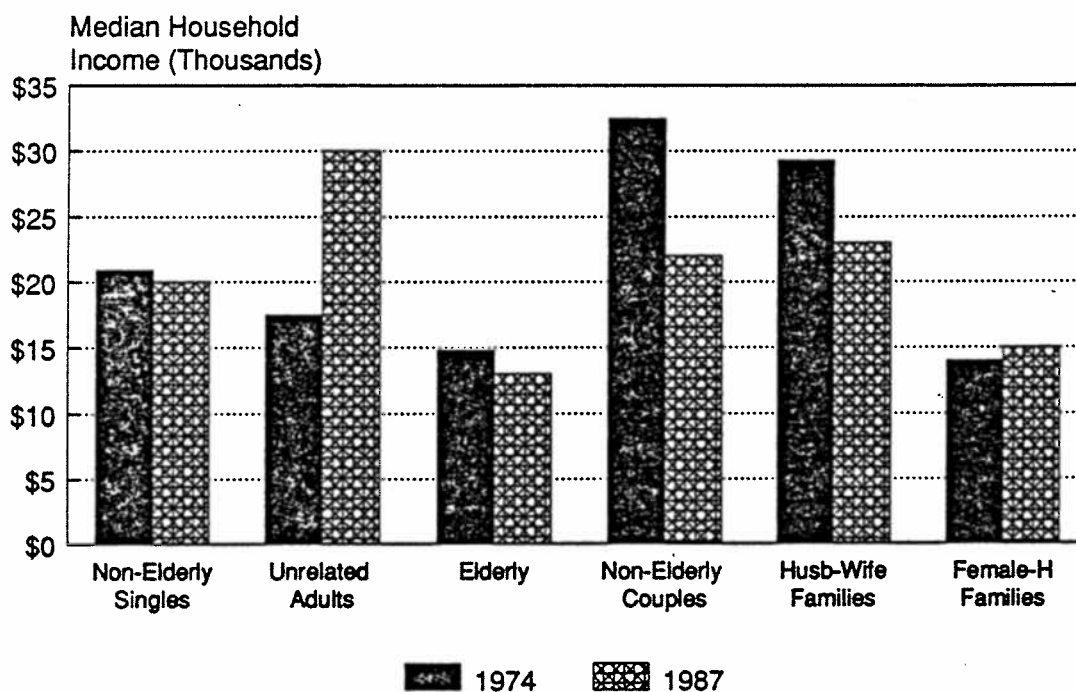
# D.C. RENTER HOUSEHOLDS

## Demographic Trends, 1974-1987



## EXHIBIT 5

## CHANGES IN MEDIAN REAL INCOMES OF D.C. RENTERS -- 1974 AND 1987



Median Household Income in 1987 Dollars

outstripped renter incomes. Overall, gross rents in the District increased at an average annual rate of 7.8% between 1974 and 1987, while renter incomes rose only 6.1% annually. The result has been a sharp decline in the affordability of rental housing, particularly for the most vulnerable segments of the renter population. Today, the majority of elderly and female-headed renters in the District pay more than 30% of their income for housing.

% paying over  
30% of inc for rent

Non-Elderly Singles	36.9%
Adult Groups	43.0
Elderly	64.8
Non-Elderly Couples	39.4
Husb-Wife Families	41.7
Female-Hd Families	59.9

While the problems of housing affordability in the District are serious, and have worsened markedly in recent years, they are not as severe, nor have they worsened as sharply, as in many other central cities of the U.S. We selected seven cities of the Northeast and Mid-Atlantic states to provide a basis for analyzing conditions and trends in the D.C. rental market. None of these cities is exactly like D.C., but all have some important similarities and differences. Five of the cities (Atlanta, Baltimore, Hartford, Philadelphia, and Pittsburgh) are uncontrolled, while Boston and Newark have local rent control programs.<sup>1</sup> Renters in all of these central cities have experienced more dramatic increases in affordability problems than have D.C. renters:

Median share of income for housing  
mid 1970s                  early 1980s

Atlanta	24%	30%
Baltimore	25	31
Hartford	28	32
Philadelphia	26	34
Pittsburgh	24	29
 Boston	 28	 31
Newark	26	31
 D.C.	 21	 23

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1. See Section I of the Technical Supplement for more on the characteristics of these comparison cities.

In general, rent levels have increased even more rapidly in other central cities than in D.C., while renter incomes have lagged even farther behind. As a result, the median central city renter in the U.S. as a whole pays 31% of income<sup>1</sup> for rent, while in D.C. the median rent burden is only about 23%.

### Changes in the Rental Housing Stock

During the 1970s, the total number of rental units in the District declined substantially -- from 199,100 in 1970 to 170,500 in 1981. This decline occurred despite new rental construction averaging about 740 units per year, and is attributable to the removal of at least 3,340 units from the rental stock annually. Two key, demand-side forces explain the 15% decline in the size of the District's rental housing inventory between 1970 and 1981. First, as discussed earlier, the total number of middle and upper income renters in the District dropped substantially, due to the loss of households to the suburbs and the rising rate of homeownership among those remaining in the District. At the same time, among renters for whom the option of homeownership was unaffordable, incomes failed to keep pace with inflation. Thus, the top end of the rental market was eroded by a decline in the aggregate level of demand, while the bottom end of the market was eroded by a decline in the real purchasing power of low and moderate income renters.

The 1970s represents a period when the opportunities for both homeownership and suburbanization were unusually attractive, not only in the District of Columbia, but throughout the country. High marginal tax rates and rapid inflation made homeownership increasingly attractive to anyone who could afford a downpayment, and the suburbs were more hospitable to minorities than they had been at any time in the past. Thus, the aggregate level of demand for rental housing declined substantially. Roughly one quarter of the net decline in the rental housing stock was matched by a drop in the total number of households living in the District, and almost half was matched by conversions to homeownership.<sup>2</sup> The fact that rental vacancy rates remained constant between 1974 and 1981 testifies to the fact that the total supply of rental housing in D.C. declined by roughly the same amount as the total level of demand. Moreover, as Exhibit 6

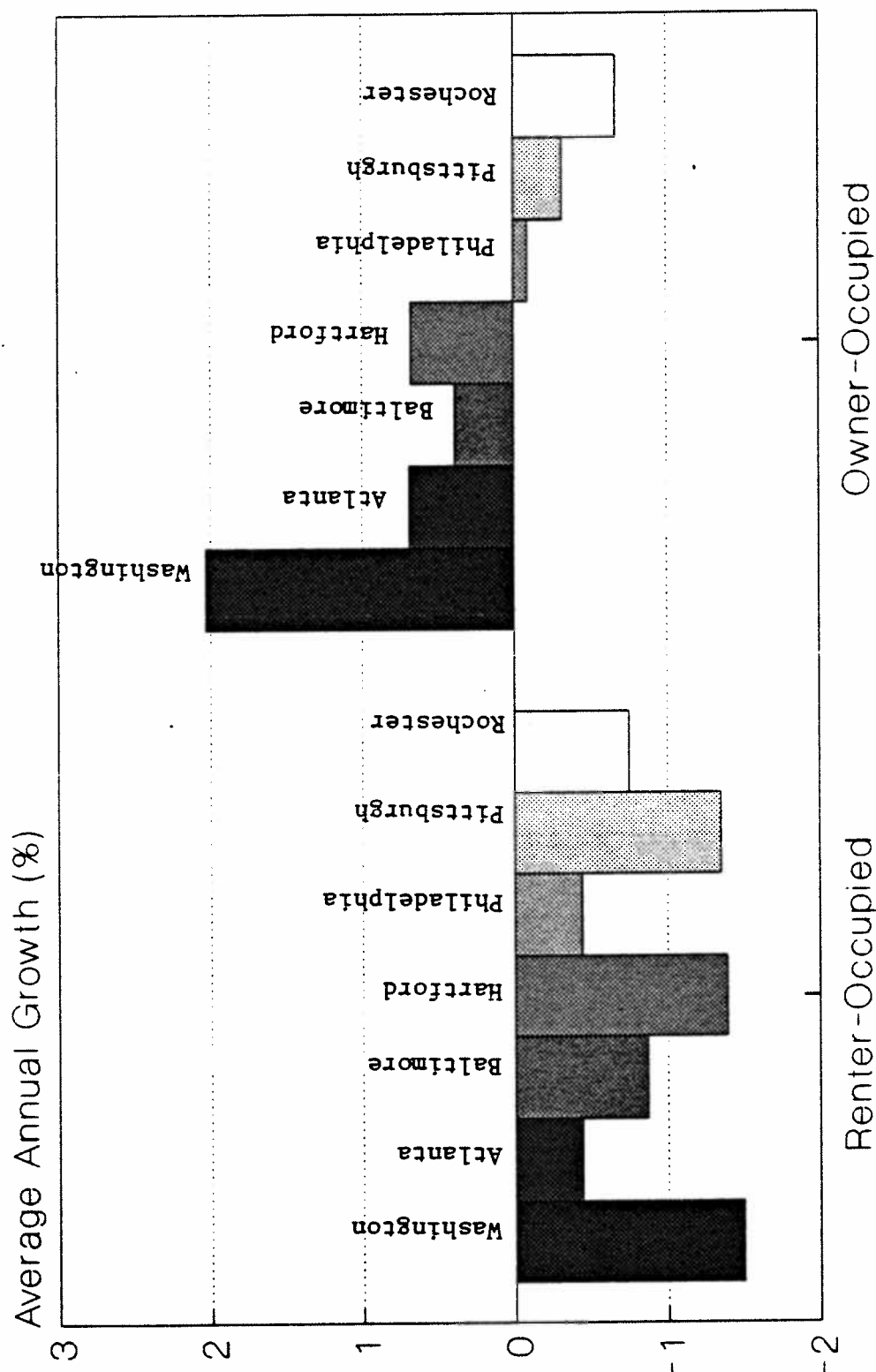
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1. Based on published AHS data for individual central cities and for the average of all U.S. central cities. The AHS is not conducted every year in all metropolitan areas. Therefore, data for Atlanta are from 1975 and 1982, Baltimore -- 1976 and 1983, Hartford -- 1975 and 1983, Philadelphia -- 1975 and 1982, Pittsburgh -- 1974 and 1981, Boston -- 1974 and 1981, Newark -- 1974 and 1981, and D.C. -- 1974 and 1981.

2. This analysis of change in the rental housing inventory during the 1970s is based on published AHS data on rental and owner-occupied units in the Washington metropolitan area.

# U.S. CENTRAL CITIES

## Trends in the Housing Stock, 1970-1983



SOURCE: AHS 1973-1983



shows, this pattern was by no means unique to the District of Columbia -- during the 1970s central cities throughout the country lost renter households (and housing units) to the combined attractions of homeownership and suburbanization.

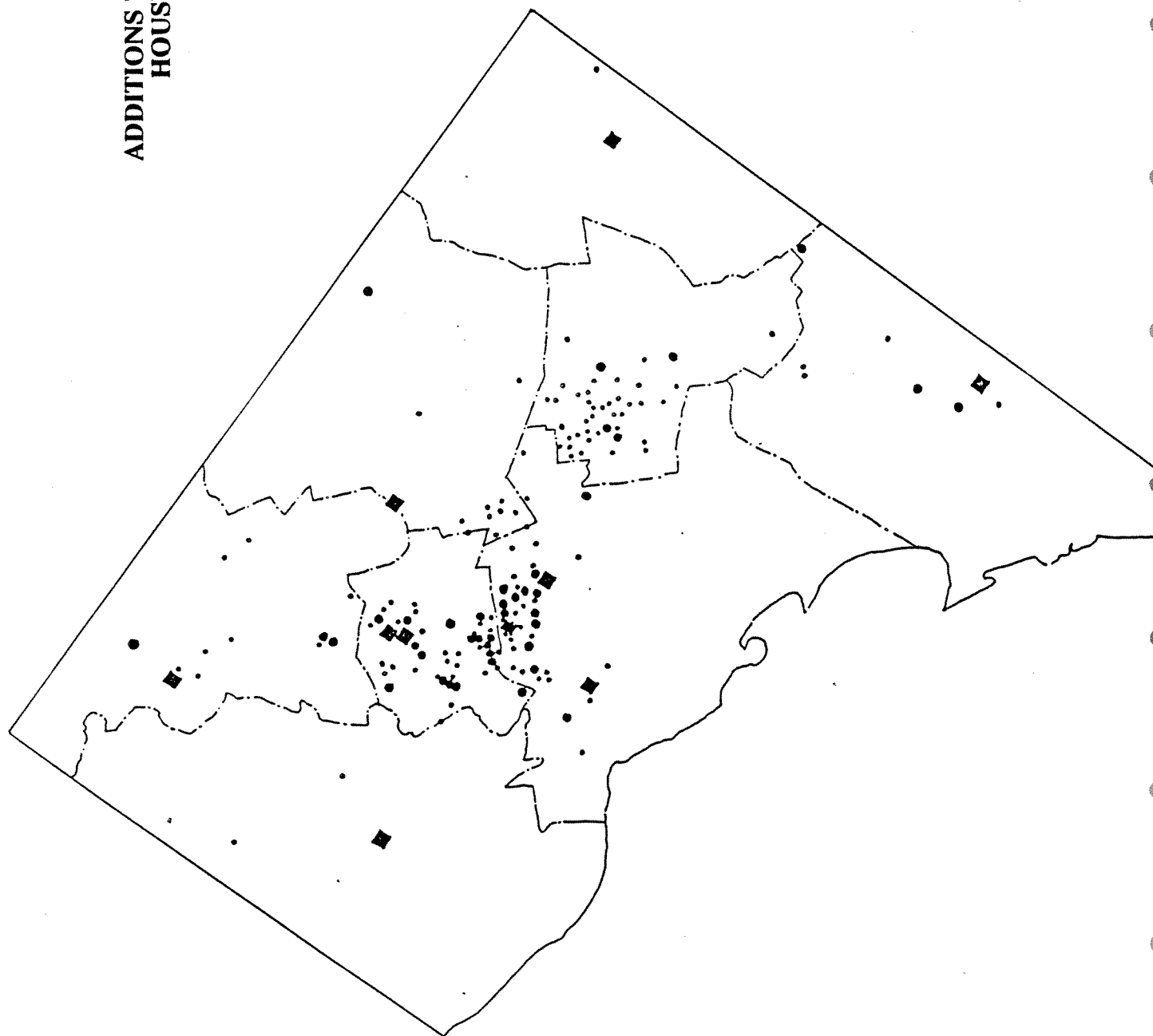
During the first half of the 1980s, the decline in demand for rental housing in the District slowed considerably. In other words, demand for rental housing in the District began to stabilize during the first half of the 1980s, probably because rising interest rates, lower inflation, and reductions in marginal tax rates have all contributed to make homeownership much less affordable relative to rental housing. However, while the loss of renter households slowed considerably during the 1980s, the supply of rental units continued its decline at a somewhat faster pace. The result has been a dramatic drop in the rental vacancy rate from 6.2% in 1981 to 2.5% in 1985.

Since 1985, the District's rental housing stock has actually started growing again, both because units are being removed from rental use at a much lower rate than in the 1970s and because units are being added to the stock at a higher rate. This reversal represents a lagged response to the renewed demand for rental housing that began earlier in the decade. Our inventory of additions to and losses from the rental housing stock indicates that the number of units on the market increased by 1,631 between May 1, 1985 and April 30, 1987. Although new construction remained at roughly the same level as in the 1970s, the rental housing stock increased by about 800 units annually, because very few units were removed from the rental stock and because a relatively large number of units were added to the rental inventory through renovations or conversions from non-residential uses:

<u>Additions:</u>	<u>May 1985-April 1987</u>
New Construction	1,003
Substantial Rehabilitation	1,094
Change in Number of Units	70
Conversion from Owner-Occupied	106
Conversion from Non-Residential	398
Total Additions	2,621
<u>Losses:</u>	
Removed from Use	152
Demolished	11
Change in Number of Units	29
Conversion to Owner-Occupied	760
Conversion to Non-Residential	38
Total Losses	990
<u>Net Change:</u>	1,631

## EXHIBIT 7

### ADDITIONS TO THE DISTRICT OF COLUMBIA HOUSING INVENTORY, 1985-1987



#### Size of Structure

- 1-4 units
- 5-49 units
- ◆ 50+ units

While rental units were added to the stock in each of the District's eight wards, the majority of the 1985-1987 additions occurred near the center of the city, in a band bordering to the north and east the commercial and governmental downtowns of Ward 2 (see Exhibit 7). The greatest concentration of activity has been along the border between Wards 1 and 2, encompassing the area from Mount Vernon Square to Dupont Circle and north into Adams Morgan. This cluster -- which also spreads into the Mount Pleasant and Columbia Heights neighborhoods -- accounts for almost 60% of the rental units added between 1985 and 1987. A second significant cluster of additions occurred on Capitol Hill but, since these properties are typically small (1 to 2 units of rental housing), they do not contribute substantially to the rental stock. Finally, a handful of large rental projects (50 or more units) were added at outlying locations in Wards 3, 4, 7, and 8. Almost all of these large, outlying projects were subsidized, either federally or by the D.C. government.

The geographic pattern of losses from the District's rental inventory between 1985 and 1987 was similar to the pattern of additions, though somewhat more broadly dispersed. Again, a cluster of activity occurred around the border between Wards 1 and 2, with many of the larger properties that were removed from the rental stock located in this area. More than 50% of the units removed from the stock were located in Wards 1 and 2, compared to less than 6% in Wards 7 and 8.

Despite the relatively high rate of increase in the District's rental housing stock during recent years, fully half of the recent additions may not remain in the rental stock permanently, because they were developed as condominiums that are currently being rented rather than owner-occupied. In fact, the vast majority (81%) of condominium units built or renovated between 1985 and 1987 are currently being rented rather than owner-occupied. Thus, developers appear to be aware that the demand for rental housing in the District -- especially among the higher income singles and adult groups -- is sensitive to the relative attractiveness of owning versus renting. And units that are being added to the rental inventory in response to a resurgence in demand can easily be converted to owner-occupancy in response to renewed pressure for homeownership.

The recent additions to the District's rental housing stock have boosted the size of the inventory, but most do not respond to the needs of the city's low income renters. During the 1970s, three quarters of the building permits issued for rental housing construction and substantial renovation were for units subsidized by the federal government. By contrast, between 1980 and 1986, only one quarter of the rental building permits issued in the District were for subsidized units, reflecting both the virtual elimination of federal housing production programs and the

increase in the volume of unassisted rental production in the District.<sup>1</sup>

While most of the units added to the rental stock in recent years are not affordable to low and moderate income households, the vast majority of the units lost from the District's rental stock since the early 1970s rented for less than \$350 (in 1987 dollars).<sup>2</sup> Thus, the inventory of low cost rental units has declined substantially in size, resulting in a serious shortage of housing affordable for the District's low and moderate income renters. The resources of low and moderate income renters in the District -- particularly the elderly and families with children -- are too limited to make the ownership and maintenance of low and moderate cost rental properties profitable. As a result, the number of unsubsidized rental units that are affordable for low and moderate income households in the District falls far short of the need for these units:

	low income <u>&lt; \$15,000</u>	moderate income <u>\$15,000-\$24,000</u>
number of households	49,000	37,000
number of affordable units	42,000	28,000

In all, there are about 25% more low and moderate income renters in the District than there are units that these households can reasonably afford.

#### Financial and Ownership Profile of the Rental Stock

Just as there are several distinct groups of renter households in the District, the owners of rental units differ in significant respects. Based on our survey of a sample of D.C. housing providers, we have defined six categories of property owners:

- 1) individual owners with small D.C. holdings -- fewer than 10 rental units overall;

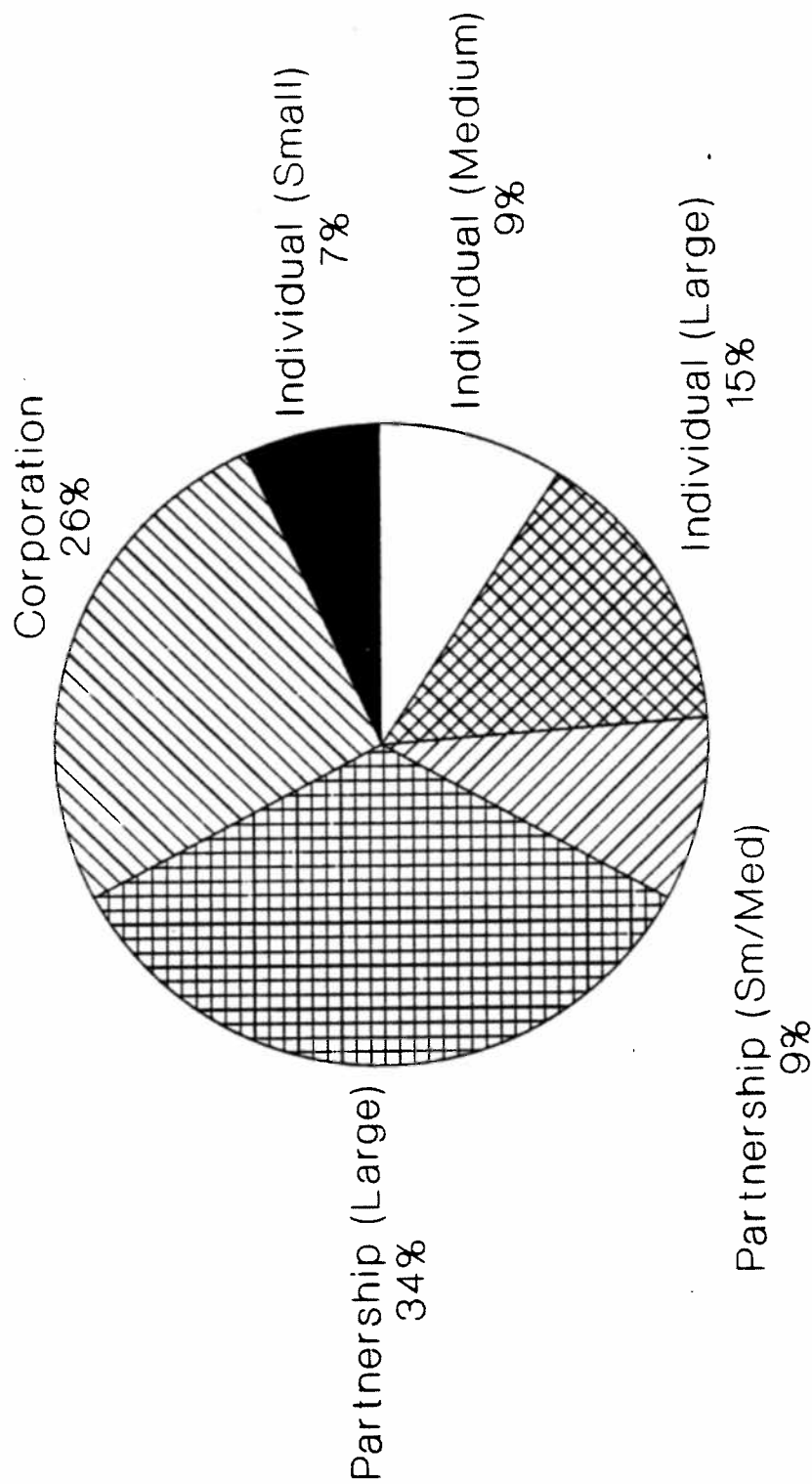
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1. These estimates are obtained from tabulations of building permits in the Washington metropolitan area assembled by the local HUD field office. Note that, since 1984, local subsidy programs have played a small but significant role in the production of D.C. rental housing, accounting for half of the subsidized units that received building permits between 1984 and 1986 -- or about 10% of all rental units for which building permits were issued.

2. Based on published AHS data on rent levels of units removed from the rental inventory.

# CONTROLLED RENTAL UNITS

Share of Units by Ownership Type



SOURCE: 1987 UI Housing Provider Survey

- 2) individual owners with medium holdings -- 10 to 49 units;
- 3) individual owners with large holdings -- totalling 50 or more D.C. rental units;
- 4) partnerships and joint ventures with small to medium holdings -- fewer than 50 units;
- 5) partnerships and joint ventures with large holdings -- 50 or more D.C. units; and
- 6) corporations -- almost all of which own 50 or more D.C. rental units.

This classification scheme reflects the fact that almost no partnerships or corporations own fewer than 10 units of rental housing in the District, and that few corporations own fewer than 50 units.<sup>1</sup>

The vast majority of controlled units in D.C. are owned by large property holders -- including individuals and partnerships with large holdings as well as corporate owners (see Exhibit 8). Small individual housing providers account for a relatively small share of the District's controlled rental stock. The units held by small providers are primarily in small properties and, although their rent levels are slightly below the average for all units, properties owned by small providers are generally in quite good physical condition. In fact, all of the units in our sample that are owned by small providers received "A" ratings from the District's housing inspectors. Most of the units with "C" ratings, on the other hand, are owned by large, corporate investors.

Three basic factors contribute to the profitability of any real estate investment: cash flow, expected property appreciation, and tax benefits obtained from the deductability of depreciation and other expenditures. Small individual owners of rental property in the District -- for whom real estate investment is typically not the primary income source -- place the greatest emphasis on tax and appreciation benefits as motives for investment, while large partnership and corporate investors are much more likely to emphasize cash flow.

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1. See Annex B for more details on the sample of controlled D.C. rental units, and our survey of the owners and/or managing agents of these units. In addition, see Section IV of the Technical Supplement for an extensive discussion of the financial and ownership characteristics of the District's controlled rental stock.

Most controlled rental units in the District generate cash returns that amount to less than 12% of current equity.<sup>1</sup> In fact, 22% of all controlled units actually generate negative cash flow. In other words, owners of these units have to supplement rent revenues each month to cover operating and interest costs. Small properties in particular (fewer than four units) are likely to generate little or no cash flow:

Property Size	Average per unit per year (1985)		
	<u>Revenues</u>	<u>Expenditures</u>	<u>Net Income/Equity</u>
1-2 units	\$4,573	\$4,754	-5.4%
3-4 units	3,053	2,943	1.0
5-9 units	3,300	2,699	4.6
10-19 units	3,519	2,831	7.0
20-49 units	4,179	3,601	5.6
50-99 units	4,215	3,152	7.8
100-249 units	4,811	3,658	10.8
250 + units	4,812	3,958	10.9

This is not necessarily because rent levels are low, but often because high property values and high levels of indebtedness boost interest and property tax expenditures. Regardless of the underlying reasons, however, it appears that small owners -- who are most likely to own the small properties -- are unlikely to enjoy substantial cash returns from their controlled holdings.

However, property appreciation substantially increases the economic return on most categories of controlled rental property in the District, and -- at least until the enactment of the Tax Reform Act of 1986 -- the rate of return on investment in D.C. rental property was largely tax free:<sup>2</sup>

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1. The financial data presented in this section were obtained from registration statements filed with DCRA for 1985. Equity is derived by applying reported equity to value ratios to DFR data on each property's assessed value as of 1985. Note that these assessed values may fall short of market value, and that, as a result, our estimates of equity may be low.

2. For details on the estimation of appreciation benefits and after-tax returns, see Section III of the Technical Supplement.

Property Size	Average per unit per year (1985)		
	Cash Flow	Appreciation	After-Tax Return/ Equity
1-2 units	\$ -181	\$2,441	10.4%
3-4 units	110	1,805	18.7
5-9 units	601	1,044	12.4
10-19 units	688	566	11.7
20-49 units	578	567	10.3
50-99 units	1,063	754	11.8
100-249 units	1,153	349	12.4
250 + units	854	-199	10.1

It is important to note that these profitability measures represent estimates of returns to investment in average properties. They obviously do not represent the actual profit levels realized by particular investors. However, while approximate, these estimates demonstrate that cash returns understate the economic rewards from property ownership, particularly for small providers. Moreover, the average after-tax rate of return for most categories of controlled rental housing in the District is in the 10% to 12% range, which compares favorably to returns on other investment opportunities.

Not surprisingly, units that are in poor physical condition generate much lower rates of return than those in a better state of repair. On average, units with poor inspection ratings generate -2.3% cash return on equity -- implying that revenues regularly fall short of expenditures. Estimated after-tax returns are positive (roughly 2% on average), but substantially below the levels generated by units that are in better physical condition. While the circumstances of individual properties differ, we find no evidence that D.C. owners are systematically profiting from the deterioration of distressed rental properties. Instead, the poor financial showing among deteriorated rental units is directly attributable to low rent levels -- per unit expenditures among these properties are comparable to those of higher quality units, but rent revenues are uniformly low. We have no way of knowing which came first -- low rent levels or poor property conditions -- but the data do suggest that properties with chronic code violations are likely to be financially distressed as well, and that rent revenues simply may not be adequate to support the repairs and capital improvements that are needed.

### Summary of Key Findings

This chapter provides an overview of conditions and trends in the D.C. rental housing market, including the characteristics of renter households, the housing problems they face, recent changes in the stock of rental housing, characteristics of housing providers, and the financial returns to investment in controlled rental property.



## Renter Households and Housing Problems

The District's renter population consists of about 157,900 households, of whom 18% receive federal or local rent subsidies

Non-elderly singles and groups of unrelated adults form an ethnically diverse and relatively affluent group, and tend to be newcomers to the D.C. area who participate only temporarily in the District's rental market. In contrast, families and elderly households who rent housing in the District are predominantly black, generally poorer, and much more likely to be long-term renters in the city.

Excessive costs constitute the most widespread housing problem for D.C. renters, and the problem of housing affordability is particularly severe for those who are poor.

During the 1970s, the the District's renter population shrank in size and -- like that of U.S. cities generally -- is increasingly composed of poor families and elderly people, who cannot afford to become homeowners, along with more affluent singles and adult groups, who are not yet ready to buy permanent homes.

The incidence of physical deficiencies in the D.C. rental stock declined during the 1970s and 1980s, but affordability problems have worsened.

While the problems of housing affordability in the District are serious, and have worsened markedly in recent years, they are not as severe, nor have they worsened as sharply, as in many other central cities of the U.S.

## Rental Housing Availability

During the 1970s, the total number of rental units in the District declined substantially, in conjunction with the decline in the number of renter households.

Early in the 1980s, the District's renter population stabilized, but the rental inventory continued to decline in size. As a result, vacancy rates plummeted from about 6% in 1981 to less than 3% in 1985.

Since 1985, the District's rental housing stock has actually started growing again, but while the recent additions to the District's rental housing stock have boosted the size of the inventory, most do not respond to the needs of the city's low income renters.

The inventory of low cost rental units has declined substantially in size, resulting in a serious shortage of housing affordable for the District's low and moderate income renters.

## Rental Housing Ownership and Profitability

The vast majority of controlled units in D.C. are owned by large property holders -- including individuals and partnership with large holdings as well as corporate owners.

Small individual housing providers account for a relatively small share of the District's controlled rental stock, and although their rent levels are slightly below the average for all units, properties owned by small providers are generally in good physical condition.

Most controlled rental units in the District generate cash returns that amount to less than 12% of current equity.

However, property appreciation substantially increases the economic return on most categories of controlled rental property in the District, and -- at least until the enactment of the Tax Reform Act of 1986 -- the rate of return on investment in D.C. rental property was largely tax free.

## 2. D.C. HOUSING PROGRAMS

This chapter describes three major D.C. government programs that intervene in the workings of the rental housing market for the purposes of making rental housing more affordable and preserving the quality of the existing stock. These programs are 1) the rent control program itself; 2) housing code enforcement; and 3) the Tenant Assistance Program (TAP).<sup>1</sup> Our objective in analyzing these three programs is to understand how they operate and what their limitations are, not to evaluate the efficiency of their administration. Thus, this chapter is intended to provide the programmatic details needed to fully assess the impacts of rent control on the District's rental housing market.

Housing code enforcement and the Tenant Assistance Program interact with the operation of the District's rent control program, and play important roles in determining how effectively the goals of the Rental Housing Act of 1985 are advanced. Rent control's primary objective is to moderate the rate at which rent levels for most units in the District increase, thereby making rental housing more affordable. Housing code enforcement is intended to preserve the quality of the existing housing stock, and, since there is the potential for maintenance and housing quality to be neglected in an environment where rent revenues are restricted, it is particularly important to understand how housing code enforcement interacts with the existing system of rent controls in the District of Columbia. And finally, the District's Tenant Assistance Program (TAP) focuses on the housing problems of low and moderate income renters, making direct rental assistance available to those who -- even in a controlled market -- pay excessive rent burdens or live in physically deficient or overcrowded units.

### The Operation of the Rent Control Program

About two thirds of the rental units in the District of Columbia are subject to rent control -- 101,100 rental units. Exemptions from controls are granted for the following categories of units:

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1. There are additional District programs that interact with rent control and that could well have been included in this examination, particularly the conversion and sale restrictions on rental property, tenant eviction protections, and the production subsidy programs currently being implemented by the Department of Housing and Community Development. However, the study's original mandate from the City Council called for an assessment of TAP and an analysis of how the new Civil Infractions Program affects housing code enforcement. Because the Civil Infractions Program has not yet been implemented for rental housing, we have provided a baseline analysis of the existing housing code enforcement process.

units owned by small housing providers -- individuals whose total D.C. holdings amount to four or fewer units;

new and substantially rehabilitated units -- in buildings constructed or renovated after 1975, or units created in existing buildings after 1979;

units in buildings that have been continuously vacant since 1985;

units owned by housing cooperative associations (with certain restrictions); and

subsidized units -- receiving federal or local project-based subsidies under programs other than TAP.

Given the limited circumstances in which exemptions are allowed, the units whose rents are unregulated differ systematically from those in the controlled stock. Almost 12,000 units of the exempt stock are in public housing projects, and another 17,700 are in privately owned projects built with federal subsidies. While these subsidized units clearly serve low and moderate income households in the District, the remaining stock of approximately 33,000 unsubsidized rental units that are exempt from controls contains more than its share of large, new, and expensive rental units:

	unsubsidized D.C. rental units <u>controlled</u>	<u>exempt</u>
% with 4+ rooms	40%	55%
median rent	\$400	\$455

The District's system of rent stabilization regulates both the frequency and the amount of rent adjustments. Rents charged for any unit must be at or below the unit's rent ceiling. Rent ceilings were initially set at 1974 rent levels, but there are several ways in which a unit's rent ceiling can be increased under the District's system of rent control. First, two types of adjustments are available to any accommodation that is licensed, registered, and in compliance with the District's housing code. These are 1) the increase of general applicability -- which allows the rent ceiling for a continuously occupied unit to rise by the previous year's Consumer Price Index (CPI), and 2) the vacancy increase -- which allows the rent ceiling for a unit that has been vacated to increase by 12% or to the rent ceiling for a comparable unit in the same property, whichever is higher. In addition, housing providers can petition to "pass through" cost increases associated with capital improvements, substantial rehabilitation, or changes in services or facilities. And finally, providers can obtain administrative approval for extraordinary rent increases necessitated by financial hardship, or secured by means of voluntary agreements with tenants.

The vast majority of rent controlled units (86%) charge rents at or very near their rent ceilings. And for units renting below their ceilings, the explanation most often given is that restrictions on the frequency of rent increases prevent the provider from raising the actual rent to the rent ceiling. But not all providers may have obtained the highest rent ceilings allowable under the law. Based on our surveys of tenants and housing providers, and on a sample of tenant and provider petitions filed over the last several years, we have analyzed the extent to which both housing providers and tenants make use of the provisions available under the District's existing rent control program.

**The Increase of General Applicability and Vacancy Rent Adjustments.** Most providers make use of the generally applicable rent adjustment process, with nine out of ten controlled D.C. rental units experiencing this type of increase in 1986. Although units are required to be substantially in compliance with the D.C. housing code to qualify for this rent adjustment, almost 20% of the tenants who reported a rent increase in the past twelve months also reported serious physical deficiencies. While our measure of physical deficiencies does not correspond precisely to the District's housing code, this evidence does suggest that a significant minority -- perhaps 10% to 15% -- of controlled units in the District implement the generally applicable rent increase despite substantial code violations.

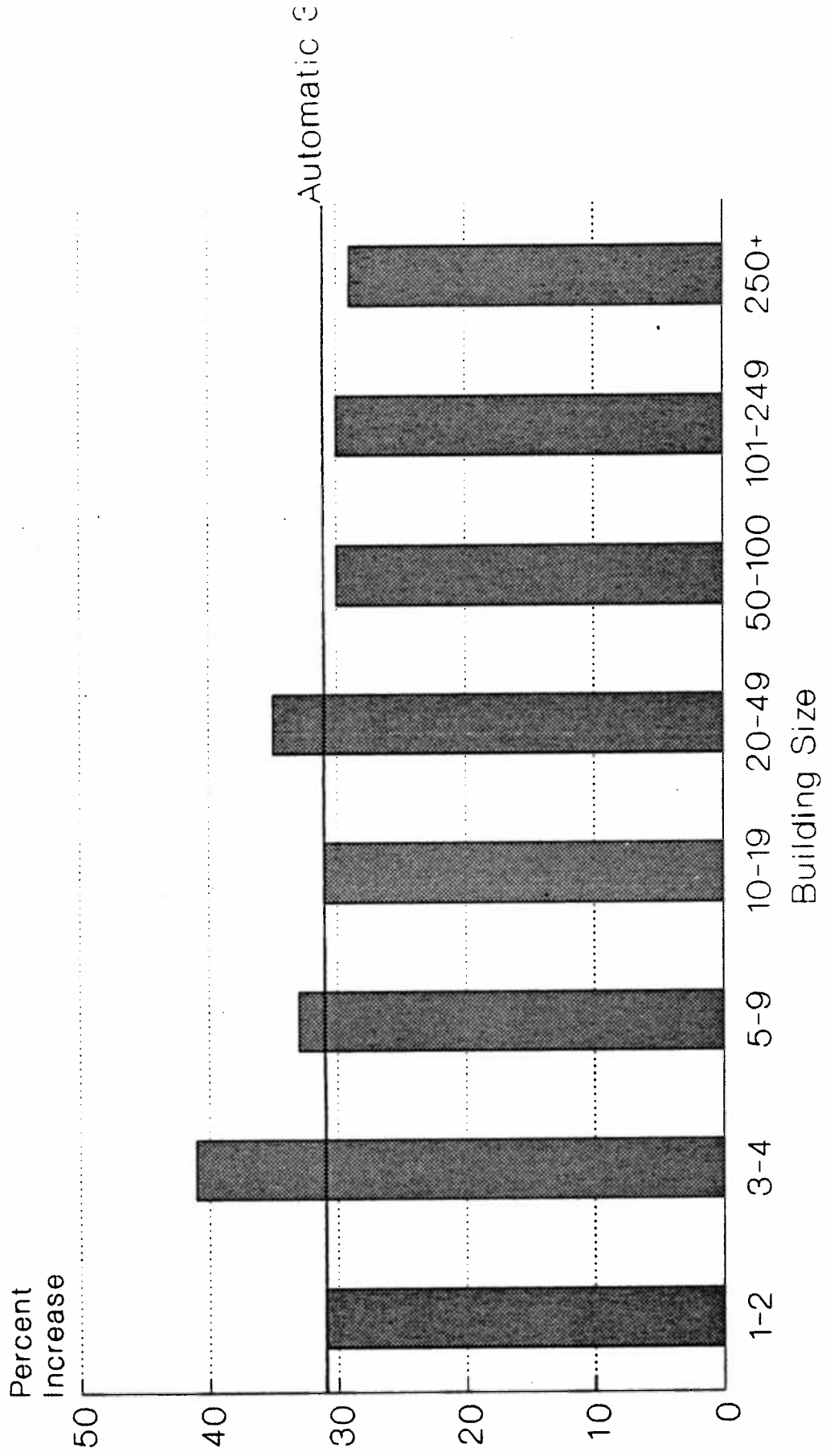
For most types of rental property in the District, the rent adjustments of general applicability have kept pace with increases in operating costs during the 1980s. As illustrated in Exhibit 9, even for units continuously occupied from 1981 through 1987, allowable rent adjustments would have kept pace with increases in the costs of operations for most types of rental properties.<sup>1</sup> The increase of general applicability resulted in an overall increase of 31% in rent levels over the 1981 to 1987 period. Average properties in most size categories experienced cumulative operating cost increases at or below this level. Only properties in the three to four unit size category experienced substantially higher increases -- averaging about 41%. And our analysis suggests that the above average rate of cost escalation experienced by these properties was primarily attributable to dramatic increases in assessed values and, hence, property taxes and interest payments. Thus, these properties have experienced above average cost increases and reduced cash flow over the past several years, but their property values, and hence appreciation benefits have increased substantially as well.

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1. Our estimates of the rate of actual operating cost inflation in the District between 1981 and 1987 is based on price changes for each operating cost item. We obtained estimates of price changes from published data or directly from the providers of services and materials. For details, see Section VI of the Technical Supplement.

EXHIBIT 9

# OPERATING COST INCREASE BY BUILDING SIZE 1981-1987 (In Percent)



SOURCE: The Urban Institute

Since roughly 10% of units in the District turn over annually, most housing providers have the opportunity to increase their overall rent revenues at a somewhat higher rate than that of continuously occupied units. Indeed, providers indicate that revenues are much closer to market levels in buildings with high turnover than in buildings where most tenants are long time stayers. However, the vacancy adjustment process can create some serious anomalies in rent levels; both tenant representatives and housing providers with whom we spoke cited examples of buildings in which two similar apartments have substantially different rents because one has been continuously occupied while the other has turned over more recently. In fact, a large apartment that has been recently occupied may rent for less than a small apartment occupied at the same time, if the small apartment has turned over more frequently in the past or if other small apartments in the same building have experienced frequent turnover.

**Tenant and Housing Provider Petitions.** In addition to the generally applicable rent adjustment and vacancy rent increases, in 1986 about 8 percent of all controlled units in the District experienced additional increases in rent ceilings approved through one of the petition processes.<sup>1</sup> Exhibit 10 presents the number of landlord and tenant petitions filed from 1983 to 1987. Housing providers filed hardship petitions, capital improvements petitions, and voluntary agreements at roughly comparable rates in 1986 and 1987. But tenant petitions are by far the most common type of petition, although their volume declined substantially from over 600 in 1985 to about 350 in 1987.

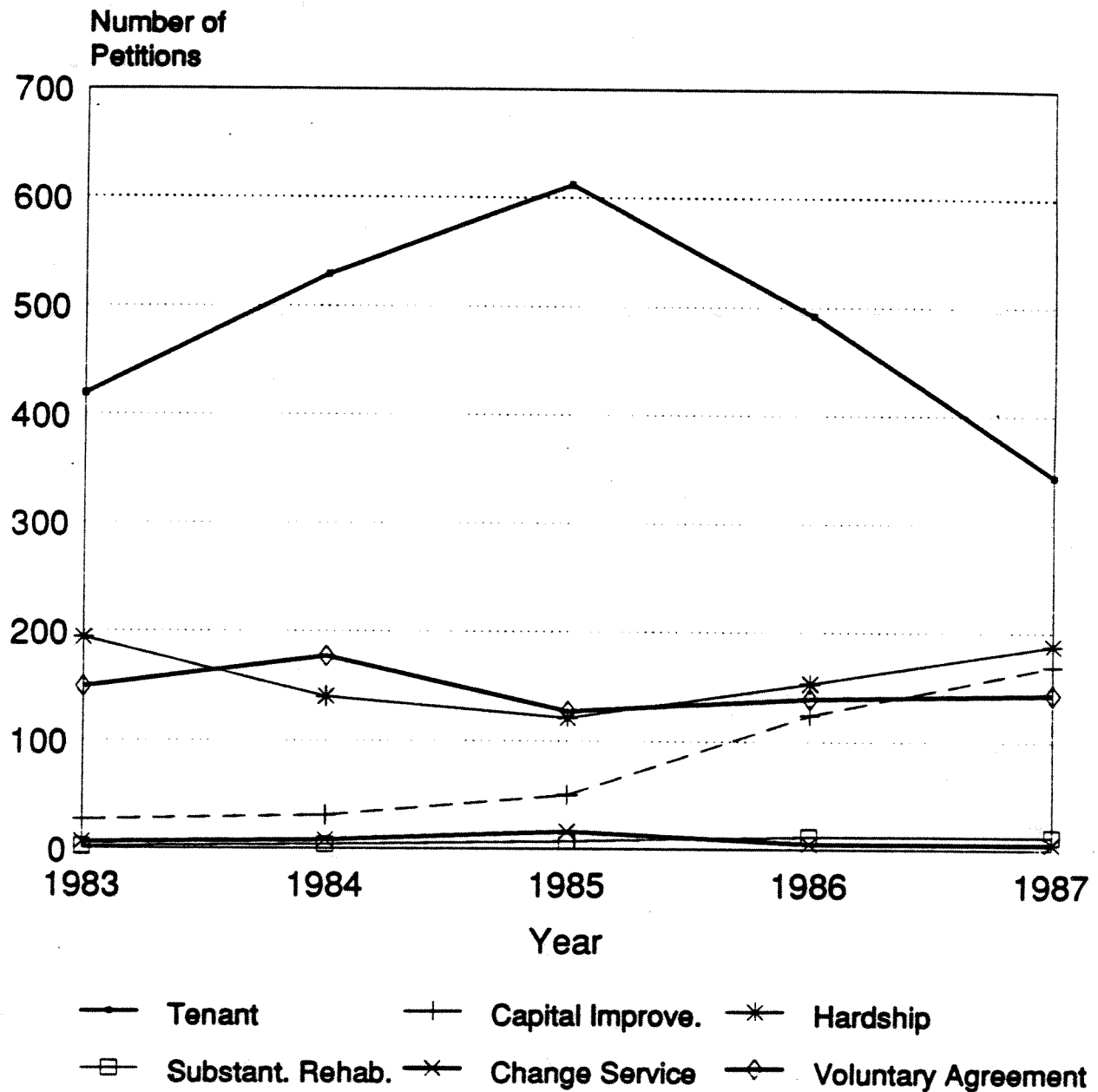
The resolution of tenant petitions -- through the Rental Accommodations and Conversions Division (RACD) of the District's Department of Consumer and Regulatory Affairs (DCRA) -- is often achieved through informal mediation, with many petitions settled prior to any formal hearing. Of those that reach the formal hearing stage, a large share (more than half) do result in rent roll-backs, reductions in allowable rent increases, or other remedial action on the part of housing providers. From this perspective, the tenant petition process appears to serve an important function as a means for mediating disputes between housing providers and tenants. However, from the perspective of housing providers, the threat of tenant petitions is one of the more onerous aspects of the District's rent control program. Providers with whom we spoke reported that a minor mistake in the calculation or timing of rent adjustments could result in substantial legal costs and possibly penalties if a tenant chose to pursue the petition process to its limits. These providers also agreed, however, with the reports of tenant representatives

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1. This analysis of the volume and outcome of rent control petitions is based on a review of DCRA records for all types of petitions filed in 1985-1987. See Annex B for more details.

EXHIBIT 10

# LANDLORD AND TENANT PETITION FILINGS BY YEAR AND PETITION TYPE 1983-1987



Source: Supplied by R. A. C. D.



that some landlords purposely violate the rights of their tenants, and that mechanisms for identifying and penalizing these intentional violations are essential.

Housing providers are entitled to file for hardship rent increases if a property's annual cash return falls short of 12% of current equity. Between 1983 and 1987, 125 to 200 hardship petitions were filed annually. Large and small properties file hardship petitions in numbers roughly proportionate to their share of the total controlled stock. Almost all of the properties that file hardship petitions receive rent increases, although generally not for the full amount requested. Among those filing hardship petitions, rent ceilings were increased by an average of 46% in 1987. This average has declined considerably since the first half of the 1980s, although the hardship increases approved for small properties have increased dramatically, and are now substantially higher than the increases approved for large properties, as illustrated in Exhibit 11.

As discussed in Chapter 1, our estimates of returns to investment indicate that the majority of controlled rental units in the District fall short of the 12% annual rate of return allowed under the hardship provisions of the current rent control program.<sup>1</sup> How do the 188 properties that filed for hardship increases in 1987 differ from the vast majority that did not? The differences do not appear to be dramatic. Among large properties, those seeking hardship petitions have above-average operating costs, but among small properties, the dominant characteristic of those filing hardship petitions is above-average levels of equity rather than unusually high operating costs. In fact, small properties filing for hardship rent increases experienced higher overall rates of return than the average for small properties generally.

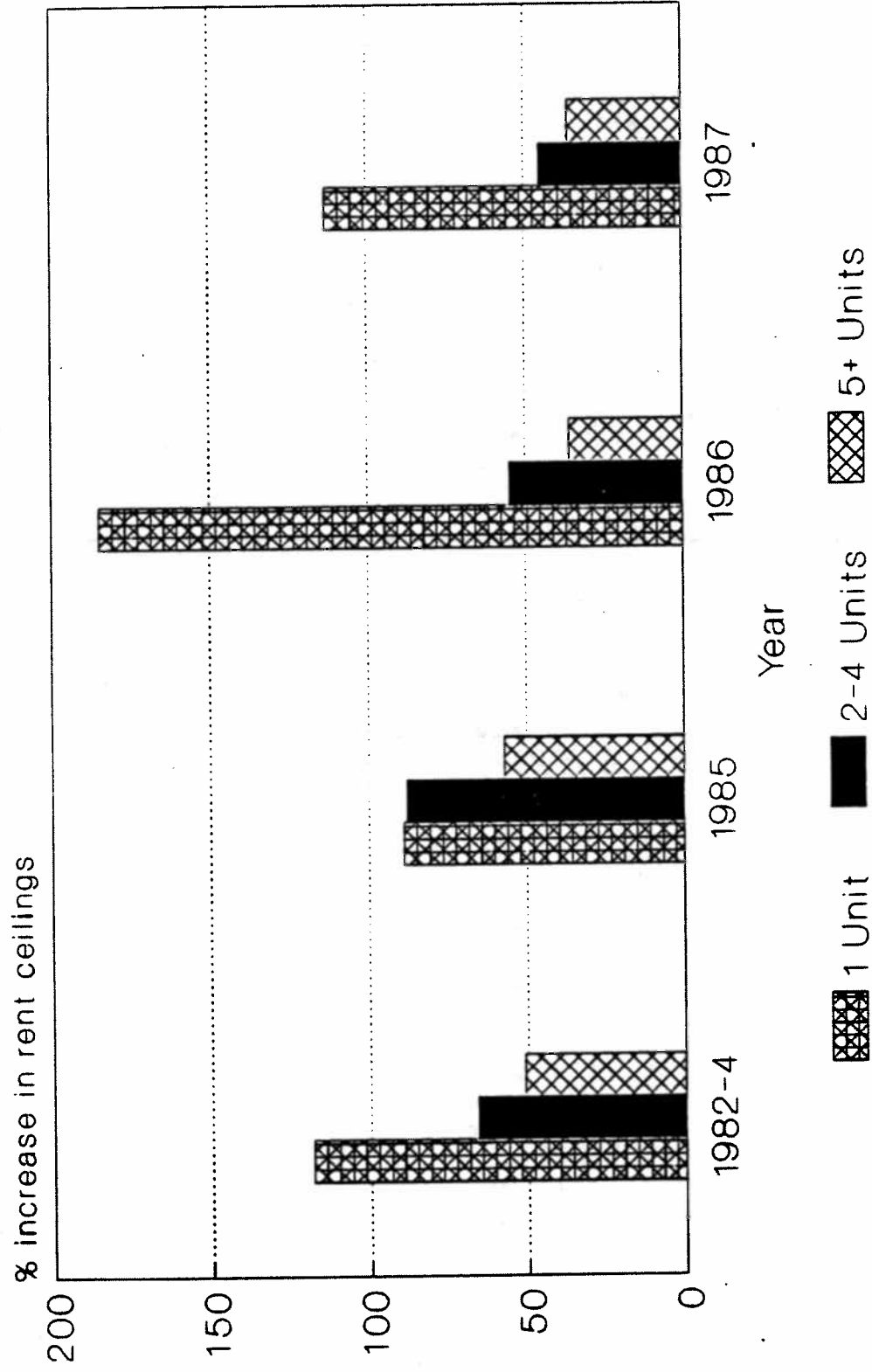
There are several interrelated explanations for the low rate of hardship petitions, given the fact that most controlled units in D.C. generate cash returns low enough to qualify for hardship increases, and the fact that the increases that have been approved over the last several years have been sizeable. First, the administrative and legal costs of filing a hardship petition are substantial. Not only is it time consuming to assemble the necessary documentation to support a petition, but a challenge by tenants is very likely, necessitating further expenditures for protracted legal representation. Indeed, almost two thirds of housing providers whose units generate less than 12% cash return indicate that it takes too long to file for a hardship

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1. Since assessed values for multifamily rental properties are generally thought to be lower than actual market values, an even greater share of controlled rental units may earn less than 12% cash return on equity than our estimates (which are based on assessed values) suggests. In particular, recently financed properties may have debt in excess of their assessed values, even though their owners have significant levels of equity at risk.

EXHIBIT 11

# AVERAGE INCREASES ON HARDSHIP PETITIONS BY BUILDING SIZE AND YEAR



SOURCE: The Urban Institute

rent increase, and about 60% indicate that the legal and accounting costs are too high.<sup>1</sup>

However, if a housing provider can anticipate a 40% to 50% increase in annual rent revenues as a result of a successful hardship petition, the legal and administrative costs would probably be justified. Thus, we can infer that many of the properties that currently qualify for hardship increases would not generate 12% cash return on current equity even in the absence of controls. In other words, providers know that their tenants are either unwilling or unable to pay substantially higher rents, even if a hardship rent increase was granted. Moreover, we know that, for many housing providers, appreciation gains and tax benefits are more important investment motives than cash flow, so that there may not be strong incentives to file hardship petitions.

However, some distressed properties may be inhibited from filing for hardship rent increases even though they need them desperately. For properties with low revenues and significant physical deficiencies, housing providers may find themselves in a kind of "catch-22" -- their current rents are too low to finance needed repairs, but a hardship increase cannot go into effect until the property passes a housing code inspection. If there is a high degree of delay and uncertainty involved in the process of applying for and obtaining a hardship rent increase, banks are unlikely to help finance the needed improvements. For these properties, the administrative and legal requirements involved in applying for a hardship petition and completing the required building improvements may in fact pose an unsurmountable hurdle, so that the hardship petition process may not, in fact, be meeting the needs of the most vulnerable properties.

An alternative for housing providers who seek substantial increases in rent ceilings is to negotiate voluntary rent increases with their tenants. Between 1985 and 1987, approximately 150 voluntary agreements were filed each year. D.C. housing providers appear to negotiate voluntary rent increase agreements with tenants for rental properties that are in better than average financial condition. Large and small properties seek this type of increase in numbers roughly proportionate to their share of the total housing inventory, and -- like hardship petitions -- voluntary agreements typically result in substantial increases in rent ceilings -- the average 1986 increase was 46%.

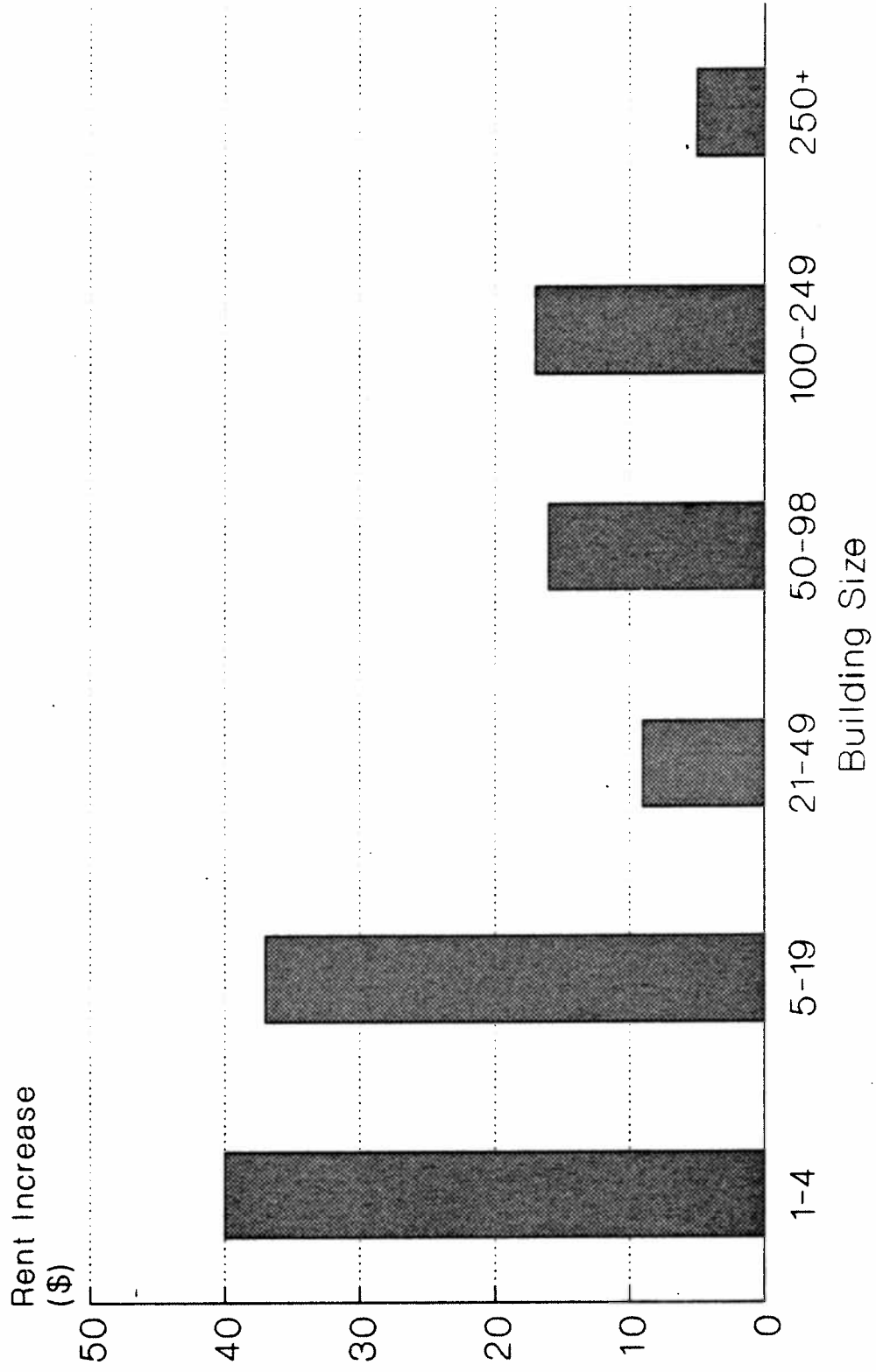
Capital improvements and substantial rehab rent increases are designed to allow owners to improve the quality of their rental properties and to raise rents sufficiently to recapture the costs of their incremental investments, and -- in the long term -- to

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1. These results are obtained from our mail-back survey of a sample of owners and/or managers of the controlled properties for which we obtained financial statements.

EXHIBIT 12

# AVERAGE PER-UNIT RENT INCREASES APPROVED FOR CAPITAL IMPROVEMENTS 1986



SOURCE: The Urban Institute

earn a higher return on their equity. The volume of substantial rehab petitions has remained at almost negligible levels over the 1980s, but the number of capital improvements petitions has increased dramatically from about 50 per year from 1983 through 1985, to more than 150 in 1987. Unlike hardship petitions and voluntary agreements, capital improvement petitions are much more likely to be sought by owners of large rental properties, and the resulting rent increases are substantially lower. As illustrated in Exhibit 12, the largest increases have been experienced by small properties, where capital improvements petitions have resulted in approved rent increases averaging from \$35 to \$37 per month. For large properties, the average rent increase amounted to only about \$17 per month.

**Understandability of the Rent Control Program.** The various provisions of the District's existing system of rent control are designed to balance the interests of tenants in keeping rent levels low against the interests of housing providers (and ultimately tenants) in making rental housing investment sufficiently profitable to attract investment. The result of this balancing is a rather complex set of rules governing rent increases, but the majority of D.C. housing providers report that they find this system reasonably understandable. Owners of 78% of controlled units in the District rate their understanding of the District's rent control provisions as "good" or "excellent." Individual investors with small holdings are less confident of their understanding of the local rent control provisions, with only about 60% claiming a "good" or "excellent" understanding. As illustrated below, the provisions that create the greatest confusion for housing providers in the District are those dealing with the timing of rent adjustments:

Percent of controlled units whose owners  
have difficulty understanding:

coverage of controls	7%
permitted increases	17
vacancy allowances	18
eviction procedures	22
unit recovery	18
base & ceiling rents	20
timing of adjustments	37
tenant petitions	6
other	10

### Housing Code Enforcement

The District government has designed a systematic approach to housing code enforcement, in an effort to ensure that housing providers maintain their rental properties, and that the quality of the city's rental housing inventory is preserved. The existing system is currently in the process of being revised in

response to the Civil Infractions Act. The analysis presented in this section is intended to provide an overview of how the system has been working, and to serve as a base-line for future assessments of housing code enforcement in D.C. This section describes how the existing system is intended to operate as well as how it operates in actual practice, with special attention to the sources of delays in the resolution of housing code violations.

All licensed residential properties (buildings with housing business licenses) in the District are subject to annual scheduled inspections. Properties with histories of code violations are subject to more frequent and intensive inspections than those that have had few serious violations in the past and have promptly corrected any violations cited by inspectors. More specifically, all licensed residential properties in the District receive an inspection rating of A, B, or C, where an A rating indicates that a building has had no serious violations, few minor violations, and a history of prompt code compliance. In contrast, a C rating is applied to properties with several serious violations, numerous minor violations, or a history of poor code compliance. Buildings with A ratings -- which account for 80% of controlled rental units -- are subject to one license inspection annually, with only a sample (roughly 10%) of the units in an A-rated building are targeted for inspection at each visit. Buildings with B and C ratings are subject to two license inspections annually, with half of the units in B buildings and all of the units in C buildings targeted for inspection at each visit.

In addition to scheduled inspections, D.C. rental properties are inspected in response to complaints by tenants and/or neighbors. In fact, the vast majority of inspections actually occur as a result of complaints rather than through the scheduled inspections process. Over the last three years, the Housing Inspection Division (HID) has conducted a large volume of complaint-based inspections -- 17,632 in 1985, 20,187 in 1986, and 46,884 in 1987. Since the advent of the 8DC-HELP program, which funnels telephone complaints from city residents to the appropriate city agencies, the volume of complaint inspections has grown by an estimated 300%.

While the volume of complaint-based inspections is high, HID has not always been able to meet its objective of conducting scheduled inspections in all licensed properties.

	<u>1985</u>	<u>1986</u>	<u>1987</u>
Buildings with at least one scheduled inspection	4,042	10,615	5,573
Percent of licensed buildings	38%	100%	53%

And unfortunately, the records maintained by HID do not make it possible to determine the number of buildings inspected

annually on the basis of complaints, or the total number of buildings subjected to one or more inspections of any kind in a given year.

Exhibit 13 outlines the established procedures for processing housing inspections in the District of Columbia. When code violations are found by housing inspectors -- either in a scheduled inspection or on the basis of a complaint -- notice is served to the property owner (or agent), who is required to abate the violations within a designated time period. Abatement times are delineated by the inspectors, based on their assessments of the severity of the violations, the threat to tenants' health and safety, and the time involved in effecting the necessary repairs. Abatement of emergency violations may be required within hours, while other serious violations are scheduled for abatement within ten days. A reinspection is scheduled to confirm that violations have indeed been eliminated. When violations are not abated by property owners, inspectors generally schedule a reinspection, but in circumstances where the code violations create an imminent danger to the health or safety of tenants, the inspector may refer properties to the Assessments branch of the Department of Consumer and Regulatory Affairs, which will contract to make the repairs required, and place a levy or lien on the property in the amount of these costs. Owners who persistently fail to abate code violations can also be referred to the District's Corporation Council for criminal prosecution.

The Housing Inspections Division (HID) will soon begin implementing the District's new Civil Infractions Program for housing code enforcement. This program authorizes HID to fine property owners for housing code violations rather than (or in addition to) referring those who fail to correct violations for criminal prosecution. The Civil Infractions Program is intended to encourage property owners to comply with the District's housing code, to create incentives for abating violations promptly when notices are issued, and therefore to improve the condition of the District's housing stock.

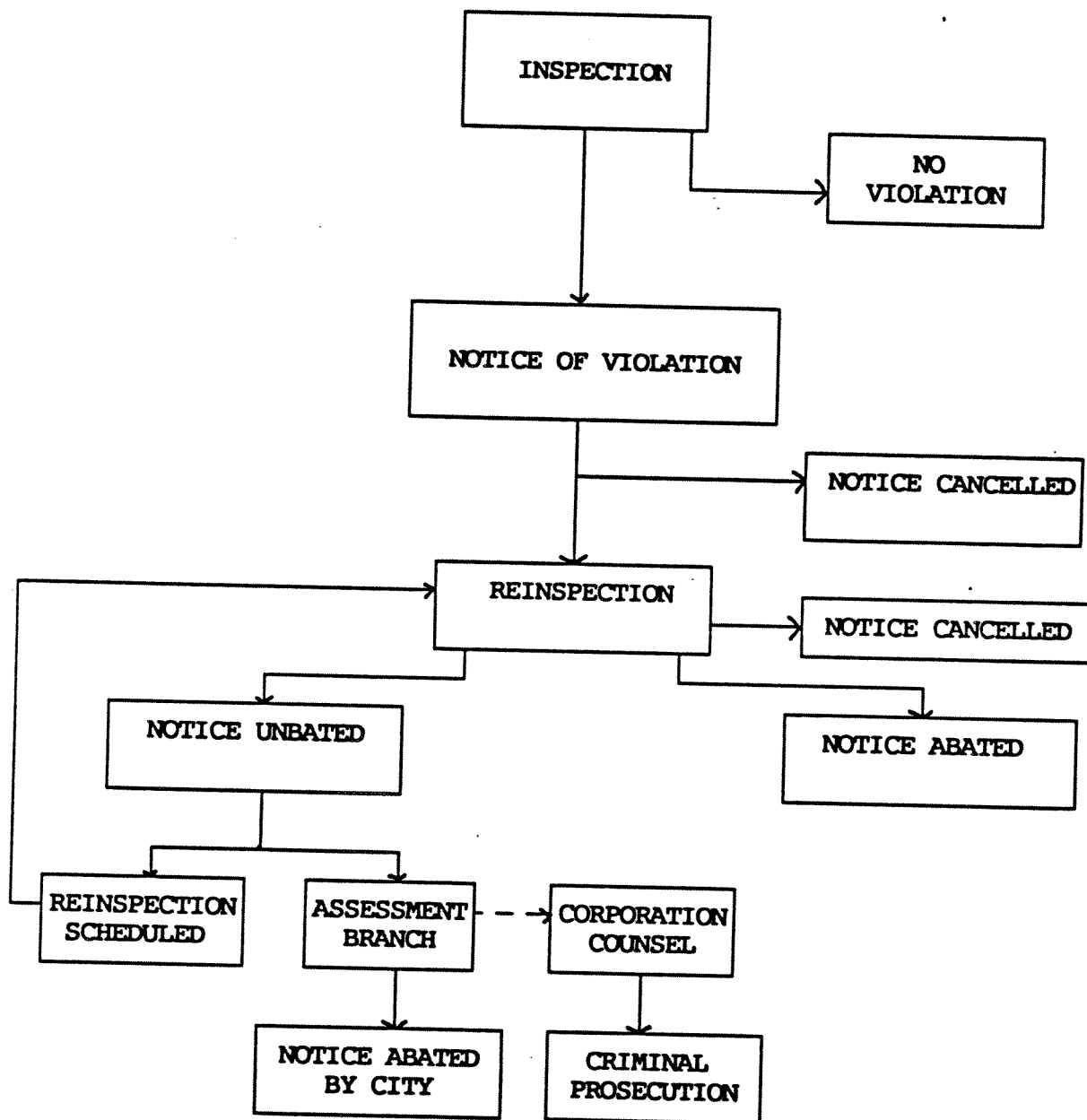
Under the existing enforcement system, the majority of code violations cited by District housing inspectors are ultimately abated by property owners.<sup>1</sup> Of the 647 notices of violation included in our sample, 501 (77%) were abated by the owners, 9 were referred to Assessments for abatement by the City, and 137 (21%) were cancelled, either because of excessive delays by HID or because tenants did not allow inspectors into their units for reinspection. When notices are cancelled it is entirely possible

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1. The analysis that follows is based on the inspection and code enforcement histories gathered from HID files for a sample of 319 rental properties. This represents all of the cases from our original sample of 814 controlled rental properties for which inspection histories were available from HID files. See Annex B of this report and Section VII of the Technical Supplement for more details.

## EXHIBIT 13

## THE HOUSING CODE ENFORCEMENT PROCESS





that many of the individual violations cited have been abated, and that only one or two are still outstanding. While most D.C. housing providers ultimately abate violations cited by housing inspectors, abatements generally are not recorded within the times allotted by housing inspectors:<sup>1</sup>

	Median number of days	
	<u>In Designated Compliance Period</u>	<u>From First Inspection to Date Abatement Recorded</u>
Emergency Notices	1	6
Serious Notices	5	22
Non-Serious Notices	20	88

There are three critical sources of delay in the existing enforcement process: 1) delay in the service of violation notices to property owners; 2) delay in reinspection to determine whether abatement has occurred; and 3) delay by property owners in performing needed repairs. As illustrated by Exhibit 14, each step in the enforcement process typically takes longer than the original compliance deadline imposed by the housing inspector. Clearly, however, HID has been successful at processing emergency violations on an accelerated schedule, and serious violations receive higher priority than those designated as non-serious.

Housing providers are clearly responsible for some of the delays in the abatement process. Specifically, the need for multiple reinspections for roughly one third of all violation notices indicates that providers do not always correct all violations promptly upon receipt of a notice. However, almost every phase of the abatement process could be substantially accelerated by means of more prompt action by housing inspectors. First, notices often are not served until several days after an inspection has taken place, and the enforcement clock does not start ticking until service of notice has occurred.<sup>2</sup> Second, inspections and reinspections could be scheduled to coincide more closely with the designated abatement times, so that providers know that a housing inspector will arrive to ensure that violations have been abated within the time specified. In some instances, reinspections appear to be hampered by tenants, who are unwilling to give up their keys, or to make themselves available to admit inspectors to their units. HID is currently

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1. Note that there is, in fact, no way to know exactly when abatement actually occurs. We simply know when abatement was recorded by the housing inspector.

2. Legal requirements regarding the service of notice necessarily impose some unavoidable lag time.

## PROCESSING TIME FOR NOTICES OF CODE VIOLATION

	SERIOUS NOTICES	NON-SERIOUS NOTICES
	Median Time	Median Time
Inspection to Notice Served	4 Days	19 Days
Compliance Deadline	5 Days	20 Days
Notice Served to 1st Reinspection*	13 Days	46 Days
1st Reinspection to 2nd Reinspection	8 Days	15 Days
2nd Reinspection to 3rd Reinspection	12 Days	19 Days
3rd Reinspection to 4th Reinspection	12 Days	14 Days
4th Reinspection to 5th Reinspection	16 Days	4 Days
1st Reinspection to Date Abatement Recorded	22 Days	88 Days

	EMERGENCY NOTICES	
	LESS THAN 1 DAY COMPLIANCE DEADLINE	1 DAY COMPLIANCE DEADLINE
Inspection to Notice Served	1 Day	1 Day
Compliance Deadline	4 Hours	1 Day
Notice Served to 1st Reinspection*	2.5 Days	5 Days
1st Reinspection to 2nd Reinspection	2 Days	4 Days
2nd Reinspection to 3rd Reinspection	2 Days	2 Days
1st Reinspection to Date Abatement Recorded	8 Days	8 Days

Source: 1985 HID files for 319 Sample Properties  
 \*Note: Includes designated compliance period

experimenting with conducting some reinspections by telephone (with tenants) as a mechanism for overcoming this problem. Finally, penalties could be imposed more aggressively, so that providers have a stronger incentive to respond as soon as they receive notices of housing code violations. The Civil Infractions Program may have the potential to achieve this objective, by authorizing housing inspectors to impose fines for unabated code violations, where in the past enforcement remedies have been limited to the more extreme (and time consuming) measures of Assessments and referral for criminal prosecution. However, since the Civil Infractions Program also offers the opportunity for housing providers to appeal their penalties, it may actually result in more lengthy delays.

### Direct Housing Assistance for D.C. Renters

A primary objective of the District's rent control program is to keep rent levels from rising too rapidly, and thereby to make rental housing more affordable for everyone. In addition, however, federal and local housing subsidy programs offer more direct assistance to low income households. This assistance can take one of four basic forms: 1) public housing developments; 2) federal assisted, private housing developments; 3) federal certificates and vouchers; and 4) D.C. Tenant Assistance Program (TAP) certificates. Public housing and federally assisted private housing projects currently serve 9,387 and 16,632 D.C. households, respectively. Another 1,200 D.C. renters receive federal housing certificates or vouchers, supplementing the rents they can afford to pay for conventional units within the existing housing stock.

In an effort to directly address the housing needs of low and moderate income renters who are not served by federal subsidy programs, the District enacted the Tenant Assistance Program (TAP) in 1985. This program, which began issuing certificates in 1986, is very similar in design to the federal Section 8 certificate program. Specifically, participating households contribute at least 30% of their income for rent, and TAP supplements this payment up to a predetermined "payment standard," which is based on the cost of adequate quality units of various sizes available from the existing rental stock. Thus, households who receive TAP (or federal Section 8) certificates seek conventional housing units from the existing, privately owned rental stock. Their landlords receive the same rents paid by unassisted tenants, but only a fraction is paid by the TAP recipient while the remainder is paid by the District government.

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1. According to the District's Department of Public and Assisted Housing, 2,567 of the city's 11,954 public housing units are currently vacant -- a vacancy rate of 21%. 192 of these vacant units are uninhabitable and scheduled for demolition, 1,418 are scheduled for modernization, and the remaining 957 are available for occupancy.

## EXHIBIT 15

## TAP INCOME ELIGIBILITY LIMITS

Number of Persons in Household	August 1987- Present
1	\$17,600
2	20,000
3	22,650
4	25,150
5	26,750
6	28,300
7	29,900
8	31,000

## TAP PAYMENT STANDARDS

## Existing Units

Unit Size	Low Rise	High Rise	New or Rehab Units
0 BR	\$ 437	\$ 529	\$ 651
1 BR	517	609	732
2 BR	588	790	812
3 BR	707	—	891
4 BR	792	—	1,014
5 BR	911	—	1,166
6 BR	1,030	—	1,318

Exhibit 15 summarizes income eligibility levels and payment standards under TAP. Altogether, 41% of the D.C. renters who do not already receive assistance under federal housing programs are eligible to participate TAP -- a total of about 53,000 households. Approximately \$15 million in annual subsidies have been allocated for the program, enough to assist between 3,400 and 3,500 households, given current subsidy levels per recipient.<sup>1</sup>

However, as of January 1988, only 2,581 TAP certificates had been issued, and roughly half of these certificate holders (1,095 households) had succeeded in finding units in which they could actually receive benefits under the program. In other words, only about two in five certificate recipients are currently receiving benefits. Some of these certificate holders are engaged in the housing search process, and will ultimately become subsidy recipients. Allowing for a 90 day search period, we estimate that half of all TAP certificate holders ultimately become program participants -- a success rate of 50%.

Because of the slow rate at which certificates have been issued and the relatively low success rate among certificate recipients, a number of program variants have been introduced to TAP in an effort to increase the number of households served. The program now consists of the following components:

The General Application Program is the basic, tenant-based component of TAP, modeled on the federal Section 8 program.

The Emergency Component of TAP was originally established as a set-aside for special needs populations, but became a separate program in 1987. Its objective is to provide a mechanism for processing emergency cases outside of the regular program waiting list. To date, 28% of all TAP households have been served under this component, including many who were homeless or about to become homeless.

The Designated Housing Unit Program is a variant on the basic, tenant-based approach adopted by the District under TAP. This component reserves 15 years worth of subsidies for designated units -- including units in properties receiving hardship rent increases, distressed properties participating in DHCD's Distressed Property Improvement Program, and properties undergoing substantial rehabilitation or new construction. As of January 1988, only five properties had participated in this program.

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1. Because TAP has been slow to spend the funds it has been allocated, the 1988 allocation of \$15 million has been reduced to only about \$10 million. See Section V of the Technical Supplement for more details on the design and implementation of TAP.

The In-Place Program is the most recent addition to TAP and, is only now being implemented. This component is designed to assist eligible households who already live in units that meet program standards, but who pay excessive rent burdens. In principle these households could participate under the General Application Program as well, but the In-Place Program will take applications jointly from tenants and housing providers, will apparently maintain a separate waiting list, and will expedite processing because no housing search will be involved.

The introduction of these program variants may increase the rate at which households are enrolled in TAP, but additional efforts should be focused on both the rate at which certificates are issued and the share of certificate recipients that succeed in finding units in which they can actually begin to receive subsidy benefits. Given the pool of unused subsidy funds available and the volume of need in the community, issuing more certificates, and boosting the success rates of certificate recipients should be TAP's short-term priorities. If these efforts are successful, it may then become critical to determine what share of the available subsidy funds to allocate to each program component, since these components serve different segments of the eligible population.

TAP currently has a waiting list of over 10,000 households, most of whom submitted pre-applications during a two-week application period (in May 1986) that was preceded by a series of Public Service Announcements and the publication of the application form in area newspapers. The program is currently closed to new applications, other than emergency cases, which are processed through the Department of Human Services. Less than one third of all the households who are eligible to participate in TAP know about the program. Participants appear to be among those with the most urgent needs for housing assistance -- they are poorer, more predominantly black, and less likely to be elderly than the population of eligible households:<sup>1</sup>

	<u>Eligible Households</u>	<u>TAP Recipients</u>
Elderly	33%	12%
Black	74%	98%
Incomes --		
<\$15,000	77%	94%
\$15-\$24,000	23	6
\$25,000+	0	0

---

1. Characteristics of eligible households were obtained from our survey of D.C. renters, while characteristics of TAP recipients were obtained from program files.

Based on a review of TAP administrative procedures, we recommend four important changes to increase the volume of certificates issued. The first of these is already in the planning stages:

Establish a one-stop application desk for all tenant subsidies. This will reduce the burden on needy households to go from office to office to apply for various assistance programs, and it will reduce the number of walk-ins to the TAP offices.

Centralize the scheduling of enrollment interviews and take into account the fact that roughly one third of scheduled appointments are likely to result in no-shows. The TAP manual suggests that enrollment interviews should be scheduled centrally, but currently TAP specialists schedule their own interviews, so that there is no way of knowing whether they are working as efficiently as possible.

Provide the TAP office with adequate clerical support so that specialists are not answering the telephones and responding to individuals who walk into the office without appointments.

Reduce the burden on TAP specialists of responding to call-backs from TAP recipients with problems related to their current units, landlords, or neighborhoods. One approach to this problem might be to designate an individual staff member to respond to these call-backs. Another might be to coordinate with the 8DC-HELP program to provide an effective referral service.

If these administrative reforms were implemented, TAP specialists would be able to issue certificates more efficiently, and their supervisors would be in a better position to determine whether more specialists are needed (possibly on a temporary basis) to issue all of the available certificates as promptly as possible.

Even if a greater volume of TAP certificates could be issued, roughly half of the households who receive them can be expected to return them, unused, due to their inability to find a qualifying unit. This 50% success rate is also typical of the federal Section 8 program, which has had much longer to overcome administrative start-up programs. One way to address the relatively low success rate is to provide TAP recipients with more aggressive assistance in the housing search process. Currently, TAP staff provide certificate recipients with a list of buildings known to accept TAP recipients, and have taken some steps to promote the program among the city's housing providers. A more assertive approach would include three important components:

Develop a comprehensive data base of available units throughout the city.

Aggressively promote TAP to housing providers.

Offer one-on-one housing search assistance to TAP recipients who need to move to qualify for assistance. This assistance can range from counseling on how to search for housing and how to make the most of an interview with a housing provider to actually accompanying individuals when they look for units.

These activities would not necessarily have to be performed by TAP staff. They might be performed jointly for TAP and the federal Section 8 certificate and voucher programs, or they might be contracted out to one or more of the non-profit housing counseling agencies that operate in the District of Columbia.

Even with housing search assistance, it is possible that a substantial share of TAP certificate holders (perhaps 30% to 40%) will not be able to find units in which they can receive benefits. There are two explanations for persistently low success rates among TAP and federal Section 8 certificate holders. First, housing providers may be reluctant to participate in assistance programs, and second, there simply may be too few units available at rents close to or below the payment standard. The evidence suggests that both of these problems interfere with the provision of housing subsidy assistance in the District.

While it is illegal to discriminate on the basis of receipt of public assistance in D.C., only about half of the housing providers we surveyed indicated that they would be likely<sup>1</sup> to participate in TAP if approached by a certificate holder.

Share of rental units for which provider is unlikely to accept TAP tenants because:

don't want to get involved in government programs	73%
concerned about receiving timely payments	46%
program guarantees only one year of funding	37%
need more information to decide	19%
allowable rents too low	8%

---

1. Providers of 92% of the District's rental units are aware of TAP, according to our survey of a representative sample of owners and/or managers.



Many of these concerns were echoed by individual housing providers with whom we conducted in-depth interviews. In particular, providers are wary of committing themselves to a program which is funded on an annual basis, and fear that TAP households may include a large share of "problem" tenants, since the program is currently being used to address the emergency needs of homeless households.

A larger share of District housing providers (accounting for 71% of the rental stock) would be willing to participate in TAP on behalf of an existing tenant, suggesting that the In-Place Component may be substantially more effective at achieving enrollment than the General Application Program. Provider resistance to TAP should gradually recede in the face of the program's continued successful performance, and the provision of housing search assistance may help combat outright bias against TAP certificate holders. In addition, TAP should be aggressively marketed and promoted to housing providers, so that misperceptions about the program do not prevent needy households from receiving benefits.

In addition to the problem of resistance on the part of D.C. housing providers, the District's housing stock simply contains a limited number of units renting at or below the payment standards for both TAP and the federal Section 8 program. It is not necessarily that the payment standards are too low; substantially more than half (61.6%) of the District's rental units fall below the TAP payment standards and are free of physical deficiencies. In addition, among units that became available for occupancy within the last two years, roughly half fell below the payment standard, suggesting that units do become available for occupancy at rents that could potentially accomodate TAP participants.

Unfortunately, however, the number of low and moderate cost housing units (with rents below the payment standard) is not large enough to serve the combined number of low and moderate income households, and turnover occurs at an extremely low rate. As a result, by enhancing the ability of low-income households to afford moderate cost units, TAP increases the competition for the limited number of units available for occupancy in any year. The Designated Units Program may help address this problem by offering housing providers a guaranteed stream of rent subsidies that will encourage them to add units to the moderate cost rental stock, or to improve units that have fallen into serious disrepair. Thus, the long-term effectiveness of TAP may depend on the District's ability to induce the production of more moderate-cost rental units -- through the use of TAP and other subsidies -- to serve both TAP recipients and others with low and moderate incomes.

## Summary of Key Findings

This chapter describes three District programs that play critical roles in the rental housing market, and that are key to understanding the impacts of rent control on market outcomes. These three programs are the rent control program itself, housing code enforcement, and the Tenant Assistance Program (TAP).

### **The Rent Control Program**

The vast majority of rent controlled units (86%) charge rents at or very near their rent ceilings, and most providers make use of the generally applicable rent adjustment process, with nine out of ten D.C. rental units experiencing this type of increase in 1986.

For most types of rental property in the District, the rent adjustments of general applicability have kept pace with increases in operating costs during the 1980s.

A significant minority -- perhaps 10% to 15% -- of controlled units in the District implement the generally applicable rent increase despite significant code violations.

In addition to the generally applicable rent adjustment and vacancy rent increases, in 1986 about 8 percent of all controlled units in the District experienced additional increases in rent ceilings approved through one of the petition processes.

Only a fraction of the properties that are technically eligible for hardship rent increases file petitions for these increases, despite the fact that among those filing hardship petitions, rent ceilings were increased by an average of 46% in 1987.

The primary reason why so few housing providers file for hardship petitions is that the administrative and legal costs of filing are not justified by the rent increase that tenants would actually be willing and able to pay.

D.C. housing providers appear to negotiate voluntary rent increases with tenants in properties that are in better than average financial condition, and like hardship petitions, voluntary agreements typically result in substantial increases in rent ceilings -- the average in 1986 was 46%.

The number of capital improvement petitions filed annually has doubled since 1985, but these petitions typically yield quite modest rent increases. The largest capital improvement rent increases have been experienced by small properties, where capital improvements petitions have resulted in approved rent increases averaging from \$35 to \$37 per month. For large properties, the average rent increase amounted to only about \$17 per month.

## Housing Code Enforcement

The vast majority of inspections actually occur as a result of complaints rather than through the scheduled inspections process.

The majority of code violations cited by District housing inspectors are ultimately abated by property owners, but abatements generally are not recorded within the times allotted by housing inspectors.

There are three basic sources of delay in the existing enforcement process: 1) delay in the service of violation notices to property owners; 2) delay in reinspection to determine whether abatement has occurred; and 3) delay by property owners in performing needed repairs.

Housing providers are responsible for some of the delays in the abatement process. However, almost every phase of the abatement process could be substantially accelerated by means of more prompt action by housing inspectors.

## Tenant Assistance Program

Altogether, 41% of the D.C. renters who do not already receive assistance under federal housing programs are eligible to participate TAP -- a total of between 54,000 and 56,000 households. Approximately \$15 million in annual subsidies have been allocated for the program, enough to assist between 3,400 and 3,500 households, given current subsidy levels.

As of January 1988, only 2,581 TAP certificates had been issued, and roughly half of these certificate holders (1,095 households) had succeeded in finding units in which they could actually receive benefits under the program.

The recent introduction of new program variants may increase the rate at which households are enrolled in TAP, but additional efforts should be focused on both the rate at which certificates are issued and the share of certificate recipients that succeed in finding units in which they can actually begin to receive subsidy benefits.

Only about half of the housing providers we surveyed indicated that they would be likely to participate in TAP if approached by a certificate holder. A larger share of District housing providers (accounting for 71% of the rental stock) would be willing to participate in TAP on behalf of an existing tenant, suggesting that the In-Place Component may be substantially more effective at achieving enrollment than the General Application Program.

In addition to the problem of resistance on the part of D.C. housing providers, the District's housing stock simply contains an insufficient number of units renting at or below the payment standards for both TAP and the federal Section 8 program.

The long-term effectiveness of TAP may depend on the District's ability to induce the production of more moderate-cost rental units -- through the use of TAP and other subsidies -- to serve both TAP recipients and others with low and moderate incomes.

### 3. IMPACTS OF RENT CONTROL

By regulating the rents that housing providers can charge, rent control potentially alters housing market outcomes -- both directly and indirectly. The most obvious and direct effect of rent control is on rents -- with the assumption being that controls will reduce rents for at least some segments of the inventory. As illustrated in Exhibit 16, to the extent that rent control has any significant impact on prevailing rent levels, it may also have other effects, on both the supply and the demand side of the rental housing market.

On the supply side, we have explored the following hypotheses about rent control's possible implications:

If rents are significantly affected by controls, then property values and property appreciation may also be affected.

Rents, values, and expected appreciation are all key components of the profitability of rental housing investment. Thus, if rent controls affect these factors, they will alter the profitability of investment in the District's rental housing sector.

Profitability is a primary determinant of investment levels. Therefore, to the extent that rent control alters the profitability of rental real estate, it may alter the amount of maintenance and capital improvements performed for existing properties, thereby affecting the adequacy of the stock.

Changes in profitability may also alter the volume of units added to the rental housing stock as well as the number of units removed from the stock, thereby affecting the availability of rental units in the District.

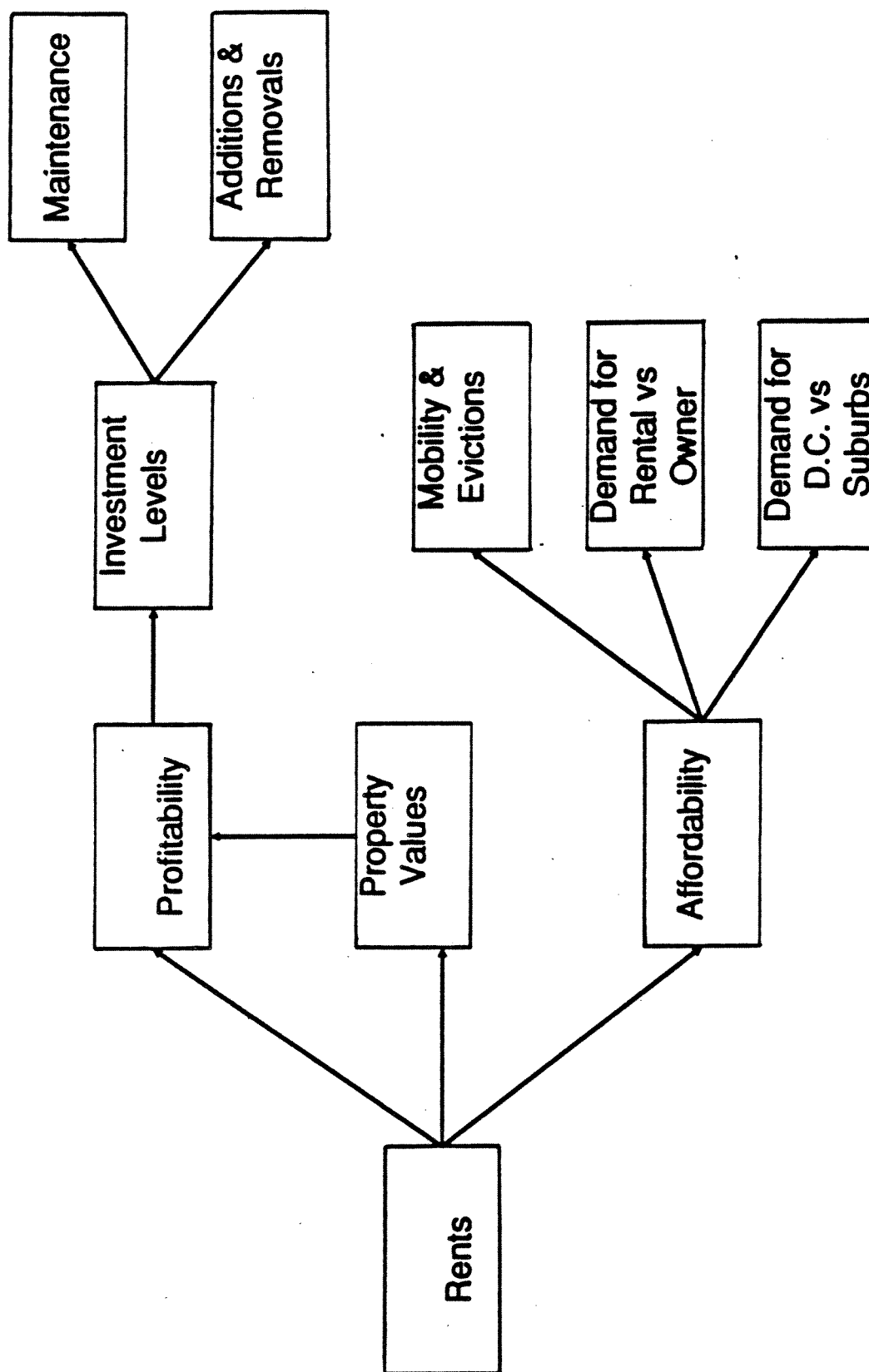
Correspondingly, the study explored the following hypotheses regarding potential demand-side effects of rent control in the District:

Changes in rent levels may make housing more or less affordable for some households, and may, therefore, alter local mobility rates -- including both voluntary and involuntary mobility.

A change in District rents may alter the relative costs of owning versus renting enough to change the tenure choices of some District households.

Similarly, a change in District rent levels may alter the relative costs of rental housing in the District and the surrounding suburbs, enough to change the location choices of some renter households.

# POSSIBLE IMPACTS OF RENT CONTROL ON MARKET DYNAMICS



This chapter presents the results of our analysis of the full range of possible market impacts of the District's existing system of rent control.

### Impacts on Rents and Affordability

Estimating what rent levels would have been in the absence of controls constitutes a critical first step in analyzing the impacts of rent control on the local housing market. Our survey of renter households provides a wealth of information about the characteristics of units on the rental market today, but it obviously cannot tell us what rent levels would have been if rent control had not been implemented. We considered three competing strategies for estimating what D.C. rents would have been in the absence of controls. These three alternatives are briefly outlined here. For More details, see Annex B or Section II of the Technical Supplement.

One approach would be to look to the uncontrolled units in the District's housing stock to determine what market conditions would be in the absence of controls. However, the exempt portion of D.C.'s rental housing stock is small, and differs systematically from the much larger stock of controlled units. Moreover, rent control may affect the rent levels of exempt units as well as those that are directly regulated. Therefore, we rejected the possibility of using the District's exempt stock to reflect unregulated market outcomes.

A second possible methodology would be to apply the relationship that exists today between the characteristics of rental housing units in the suburbs and their rent levels. In other words, we might assume that, in the absence of controls, D.C. units would rent for the same amount as comparable units in the surrounding suburbs. However, the suburban rental stock and renter households are quite different from those of the District of Columbia. This makes it hard to accept an argument that, in the absence of controls, the relationships between unit characteristics and rents in the District would follow the patterns observed in nearby suburban jurisdictions.

Finally, the third approach available is to rely on the relationships between housing characteristics and rent levels that existed in D.C. before the implementation of controls, and to look to other metropolitan areas for estimates of how central city rent levels have changed over the intervening years. This approach, which we consider the best available methodology for estimating rents in the absence of controls, uses 1974 Annual Housing Survey (AHS) data for D.C. to determine the contribution of various housing attributes to total rent. This enables us to estimate what today's units would have rented for before the imposition of rent control. These rent estimates are then adjusted upward to account for the overall inflation in rent levels that prevailed in uncontrolled central cities during the 1970s and early 1980s.

Once we have estimated the relationship that prevailed between housing unit characteristics and rent levels before the imposition of controls, the task still remains of determining how rapidly D.C. rent levels would have increased over the intervening years in the absence of the rent control program. Between 1974 and 1987, rent levels in the District rose by about 7.8% annually. Suburban rents rose somewhat more rapidly -- at about 8.3% annually over the same period. In uncontrolled metropolitan areas of the Northeast and mid-Atlantic regions, central city rents generally rose more rapidly than in D.C. -- and typically a half to one and a half percentage points faster than rents in their surrounding suburbs:

Average Annual Increases in Median Rents  
(mid 1970s through early 1980s)

	<u>Central City</u>	<u>Suburbs</u>
Atlanta	10.2%	9.0%
Baltimore	8.9	8.8
Hartford	9.0	9.3
Philadelphia	9.9	7.7
Pittsburgh	11.5	11.0
Rochester	7.5	7.5
U.S. Average	9.4	8.9
D.C.	7.8	8.3

On the basis of this evidence, we conclude that in the absence of controls, D.C. rent levels would have increased more rapidly than rent levels in the surrounding suburbs -- at an average annual rate of at least 8.5% and no more than 11%. Given the differential between central city and suburban rent inflation rates in other metropolitan areas, our best estimate of the average annual rate of market rent inflation for the 1974 to 1987 years is 9.5%. This estimate not only reflects a "typical" differential between the central city and surrounding suburbs, but it also corresponds to the average rate experienced by the uncontrolled central cities listed above, and to the average for all central cities nationwide.

This level of rent inflation would have produced higher average rent levels and housing expense burdens than those that prevail today -- levels more typical of other central cities in the U.S. Specifically, our estimates suggest that, in the absence of controls, D.C. renters would be paying between \$95 and \$100 more per month in rent (including utilities) than they do today. It is essential to keep in mind that the methodology we have adopted for estimating "market" rents does not purport to provide definitive estimates of what any individual unit would rent for if controls were eliminated today. Instead, our objective is to reveal overall market patterns and trends. Thus, some factors



that may be important ingredients of a particular unit's marketability are omitted from our estimates. Nevertheless, this methodology is effective at explaining broad rent patterns, and for approximating average market rent levels for important segments of the District's rental stock.

Without question, the rent savings generated by controls moderate the problems of housing affordability faced by D.C. renters. As Exhibit 17 shows, at the rent levels estimated for an uncontrolled market, the share of households paying more than 30% of their income for rent would increase from its current level of about 43% to more than 50%. Thus, while affordability problems in the District are severe today, a much larger number of renter households would pay excessive rent burdens in the absence of rent control.

While the rent savings generated by rent control are substantial, they are not evenly distributed among all D.C. renters. In fact, not all households would be paying more in an uncontrolled market than they do today. As Exhibit 18 illustrates, about one quarter of all D.C. renters probably pay rents as high -- and perhaps higher -- than the "market" rents that would prevail in the absence of controls. And, among those who experience rent savings, about one third pay rents that are within \$100 of estimated market rents, another third pay between \$100 and \$200 less they would in the absence of controls, and the remaining third pay rents that more than \$200 below market rent levels.

The households who enjoy the greatest rent savings are those who have remained in their controlled units for several years. The vast majority of households who occupy controlled units and who have remained in their units for six years or more enjoy substantial rent savings, while roughly half of those who are recent movers pay rents as high, or higher, than they would in the absence of controls. Our estimates suggest that, when controlled rental units are vacated, housing providers sometimes raise rents to levels above those that would prevail in the absence of controls, to compensate for the fact that, if the new tenant stays for more than a year or two, rents will be constrained from rising as rapidly as they would in the absence of controls. Thus, the turnover history of controlled units also plays an important role in determining the level of rent savings -- with units that turn over frequently much more likely to charge rents close to market levels than units that have experienced only occasional turnover.

The monetary benefits to tenants are clearly larger on average in controlled units than in units that are exempt from controls. But our estimates indicate that, in the absence of controls, rent levels would also be higher on average in exempt units. In fact, slightly over half of the D.C. renters who live in unsubsidized exempt units appear to pay less than they would in the absence of controls. In other words, the existing system of rent control in the District appears to be holding rents down for exempt units as well as for the units that are directly regulated.

# D.C. RENTAL UNITS

## Rent Burdens w/ Actual & Estimated Rents

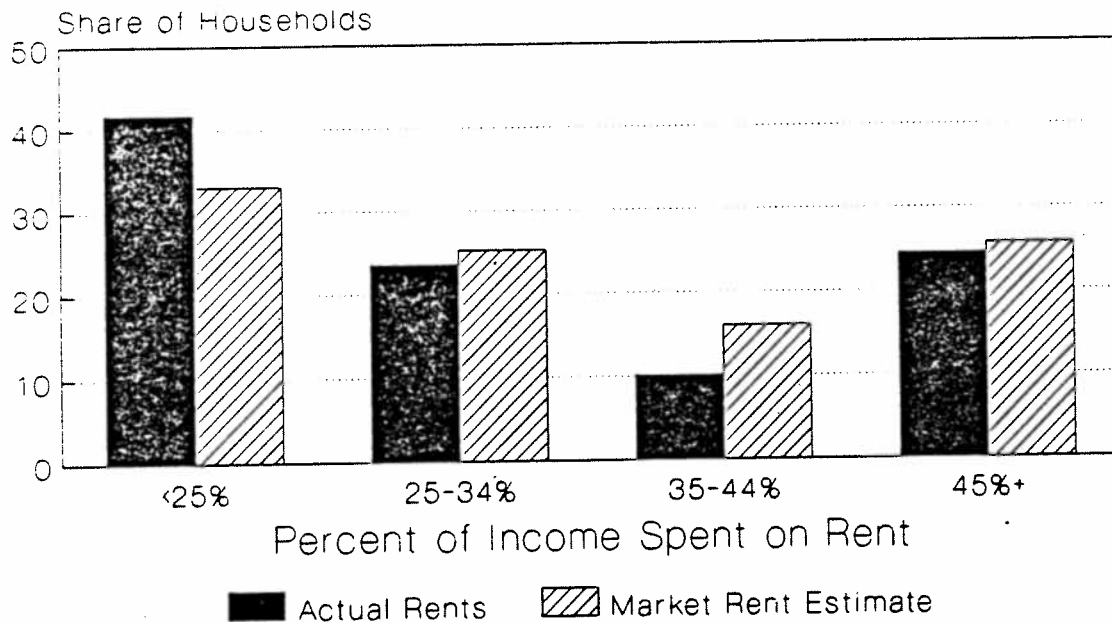
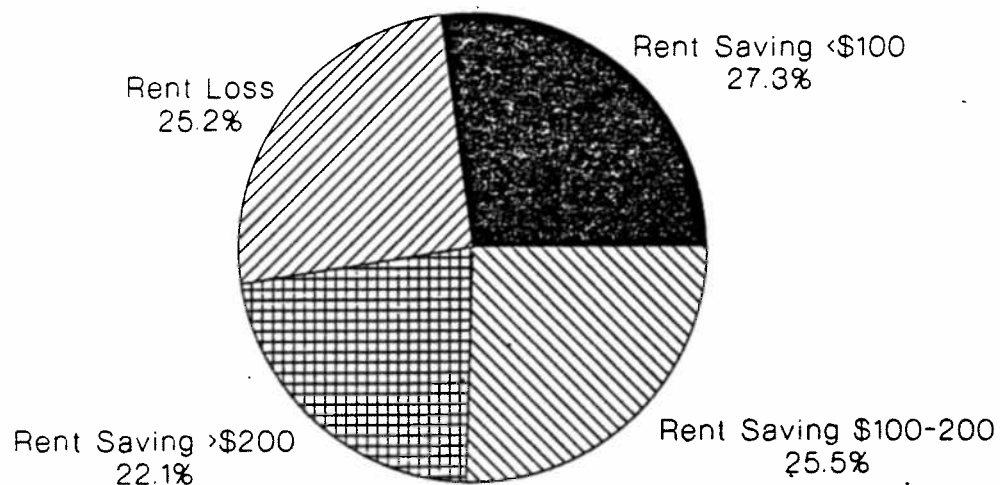


EXHIBIT 18

# D.C. RENTAL UNITS

## Estimated Rent Savings or Losses



Note: Rent Savings and losses represent estimated market rent minus actual rent.

SOURCE: 1987 U.I. Tenant Survey

What types of households benefit from a system of controls that provides the biggest savings to long-term stayers? In general, elderly households and families with children are the most likely to enjoy rent savings from the existing system of controls, while the younger and more mobile singles and adult groups are the most likely to pay rents that are as high or higher than those that would prevail in the absence of controls.

Moreover, poor and moderate income households are more likely to enjoy direct rent savings than are those with higher incomes. Specifically, as shown in Exhibit 19 about 80% of poor households (annual incomes under \$15,000) pay below market rents, compared to 65% of high income renters (annual incomes over \$50,000). This pattern stems from the fact that (as discussed in Chapter 1) the most affluent segments of the District's renter population consist of young singles and groups of unrelated adults, who are more likely to be recent movers and to occupy the newer, more expensive, and larger units that typify the exempt portion of the District's rental stock.

It is important to keep in mind that neither household composition nor income directly determines the level of rent savings under the existing system of rent control in the District of Columbia. An elderly couple or a low income family who moved into their units this year would probably be paying rents as high or higher than market rents. And correspondingly, an affluent group of young adults will begin to enjoy significant rent savings if they remain in a controlled unit for more than a year or two. The rent savings generated by controls are available to households of all types and income levels, but they arise primarily through the continuous occupancy of controlled units.

The tendency for rent levels to be above market levels for recently vacated units means that movers and newly forming households who are poor are especially likely to face unaffordable rent burdens. Because the existing system of controls is designed to generate benefits for those who remain in their units, poor households that are newly forming or mobile may actually have greater difficulty finding affordable housing than they would in an uncontrolled market. In fact, a large share of the poor households who stand at greatest risk of homelessness are recent movers whose rents are as high or higher than those that would prevail in the absence of rent control.<sup>1</sup>

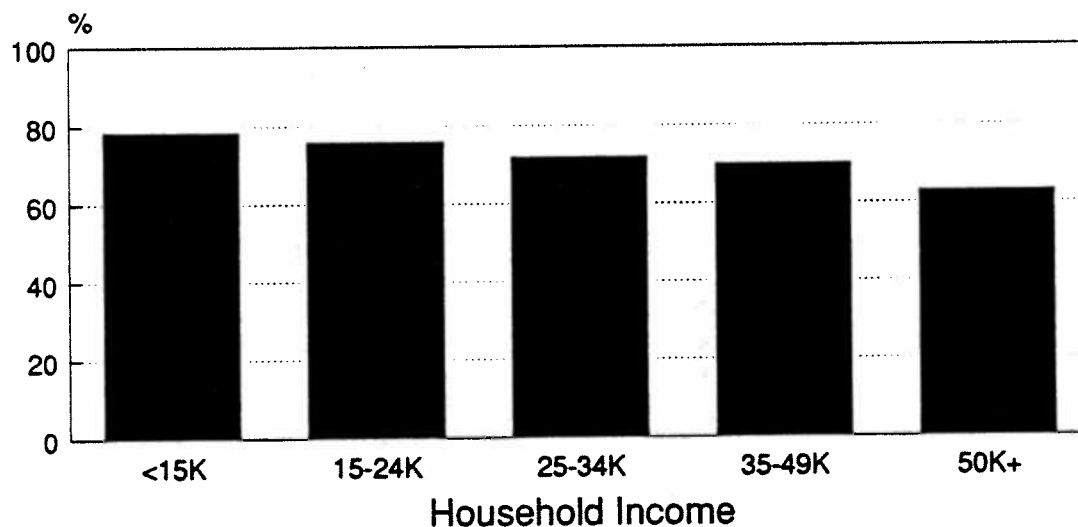
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1. Households who pay more than 75% of their income for rent are defined as "at risk of homelessness." See Section VII of the Technical Supplement for a description of these households and their housing circumstances.

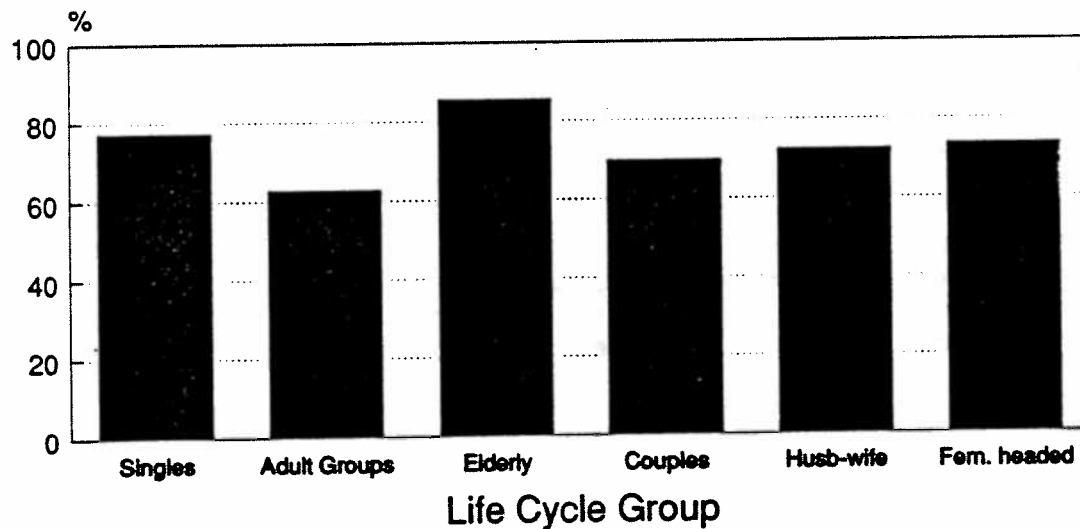
## EXHIBIT 19

# D.C. RENTAL UNITS

Estimated Share of Households  
with Rent Savings



SOURCE: 1987 U.I. Tenant Survey



SOURCE: 1987 U.I. Tenant Survey

## Tenant Perceptions of Rent Control

District renters -- including those living in both controlled and exempt units -- strongly approve of rent control. For virtually all segments of the renter population, sentiment runs at least 3 to 1 in favor of rent control. The only group with a lower level of enthusiasm for the existing system of controls consists of households who think that their rents are just as high or higher than they would be in the absence of controls. But even among these households, two thirds express support for rent control, suggesting that non-monetary benefits -- predictability of rent increases, for example -- as well as direct rent savings play a key role in shaping tenants' perceptions.

Although D.C. renters are enthusiastic about rent control, many do not really know whether or not the units in which they live are controlled. Specifically, almost 40% either do not know or answer incorrectly when asked to identify the control status of their units.<sup>1</sup> Tenants in controlled units are more likely to know their control status than those who live in exempt units, and the share of households with accurate information increases systematically among those who have remained in the same units for several years. But the fact remains that two out of every five D.C. renters are either uninformed or misinformed about their control status.

The primary benefit of rent control, as perceived by residents of controlled units, is that it makes rents more affordable. Roughly 90% of those who live in controlled rental units indicate that rent control has made their apartments more affordable. But tenants also value the sense of security provided by the existing system of controls; about 80% of those who live in controlled units say that rent control provides them with the security to stay in their apartments if they want to.<sup>1</sup> Most of these households (almost 75%) also indicate that rent control increases their incentive to stay in their existing apartments even if they might prefer to move. Thus, D.C. renters recognize that continuous occupancy of a controlled unit is what generates the greatest monetary savings under the existing system of controls, but this impediment to mobility does not appear to outweigh the benefits of controls in the minds of most.

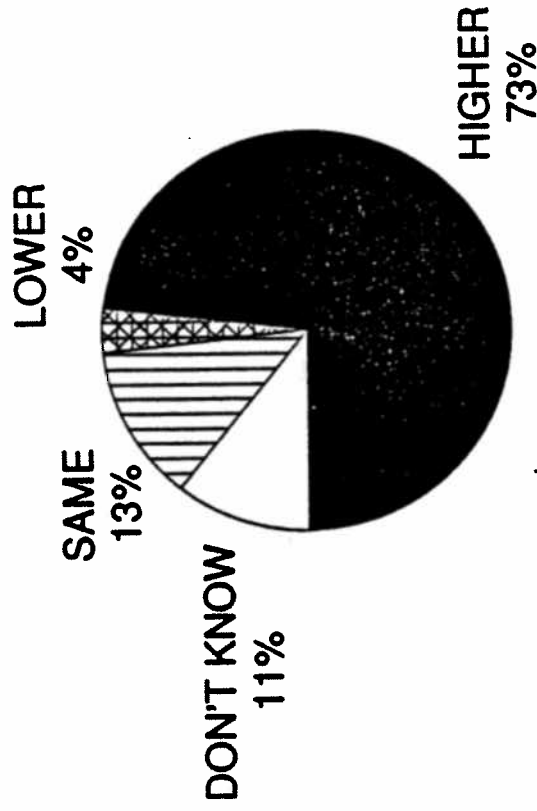
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1. For a subset of the households in our tenant survey, we were able to determine the actual control status from DCRA registration records. See Section II of the Technical Supplement for details. Throughout this report, when controlled and exempt units are compared, only units with verified control status data have been included in the comparisons.

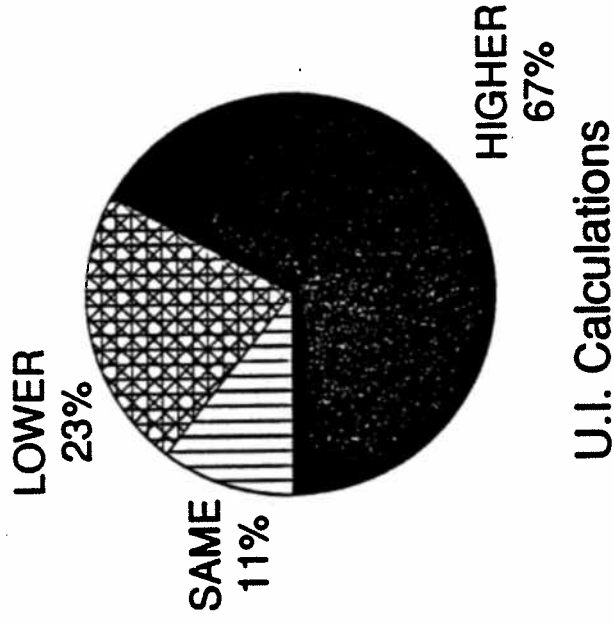
2. Note that many D.C. renters -- as well as housing providers -- do not distinguish the rent stabilization program from eviction protections. Thus, some of the benefits tenants attribute to rent control may actually stem from the District's accompanying system of eviction protections.

# D.C. RENTER PERCEPTIONS

Without Rent Control  
Rent Would Be ...



Tenant Estimates



U.I. Calculations

Most tenants in controlled rental units (80%) believe that building maintenance is as good or better than it would be in the absence of rent controls, and a substantial share (61%) report that the protections offered by rent control make them more willing to insist on building repairs. Low income households were particularly likely to include this as a benefit of the District's rent control program.

While D.C. renters clearly realize that the benefits of the existing system of rent control increase with length of tenure, many appear to overestimate the monetary benefits they obtain. As Exhibit 20 shows, almost three quarters (73%) of D.C. renters believe that they would be paying higher rents in the absence of controls, and only 17% think that market rents would be the same or even lower than their current rents. In contrast, our estimates of market rents for D.C. units imply that about one third of all renters would be paying roughly the same amount, or in some cases less, in the absence of controls. Recent movers are particularly likely to think they are obtaining direct rent savings when our estimates suggest that they are paying as much or more than they would in the absence of controls.

### Household Mobility and Choice

The District's existing system of rent control clearly affects the price of rental housing in the city, as well as the relative costs of moving versus staying. Tenants recognize that rent control conveys substantial rent savings -- in fact, they actually appear to overestimate the magnitude of these savings -- and they understand that the structure of the local rent control program creates direct incentives to stay rather than to move. Given these direct, monetary impacts, rent control might be expected to alter the behavior of D.C. renter households -- discouraging them from moving even when an existing unit does not meet their needs, encouraging them to remain in the District rather than moving to the suburbs, and encouraging them to remain renters rather than becoming homeowners. After examining patterns of housing choice in D.C. and other central cities, we conclude that the District's existing system of rent control may contribute to the very low rate of mobility observed among D.C. renters, but it probably has not had any significant impact on homeownership rates,<sup>1</sup> or on the choice of central city versus suburban locations.

D.C. renters who live in controlled units move less frequently than those who occupy units that are exempt from controls. For example, half of all controlled units have been occupied by the same household for at least six years, compared to only about one

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1. See Section I of the Technical Supplement for more detail on the differences between renters and rental housing in D.C. and the surrounding suburbs.

third of the District's exempt units. Correspondingly, almost half of the exempt units are occupied by recent movers (households who moved in within the last two years), compared to only about one third of controlled units.

Moreover, D.C. renters are less mobile than renters in many other central cities; according to the 1981 AHS, roughly 20% of D.C. renters moved annually compared to 30% of all central city renters in the U.S.<sup>1</sup> However, as of 1981, there were other central cities with equally low mobility rates that did not have rent control -- Baltimore and Philadelphia, for example. And mobility rates among D.C. renters were just as low, both in absolute terms and in comparison to other cities, before the imposition of rent control as they were in 1981, suggesting that, while controls may be a factor in mobility decisions here, they are not the only explanation for the low rate of turnover in the District's rental housing inventory.

Since 1981, however, mobility rates have plummeted; today only about 10% of unsubsidized renters in D.C. report that they moved within the last year. While a decade of experience with rent control may have contributed to the very low rate of household mobility, we suspect that the declining availability of units that are affordable for low and moderate income also discourages households from moving. In other words, the District's rental housing market has become considerably tighter over the course of the 1980s, a trend that explains the heightened level of additions to the stock as well as the depressed rate of household mobility.

While most moves occur at the discretion of the household, 5% of D.C. renters report that they were forced to move within the last three years. In other words, about one of every six mobile renters moved involuntarily. Of these, half were evicted for non-payment of rent, 30% were evicted for other reasons, and 20% report that they were not evicted, but that they moved involuntarily, most often because they could no longer afford to pay their rent. Not surprisingly, the vast majority of forced movers are poor (annual incomes under \$15,000), and these households are now almost twice as likely to be paying unaffordable rent burdens as other D.C. renters. The incidence of forced mobility and eviction for non-payment of rent appear to be about the same in both the controlled and the exempt portions of the stock.

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1. The comparatively low mobility rate observed for D.C. renters applies to all segments of the renter population except for the elderly. For example, in 1981 24% of non-elderly singles and 19% of poor renters in the District were recent movers, compared to 34% and 31%, respectively, for all U.S. cities. Among the elderly, roughly 9% moved annually, in D.C. and in U.S. central cities generally.



### Impacts on Revenues, Value, and Profitability

Since rent control reduces gross rent levels (rents plus utilities) by \$95 to \$100 per month on average, rent revenues to housing providers are obviously also reduced. In the absence of controls, our estimates of prevailing "market" rents for controlled units would yield substantially higher rent revenues - about 33% higher on average.<sup>1</sup> Like our market rent estimates, these revenue estimates do not presume to reflect the unique circumstances of particular rental properties, but rather to approximate the average impact of controls for properties of different types. Properties with frequent turnover already charge rents close to market levels, and therefore would experience a smaller revenue gain in the absence of controls, while properties with many long-term stayers would experience a larger gain on average.

The increased rent revenues that would prevail in the absence of controls would ultimately increase property values as well, so that the impacts of controls on the returns to investment in rental property are more complex than they may at first appear.<sup>2</sup> Exhibit 21 summarizes the estimated impacts of rent control on key financial attributes for average units in different building size categories. After adjusting for changes in equity, interest costs, and property taxes, we estimate that D.C. housing providers would realize annual increases in net income ranging from about \$600 per unit in small properties to about \$1,350 per unit in large controlled properties. At the same time, annual appreciation gains would probably grow by amounts ranging from just over \$100 per unit in large properties to \$800 per unit in the smallest properties.

If these increased revenues were entirely devoted to raising the investment returns to D.C. housing providers, the profitability of the average large rental property would rise by as much as 5

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1. From the perspective of tenants (including those living in both controlled and exempt units), the estimated rents that would prevail in the absence of controls would increase housing expenditures by \$95 to \$100 per month on average. The same market rent estimates yield a 33% increase in "contract" rents for controlled properties on average. Contract rents exclude utilities that are paid directly by tenants.

2. We assumed that the relationship between rent revenues and assessed property values that prevails today would be essentially the same in the absence of controls. Thus, higher revenues translate directly into higher value estimates. We also assumed that loan to value ratios would be roughly the same, so that both equity and debt would increase if values were higher. Finally, our estimates of appreciation benefits in the absence of controls assume no change in appreciation rates, but apply the prevailing rates to the estimated values of properties in the absence of controls. See Annex B for more details.

## EXHIBIT 21

FINANCIAL PERFORMANCE OF CONTROLLED RENTAL  
PROPERTY IN D.C.

Average Annual Per Unit Values — 1985

	<u>Actual</u>	<u>Estimated Market</u>
<u>1-2 unit buildings</u>		
Net Income	-\$ 181	\$ 632
Appreciation	2,444	3,246
After Tax Return	10.4%	11.3%
<u>3-4 unit buildings</u>		
Net Income	\$ 110	\$ 696
Appreciation	1,805	2,400
After Tax Return	18.7%	20.5%
<u>5-9 unit buildings</u>		
Net Income	\$ 601	\$1,433
Appreciation	1,044	1,389
After Tax Return	12.4%	14.2%
<u>10-19 unit buildings</u>		
Net Income	\$ 688	\$1,699
Appreciation	566	752
After Tax Return	11.7%	14.6%
<u>20-49 unit buildings</u>		
Net Income	\$ 578	\$1,764
Appreciation	567	754
After Tax Return	10.3%	13.9%
<u>50-99 unit buildings</u>		
Net Income	\$1,063	\$2,321
Appreciation	754	1,003
After Tax Return	11.8%	14.3%
<u>100-249 unit buildings</u>		
Net Income	\$1,153	\$2,503
Appreciation	349	464
After Tax Return	12.4%	15.8%
<u>250+ unit buildings</u>		
Net Income	\$ 854	\$2,196
Appreciation	- 199	- 264
After Tax Return	10.1%	15.1%

percentage points, while the profitability of smaller properties would rise by only one or two percentage points (see Exhibit 22). But the majority of controlled housing providers in the District indicate that, if their revenues were to rise significantly, either maintenance expenditures would be increased or property improvements would be undertaken:

If your property experienced a significant increase in revenues, this increase would be used to --

increase returns to investors	37.5%
undertake deferred maintenance or capital improvements	66.7%
enhance routine maintenance	23.1%

If the typical housing provider used half of the increase in net operating revenues to either expand maintenance or finance property improvements, then the estimated profitability of the average large rental property would increase by about two percentage points while the profitability of small properties would increase by less than one percentage point on average.

#### Impacts on Maintenance and Housing Quality

There is conflicting evidence regarding the impacts of rent control on the maintenance of rental housing in the District. On the one hand, we find no indication that a decade and a half of local rent control has resulted in the deterioration of D.C. rental housing. Since 1974, the share of units that are physically deficient has actually declined -- from 26% to 20%. Moreover, D.C. units that are exempt from controls exhibit a higher rate of deficiencies than those subject to controls (25% versus 20%), despite the fact that uncontrolled units are typically more expensive.<sup>1</sup> Finally, tenants do not believe that landlords are neglecting housing maintenance as a result of rent control, and, in fact, many indicate that the existing system of controls makes them more confident about asking landlords to correct physical deficiencies in their units.

On the other hand, rent revenues would be 33% higher on average in the absence of controls and, as outlined earlier, these increased revenues would yield sizable annual increases in net operating incomes. According to D.C. housing providers, the increases estimated for average units would be sufficient to

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1. Part of the explanation for this result may be that a large share of exempt units are single-family homes, which are not subject to inspections by HID, except on a complaint basis.

correct deferred maintenance problems for roughly half of the units that are currently in less than adequate physical condition. Moreover, among providers who report that their units are in deteriorated physical condition or that current levels of maintenance expenditures are not sufficient to preserve the quality of their properties, insufficient revenue is the most frequent -- though not the only -- explanation:

For properties in less than adequate condition,  
reasons for not undertaking needed repairs:

rent revenues are not high enough	87.3%
neighborhood conditions	31.4%
cannot obtain financing	7.8%
building is occupied	5.6%

Thus, there are good reasons to conclude that, in the absence of controls, at least a portion of the increased rent revenues would be used for property maintenance and improvements, and that the amounts involved would probably be large enough to have a significant impact on property conditions. If housing providers devoted incremental rent revenues to housing repairs and improved maintenance, the quality of the rental housing stock would be higher in the absence of controls. However, we do not find evidence that the quality of the stock has actually deteriorated under rent control, or that owners of exempt units in the District -- which do generate higher rent revenues -- engage in correspondingly higher levels of maintenance and improvements. And finally, for at least three quarters of the D.C. rental units with the most serious physical deficiencies, the higher revenues estimated in the absence rent control would probably not be sufficient to support the needed improvements.

#### Impacts on the Size of the Rental Inventory

Since rent control significantly reduces rent revenues for the majority of D.C. units -- including exempt as well as controlled units, some providers may be discouraged from adding new or rehabilitated units to the rental inventory, and others may remove units from the available supply. Moreover, even if investment in D.C. rental property is reasonably profitable, some members of the real estate industry argue that the existing climate of vigorous tenant protection -- including rent control, housing code enforcement, eviction protections, and condominium conversion restrictions -- is sufficiently costly and intimidating to discourage investment within District of Columbia.

Housing providers who responded to our survey confirm that they perceive the District's regulatory environment as having major impacts on their operations. Owners of virtually all controlled units in our sample think rent control has a major impact on their revenues, and a majority also view the administrative costs of rent control as a significant factor in their operations:

<u>D.C. regulations perceived to have a major impact on --</u>	<u>percent of controlled units</u>
revenues	90%
administrative costs	84
eviction costs and delays	77
property value	50
unit recovery	30
substantial rehab decisions	24

Moreover, owners of 80% of controlled rental units in D.C. indicate that they do not expect to invest in D.C. rental housing in the future. The reasons most commonly cited are that rents are not high enough to make rental real estate an attractive investment (45.5%), and that the D.C. regulatory environment makes investment in other jurisdictions more attractive (50.2%).<sup>1</sup> It is interesting to note, however, that among small individual owners, the most common reason given for avoiding future investment was not the local regulatory environment, but the expectation that the new federal tax law will make rental real estate a less attractive investment than it has been in the past.

Do recent trends in the size of the District's rental stock support the argument that rent control reduces housing supply? The precipitous decline in the size of the District's rental housing stock that occurred during the 1970s and early 1980s is often cited as evidence that rent control chokes off supply. Rent control and the other tenant protections that accompany it may have played an important role in the decisions of some potential investors. In particular, owners of single family homes, who could easily sell their units on the burgeoning homeownership market, may have been discouraged by the imposition of rent control from keeping these houses in the rental inventory. However, evidence of comparable stock losses in other, uncontrolled central cities over the same period strongly suggests that the local regulatory environment should not be blamed for current shortage of low and moderate cost rental housing in the District.

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1. Note that respondents could select more than one primary reason why future investment was not planned. See Section IV of the Technical Supplement for more details.

The 1970s was a period in which many central cities -- controlled as well as uncontrolled -- experienced declining rental housing inventories:

Average annual percent change in  
the rental inventory, 1970-1983:

Atlanta	-0.4%
Baltimore	-0.9
Hartford	-1.4
Philadelphia	-0.4
Pittsburgh	-1.4
Rochester	-0.8
Washington, D.C.	-1.4

As discussed earlier, this decline was triggered not by local regulatory conditions, but by nationwide economic trends that made homeownership overwhelmingly attractive, by the expansion of suburban housing opportunities, and by the declining purchasing power of the households who continued to rely on the rental market. Units were withdrawn from central city rental inventories, and the level of new (unsubsidized) rental production was low because fewer middle and high income households were choosing to be central city renters, and because the remaining renters could not afford to make housing investment sufficiently profitable.

Even during the 1970s, when the rental stock was shrinking, new rental units were being built in the District. In fact, D.C. experienced a higher rate of new rental housing construction than many uncontrolled cities:

Average annual rate of new  
rental construction (1973-1980)

Atlanta	2.0%
Baltimore	1.8
Hartford	0.0
Philadelphia	0.7
Pittsburgh	0.0
Rochester	2.0
Washington, D.C.	1.5

Between 1970 and 1981, while the District's rental housing inventory experienced a net loss of more than 1,000 units annually on average, roughly 400 new rental units were built each year. While about three quarters of these new units received

federal subsidy assistance, other, uncontrolled central cities in the Northeast and mid-Atlantic region experienced much lower rates of new rental construction during the 1970s.

During the first half of the 1980s, the decline in demand for rental housing in the District slowed considerably. Specifically, between 1974 and 1981, the number of renter households in the District fell by almost 3,000 per year on average. Between 1981 and 1985, this annual figure fell to below 1,000. In other words, demand for rental housing in the District began to stabilize during the first half of the 1980s, in part because rising interest rates, lower inflation, and reductions in marginal tax rates have all contributed to make homeownership much less affordable relative to rental housing. In fact, the rate of homeownership in the nation as a whole, which increased from 64.2% to 65.6% in the 1970s, declined to 64.0% by 1987, with affluent singles and childless couples as well as young families electing to continue renting rather than entering the homeownership market.

However, while the loss of renter households slowed considerably during the 1980s, the supply of rental units continued its decline at a somewhat faster pace. The result has been a dramatic drop in the rental vacancy rate from 6.2% in 1981 to 2.5% in 1985. More recently, the District's rental stock has started to grow in size, increasing by about 800 units annually since 1985. We suspect that in part, this turn-around reflects the conversion and sale restrictions enacted in 1981, which sharply limit the circumstances in which rental properties can be converted to owner-occupancy or otherwise removed from the inventory. But in addition, the resurgence of demand for rental housing -- reflected in falling vacancy rates -- appears to have attracted new investment in the District's rental housing market. In other words, the recent increase in the size of the rental inventory represents a lagged market response to renewed levels of effective demand.

It is possible that this response might have occurred more quickly in an unregulated rental market, but the responsiveness of District investors to the changing demands for rental housing -- and the similarity of recent trends in uncontrolled central city markets -- suggests that rent control is not a determining factor in investment decision-making, although it certainly may be a consideration. Recent investors in new and substantially rehabilitated rental units report that they do not see rent control as a deterrent, and only about one quarter of those interviewed advocated the elimination of rent control. More cited the District's system of eviction protections -- which is seen to reflect a strong "pro-tenant" bias in the District's regulatory environment -- as a serious cause for concern. In addition, the cost and availability of land and/or structures for new construction and substantial rehabilitation, as well as the availability of long-term financing are cited by the providers of

new D.C. rental units as constraints on their ability to build or substantially renovate housing in the District.<sup>1</sup>

While additions to the rental housing stock do not appear to be very sensitive to the presence of rent control, losses from the rental stock have a much greater impact on the availability of housing for low and moderate income renters, and -- over the last decade and a half -- rental inventory losses have been much more volatile than inventory additions. During the 1970s, an average of 1,000 units were actually removed from the District's housing stock annually, and the vast majority of these units rented for less than \$350 (in 1987 dollars). Again, this phenomenon was by no means unique to the District; many uncontrolled central cities also lost rental units during the 1970s:

Annual rate of rental  
unit removals (1973-1980)

Atlanta	2.7%
Baltimore	3.0
Hartford	4.4
Philadelphia	3.2
Pittsburgh	4.0
Rochester	5.3

Washington, D.C.    4.5

These losses reflect the overall decline in demand for central city rental housing relative to homeownership and relative to suburban housing opportunities.

Another important explanation for the removal of units from the rental inventory is the declining purchasing power of low income renter households. Increasingly, the amounts that low and moderate income renters can afford to pay for housing fall short of what it costs to provide decent rental accommodations. Thus, as rental units age, they are more likely to drop out of the inventory altogether than to filter down to form a stock of older but decent and affordable rental housing.

Rent control has not caused this problem, but it may play a role in the removal of units from the District's rental housing stock. Our inventory of additions to and losses from the District's rental housing inventory indicates that roughly 160 rental units were either temporarily or permanently removed from the housing stock between May 1985 and April 1987. Almost all of these units

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1. Because the number of providers who have added units to the stock in the last two years and who could be reached for telephone interviews was small (17 interviews), we cannot provide statistical breakdowns of their responses. For more details on these interviews, see Section III of the Technical Supplement.



were controlled, and owners who were interviewed consistently listed rent control among the negative factors that caused them to discontinue the use of their properties. Their decisions were motivated by the lack of economic viability of their properties, and they suggested that, if the District government wants to minimize losses from the rental stock, it should make it easier to evict non-paying and destructive tenants, and it should approve legitimate substantial rehab and hardship petitions more readily.

In principle, the substantial rehab and hardship petition provisions of the District's existing system of rent control should address the problems of properties that are financially and physically distressed. In fact, while properties of this kind may be technically eligible for a hardship rent increase, their owners may be prevented from applying for such an adjustment for two important reasons. First, many low rent buildings would not pass a housing inspection, and their owners may not be able to finance repairs, given current rent levels. And second, even if an increase was approved, the tenants would not be able to afford higher rents. As a result, these properties are likely to deteriorate further, and ultimately may be removed from the rental inventory -- directly reducing the availability of housing for low and moderate income renters in the District.

While rent control plays a role in this scenario, it acts as a complicating factor, rather than as a primary cause of the dilemma. If rent control alone constrained the rents that the providers of older run-down properties could charge, and if market rents for these units were sufficiently high to induce housing providers to improve them in the absence of controls, then we would certainly observe a much higher usage of the hardship petition process, despite the costs. Given the relatively low usage of substantial rehab, capital improvements, and hardship petition opportunities, it is hard to argue that rent control, per se, is the binding constraint on the economic viability of these properties.

### Summary of Key Findings

This chapter focuses on the impacts of rent control on the affordability, adequacy, and availability of rental housing D.C. by testing a set of specific hypotheses about the impacts of rent control on both the demand side and the supply side of the District's rental housing market.

### **Rents and Affordability**

In the absence of controls, we estimate that D.C. renters would be paying between \$95 and \$100 more per month in rent (including utilities) than they do today.

At these "market" rent levels, the share of households paying more than 30% of their income for rent would increase from its current level of about 43% to more than 50%.

Not all households would be paying more in an uncontrolled market; about one quarter of all D.C. renters probably pay rents as high -- and perhaps higher -- than the "market" rents that would prevail in the absence of controls.

Average rent levels for exempt units, as well as for controlled units, would be higher in an unregulated market.

The households who enjoy the greatest rent savings are those who have remained in their controlled units for several years.

Elderly households and families with children are the most likely to enjoy rent savings from the existing system of controls, while the younger and more mobile singles and adult groups are the most likely to pay rents that are as high or higher than those that would prevail in the absence of controls.

Moreover, poor and moderate income households are more likely to enjoy direct rent savings than are those with higher incomes.

Because the existing system of controls is designed to generate benefits for those who remain in their units, poor households that are newly forming or mobile may actually have greater difficulty finding affordable housing than they would in an uncontrolled market.

### **Tenant Perceptions**

District renters strongly approve of rent control, with sentiment running at least 3 to 1 in favor of rent control.

The primary benefit of rent control, as perceived by residents of controlled units, is that it makes rents more affordable. But tenants also value the sense of security provided by the existing system of controls.

D.C. renters recognize that continuous occupancy of a controlled unit is what generates the greatest monetary savings under the existing system of controls, but this impediment to mobility does not appear to outweigh the benefits of controls in the minds of most.

Most tenants in controlled rental units (80%) believe that building maintenance is as good or better than it would be in the absence of rent controls, and a substantial share (61%) report that the protections offered by rent control make them more willing to insist on building repairs.

While D.C. renters also clearly realize that the benefits of the existing system of rent control increase with length of tenure, many appear to overestimate the monetary benefits they obtain.

### Household Mobility and Choice

The District's existing system of rent control may contribute to the very low rate of mobility observed among D.C. renters, but it probably has not had any significant impact on homeownership rates or on the choice of central city versus suburban locations.

D.C. renters who live in controlled units move less frequently than those who occupy units that are exempt from controls. And, D.C. renters are less mobile than renters in many other central cities.

Since 1981, mobility rates appear to have plummeted. This confirms that the District's rental housing market has become considerably tighter over the course of the 1980s, a trend that explains the heightened level of additions to the stock as well as the depressed rate of household mobility.

### Rent Revenues and Profitability

In the absence of rent control, rent revenues to controlled units would be substantially higher -- about 33% higher on average. D.C. housing providers would realize annual increases in net income ranging from about \$600 per unit in small properties to about \$1,350 per unit in large controlled properties.

At the same time, annual appreciation gains would probably grow by amounts ranging from just over \$100 per unit in large properties to \$800 per unit in the smallest properties.

If these increased revenues were entirely devoted to raising the investment returns to D.C. housing providers, the profitability of the average large rental property would rise by as much as 5 percentage points, while the profitability of smaller properties would rise by only one or two percentage points.

Alternatively, if the typical housing provider used half of the increase in net operating revenues to either expand maintenance or finance property improvements, then the estimated profitability of the average large rental property would increase by about two percentage points while the profitability of small properties would increase by less than one percentage point on average.

## Housing Quality

There is conflicting evidence regarding the impacts of rent control on the maintenance of rental housing in the District.

On the one hand, we find no indication that a decade and a half of local rent control has resulted in the deterioration of D.C. rental housing.

On the other hand, rent revenues would be 33% higher on average in the absence of controls and, according to D.C. housing providers, the increases estimated for average units would be sufficient to correct deferred maintenance problems or to achieve the needed level of maintenance expenditures for roughly half of the units that are currently in less than adequate physical condition.

## Housing Supply

The decline in the District's rental housing inventory that occurred during the 1970s was also experienced by many other, uncontrolled central cities in the U.S.

This decline was primarily triggered not by local regulatory conditions, but by nationwide economic trends that made homeownership overwhelmingly attractive, and by the expansion of suburban opportunities.

During the first half of the 1980s, the decline in demand for rental housing in the District slowed considerably. However, the supply of rental units continued its decline at a somewhat faster pace, resulting in a dramatic drop in the rental vacancy rate from 6.2% in 1981 to 2.5% in 1985.

More recently, the District's rental stock has started to grow in size, increasing by about 800 units annually since 1985. This increase in the size of the rental inventory represents a lagged market response to renewed levels of effective demand.

It is possible that such a supply response might have occurred more quickly in an unregulated rental market, but the responsiveness of District investors to the changing demands for rental housing -- and the similarity of recent trends in uncontrolled central city markets -- suggests that rent control is not a determining factor in investment decision-making.

Moreover, recent investors in new and substantially rehabilitated rental units report that they do not see rent control as a deterrent, and only about one quarter of those interviewed advocated the elimination of rent control.

The cost and availability of land and/or structures for new construction and substantial rehabilitation, as well as the availability of long-term financing are cited by the providers of new D.C. rental units as more significant constraints on their ability to build or substantially renovate housing in the District.

In principle, the substantial rehab and hardship petition provisions of the District's existing system of rent control should address the problems of properties that are at risk of removal from the rental housing stock.

However, owners may be prevented from applying for adjustments either because they cannot finance the needed repairs, given current rent levels, or because, even if an increase was approved, the tenants would not be able to afford higher rents. As a result, these properties are likely to deteriorate further, and ultimately may be removed from the rental inventory -- directly reducing the availability of housing for low and moderate income renters in the District.

If rent control alone constrained the rents that the providers of older run-down properties could charge, and if market rents for these units were sufficiently high to induce housing providers to improve them in the absence of controls, then we would certainly observe a much higher usage of the hardship petition process, despite the costs.



#### 4. POSSIBILITIES FOR THE FUTURE

The existing program of rent control in the District of Columbia has succeeded in moderating housing costs for most renter households without curtailing provider profits so severely that the availability of units is reduced. However, the existing system does not eliminate the excessive housing cost burdens confronting the majority of the city's poorest renters, and the District faces a persistent shortage of low-cost units that are affordable for low and moderate income households.

What can we expect for the future? And what approaches are available for more effectively addressing the problem of housing affordability for low and moderate income renters in the District? This chapter begins by examining trends that can be expected to shape both the demand and the supply of D.C. rental housing over the next decade. Next, we explore several variations on the existing rent control program, which were specified in the Council mandate for this study. In addition to these alternatives, we outline two key areas for improvement in the operation of the existing rent control program. Finally, the chapter concludes by sketching the outlines of a more comprehensive approach to the housing affordability problems facing low and moderate income renters in D.C.

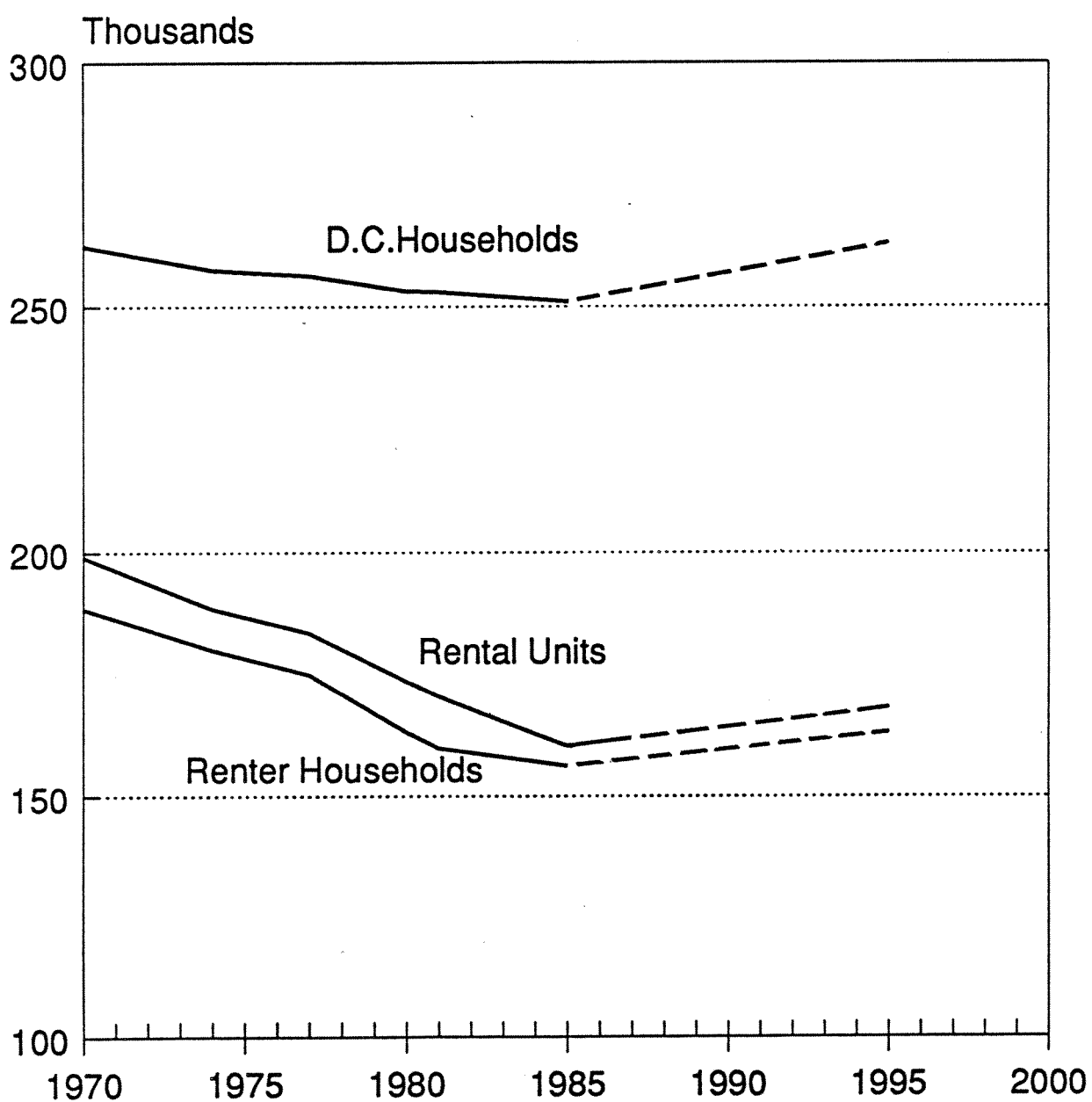
##### Changes in Renter Households and the Rental Housing Inventory

Over the past decade and a half, the District's rental housing inventory has responded to changes in the aggregate level of demand for rental units. This does not mean that the housing needs of all renters have been fully satisfied, but it does mean that the total stock of housing units has essentially matched the total population of renter households. Two dimensions of housing demand have been particularly important determinants of trends in the District's rental housing stock: 1) the number of households seeking rental housing within the District boundaries; and 2) the life-cycle status and income levels of various segments of this total renter population. The importance of these two factors will persist during the next decade, with the first controlling the overall size of the rental stock, and the second determining the affordability of rental housing and the viability of units that serve households with low and moderate incomes.

The primary determinant of the number of units added to -- or lost from -- the District's rental housing stock over the next decade is the number of D.C. households who choose to be renters. As illustrated in Exhibit 22, the District's total population of households declined during the 1970s and early 1980s, although the rate of decline slowed considerably after 1980. The most recent forecast by the District's Office of Planning sets the 1996 household population at 263,200, an increase of about 12,000 households over the total of 251,100 recorded in the 1985 AHS.

## EXHIBIT 22

# TRENDS IN D.C. RENTAL HOUSING SUPPLY AND DEMAND 1970-1995





The share of these households who rent declined during the 1970s -- from 72% in 1970 to 63% in 1981 -- in response to strong economic pressures for homeownership throughout the U.S. Since 1980, the national homeownership rate has actually declined slightly, and the share of D.C. households who own their homes has remained essentially unchanged since 1981. National forecasts predict renewed growth in the rate of owner-occupancy by the end of this century -- from 64% in 1985 to 68% in the year 2000.<sup>1</sup> This forecast is based on the assumption that, as the remaining members of the baby boom generation reach full maturity and form permanent households, most will shift from renter to owner-occupant status. However, the rate at which these households achieve homeownership will be extremely sensitive to changes in the economic factors that make homeownership more or less affordable, particularly house value inflation rates, interest rates, and the federal tax treatment of mortgage interest and property taxes. We have estimated that the share of D.C. households who rent will either remain at its current level or increase by a few percentage points over the course of the next decade (see Exhibit 22).

During the 1970s, the size of the District's rental housing stock declined in direct proportion to the number of renter households, maintaining a vacancy rate of about 6% through 1981. However, after 1981, the rental stock continued its earlier rate of decline, while the renter population began to stabilize. As a result, vacancy rates declined to less than 3% by 1985, creating market pressures for new construction and substantial renovations, which have been reflected in a fairly high rate of additions to the rental stock since 1985. We predict that the total size of the rental housing stock will continue to grow in response to the anticipated increases in the number of renter households. Specifically, we can expect the District's stock of rental units to grow by as many as 700 units per year on average over the next decade if the Office of Planning population forecasts are borne out.<sup>2</sup> However, if the District's population continues to decline in size, or if national economic conditions generate renewed homeownership pressures, the size of the District's rental inventory could actually contract by about 100 units per year on average, and still produce vacancy rates of around 6%.

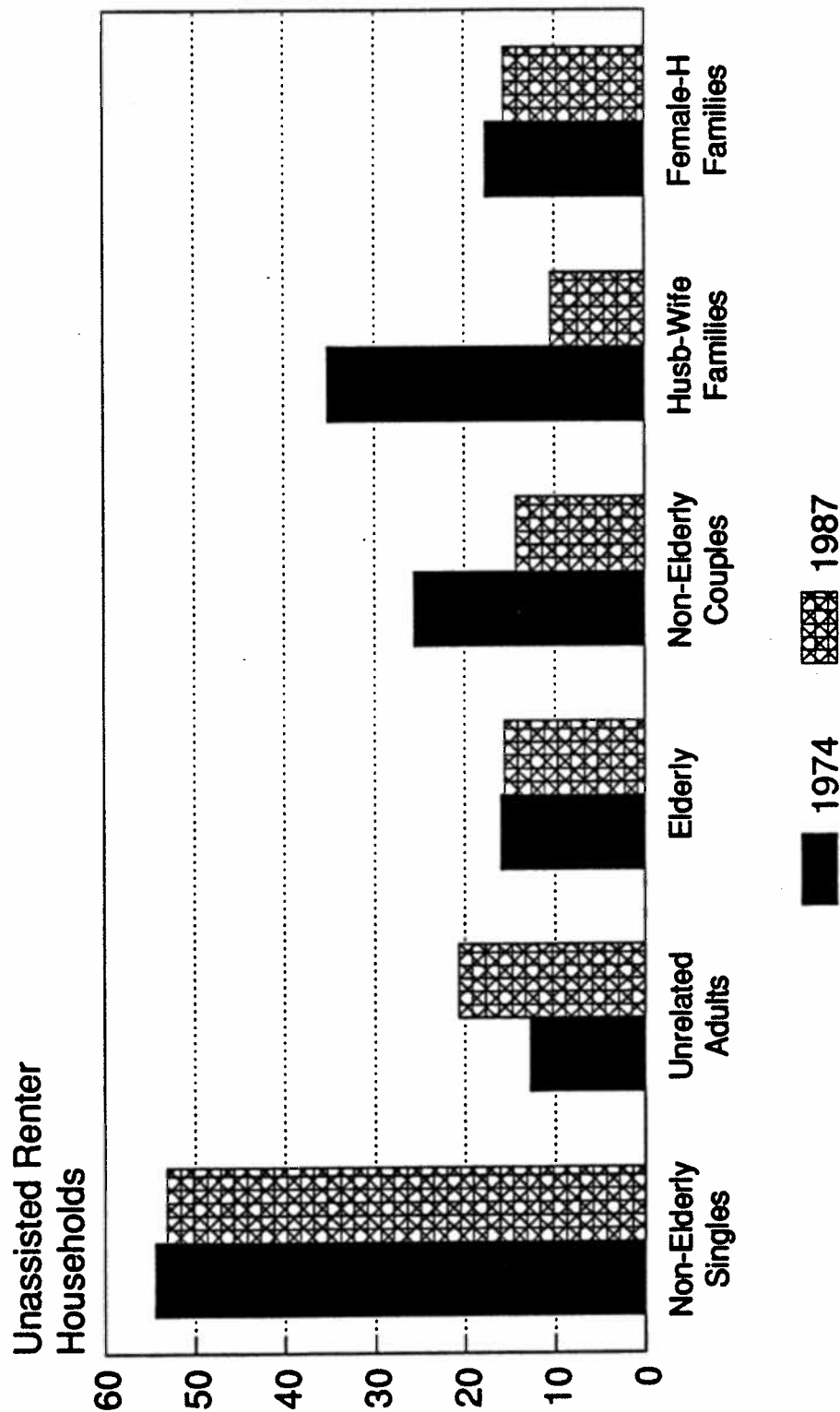
But growth in the total size of the rental inventory will not necessarily meet the needs of all segments of the renter

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1. See J.Pitkin and G.Masnick, "Projections of Housing Consumption in the U.S., 1980 to 2000, by a Cohort Method," Massachusetts Institute of Technology and Harvard University, Joint Center for Housing Studies, 1986.

2. A net increase of 200 units per year would result in a vacancy rate of about 3%, given our estimate of the number of renter households in 1996. A net increase of 600 units per year would yield a 6% vacancy rate.

# CHANGING COMPOSITION OF THE D.C. RENTER POPULATION 1974, 1987 (thousands)



population. What types of households will make up the District's renter population in 1996, and how much rent will they be able to afford to pay? As Exhibit 23 illustrates, the composition of the D.C. renter population shifted dramatically between 1974 and 1987, with an increasing share of non-elderly singles and adult groups, and a decreasing share of husband-wife families. National forecasts of household composition suggest that this shift will be cemented over the course of the next decade, but that the composition of the renter population will not change as dramatically between now and the end of this century as it did during the 1970s and early 1980s.

More specifically, national demographic forecasts to the year 2000 highlight three key trends in the profile of U.S. households:

Single individuals are the fastest growing household type. By the end of the century, their numbers will have increased almost 75%.

Two age groups contribute to the rapid growth in the number of single individuals -- elderly people and middle-aged people. These are the two fastest growing age groups among household heads, and the share who live alone will more than double by the end of the century.

The number of single-parent families with children will grow by almost half. The majority of these families will be headed by women between the ages of 30 and 55.

These trends suggest that four groups of D.C. renter households can be expected to show the fastest rate of growth in the decade ahead: non-elderly singles adult groups, elderly people, and female-headed families. However, the non-elderly singles and adult groups of the 1990s may be considerably older than those of the 1980s, composed of more middle-aged and "previously married" individuals and fewer young, "never married" members of the baby boom generation.

How much will these households be able to spend for housing? As discussed in Chapter 1, real incomes declined for all but two groups of D.C. renter households between 1974 and 1987. After adjusting for inflation, median incomes among non-elderly singles, the elderly, childless couples, and husband-wife families declined significantly. Among groups of unrelated adults -- the fastest growing segment of the D.C. renter population -- median real income increased by almost 75%. And among female-headed families with children the median real income increased only slightly.

To some extent, the decline in real renter incomes that occurred in the 1970s and early 1980s was attributable to the corresponding decline in the share of households choosing to rent. Most middle and upper income households who could afford to become homeowners did so, leaving behind a population of

renters that was both smaller and poorer. It seems unlikely that real renter incomes will continue to decline as dramatically in the 1990s. Affluent young singles, who currently rent either on their own or in groups, may shift to homeownership as they form permanent households, to be replaced by growing numbers of middle-aged singles. If so, the average real income level among this group of D.C. renters may fall modestly. But otherwise, we expect renter incomes to remain about constant in real terms over the next decade.

This means that the problem of housing affordability probably will not worsen substantially in the years ahead. But the core of permanent renters in the D.C. population will remain poor. There is no reason to expect that their income levels will begin to overtake prevailing housing costs during the 1990s. Therefore, even if developers expand the total size of the rental housing stock, in response to intensified demand pressures, low and moderate income renters in the District will continue to face a persistent shortage of affordable housing. Moreover, even with an adequate flow of additions to the rental housing stock, affordability problems will worsen if low-cost units are removed from rental use at an accelerated rate. Therefore, attention must focus on the number of units removed from rental housing use every year as well as on the number of units added to the stock.

Between 1985 and 1987, about 500 units were removed from rental use annually, while 1,300 were added, resulting in a net increase of approximately 800 rental units per year. Strategies which minimize the number of units lost from the District's rental stock over the next decade can be just as effective for ensuring the availability of rental housing as strategies which maximize the number of units added to the stock. Moreover, since both new construction and substantial renovation are costly and require large-scale financing, the units produced will either charge high rents or require large subsidies to be affordable for low and moderate income households. In contrast, the preservation of existing units that already serve low and moderate income renters can generally be achieved at much lower costs, and more immediately benefits households with housing problems.

Between 1985 and 1987, about half of the units added to the rental inventory were condominiums that are currently being rented rather than sold for owner-occupancy. If homeownership pressures rebound during the next decade, these condominiums will certainly be among the first units lost from the District's rental stock. This probably would have little impact on the availability of rental units for the remaining D.C. households who cannot afford homeownership, since newly built or renovated condominium units are unaffordable for low and moderate income households, regardless of whether they are offered for sale or for rent. Efforts to keep units in the rental inventory should focus instead on buildings that currently serve low and moderate income households, and that are at risk of removal due to declining revenues or deteriorating physical conditions.

We do not expect rent control to play a determinative role in housing supply over the course of the next decade unless operating costs (including interest and property taxes) begin to rise more rapidly than the CPI. During the 1980s, the CPI has proven to be a reasonable indicator of changes in the costs of operating rental real estate. However, during the late 1970s, increases in the CPI may have fallen short of actual increases in operating and utility costs. If the generally applicable rent increase allowed under current law does not keep pace with increases in the costs of operating rental housing, then the quality of the rental stock is likely to deteriorate and we can expect an accelerated rate of removals from the existing inventory. Other critical supply-side factors that may affect the size of the District's rental inventory include: 1) the impact of the 1986 Tax Act on the profitability of investment in rental housing; and 2) the availability and cost of financing for rental housing production and for acquisition and repairs to existing properties.

During the 1990s, the federal tax reforms enacted in 1986 will play an important role in housing markets throughout the U.S. Some forecasts have suggested that the restrictions on tax deductions for real estate investment may result in rent increases as high as 30%, or -- in markets where rents are controlled -- in correspondingly large reductions in the profitability of rental real estate. Our estimates of the after tax returns to investment in the District's controlled rental units indicate that small properties may indeed yield substantially lower returns as a result of the 1986 Act:

#### Estimated After-Tax Return on Equity for Controlled Units

	<u>before 1986</u>	<u>after 1986</u>
1-2 unit buildings	10.4%	6.4%
3-4 unit buildings	18.5	14.5
5-9 unit buildings	12.4	10.5
10-19 unit buildings	11.7	10.5
20-49 unit buildings	10.3	9.1
50-99 unit buildings	11.8	11.0
100+ unit buildings	12.4	11.7

Since tax benefits do not play as important a role in the overall profitability of larger properties, these properties are likely to be less affected by the 1986 Tax Reform Act. If small housing providers in the District are adversely affected by the 1986 Tax Reform Act, then a significant share of these providers may remove their properties from rental use or transfer them to larger housing providers, and small individual investors will be less likely to participate in the production and renovation of additional rental housing units.

The production of new and substantially renovated rental housing units, as well as the preservation of the existing inventory depends critically on the availability and cost of financing. The scope of this study did not include an empirical analysis of the availability of finance for rental housing in the District, but numerous participants in the local market have reported that loans for controlled rental properties are scarce, and that long-term financing, in particular, is difficult to secure. Some local lenders reportedly think that the District's rent control program prevents property owners from raising rents in response to increased expenses, and that, as a result, controlled properties are more likely to default on their obligations. However, D.C. financial institutions that do make loans to controlled properties indicate that lenders who take the time to understand the rent control program can profitably do business with the owners of controlled properties.

### Alternative Rent Control Provisions

Several alternatives to the District's existing system of rent control have been suggested over the course of the 1980s -- some of which are designed to phase out controls or to reduce their coverage, while others are designed to increase the benefits of rent control for low and moderate income households. As directed by the City Council, we have assessed the impacts of four specific alternatives. These assessments focus on the share of the rental inventory that would be subject to controls, the effects on housing affordability, the likely implications for housing supply, and issues of administrative feasibility.

Vacancy decontrol represents a plan for the gradual phase-out of rent control. Following a voluntary move or legal eviction, any unit in substantial compliance with the local housing code would become exempt from controls. The current pool of approximately 101,100 controlled units would be reduced only very gradually under a system of vacancy decontrols. In 1987, only about 10% of controlled units turned over, according to reports of both tenants and housing providers. And close to half of all units have been continuously occupied for more than six years.<sup>1</sup>

It is reasonable to assume that turnover rates would remain close to today's levels, despite the fact that, by moving, a household would essentially be opting out of rent control. Since turnover rates are already very low, and the existing system of controls in the District already discourages mobility, it is unlikely that the mobility decisions of renter households would be substantially affected by vacancy decontrol. Thus, in the first year of vacancy decontrol, the impact would be small -- reducing the number of controlled units by about 10%, or 10,000 to 11,000 units. By the end of six years, approximately half of today's

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1. Turnover rates do not differ systematically by the size of the rental unit.

controlled rental units would be exempt -- with roughly 50,000 units still remaining within the existing system of rent stabilization.

The impacts of vacancy decontrol on housing affordability and supply can be directly inferred from our analysis of the effects of rent control on market outcomes (see Chapter 3). In the short-term, the effects would be modest. Households who remain in their units would continue to be protected by controls, and movers would in all likelihood pay approximately the same rents that they do today, since newly occupied units currently rent for as much -- and sometimes more -- under the existing system of controls as they would in an uncontrolled market. In the longer term, as decontrolled units begin to dominate the market, prevailing rent levels would correspond to the estimated market rents discussed in Chapter 3, which are about 25% higher on average than today's controlled rents. All households living in decontrolled units would be paying higher rents than they are now, except recent movers, who would be paying about the same -- or slightly less -- than they do today. The share of households with unaffordable rent levels would increase substantially, particularly among elderly households and single-parent families.

As an expanding share of all units were decontrolled, provider revenues would gradually rise to roughly 33% above their current levels. Providers who already experience a high degree of turnover would see relatively small revenue gains, while owners with more long-term tenants would gradually obtain substantially larger revenues. If as much as half of the increased revenue was allocated to property maintenance and improvements, then the quality of the existing rental stock would gradually be enhanced, and it is possible that fewer units would drop out of the stock as a result of deferred maintenance and deterioration. However, at least some of the increased rent revenues would almost certainly be absorbed by property owners, increasing the profitability of investment in D.C. rental housing. Despite the increased profitability of rental housing investment, there is no evidence to suggest that the number of units available for rent would be any greater if vacancy decontrol was implemented.

Although vacancy decontrol would gradually reduce the number of units subject to controls, it would complicate the District's rent control program tremendously, from the perspective of housing providers, tenants, and program administrators. Specifically, almost all buildings that are currently controlled would continue to have some controlled units for at least six years, with the number of controlled units in any property likely to change every year. Therefore, housing providers and DCRA would be faced with the task of keeping track of which units in a given building remain subject to controls and which units are exempt. Tenants -- who are currently quite poorly informed about the control status of their units -- would certainly have even greater difficulty understanding their rights and circumstances, since different rent levels and different rules for rent adjustments would apply within the same rental building.

Luxury decontrol represents an effort to target the benefits of rent control more closely to low and moderate income households, compared to the existing system which generates benefits even for the most affluent renters. Of the over 200 U.S. jurisdictions with rent control ordinances, we identified four communities -- all in California -- that have implemented luxury decontrol.<sup>1</sup> In each case, the luxury decontrol provision was implemented along with the original rent control ordinance, and "luxury units" are consistently defined by their rent levels:

Luxury Exemption Rent Levels  
(in cities that exempt luxury units)

	<u>Effic-</u> <u>iciencies</u>	<u>1 Bedrm</u>	<u>2 Bedrm</u>	<u>3 Bedrm</u>	<u>4+ Bedrm</u>	<u>Effective</u> <u>Date</u>
Los Angeles	\$302	\$420	\$588	\$756	\$823	1978
Thousand Oaks	400	500	600	750	900	1980
Palm Springs	450	450	450	450	450	1979
Beverly Hills	600	600	600	600	600	1978

Units originally qualifying for the luxury exemption remain exempt, and no new units receive exemptions, regardless of rent increases.

If luxury decontrol is considered in the District, exemptions should be based on rent levels, as in other cities. Defining a package of "luxury" amenities -- security system, air conditioning, or swimming pool, for example -- is simply too likely to include buildings that serve low and moderate income households as well as buildings that primarily serve the city's most affluent renters.<sup>2</sup> Nevertheless, implementing a rent-based luxury decontrol provision in the District today, after roughly a decade and a half of controls, would be complicated somewhat by the fact that rent levels depend on turnover history, and by the fact that the current occupants of high rent units would probably object strenuously to the prospect of "losing" the benefits of rent control.

These objections can be addressed by using turnover rents to define "luxury" units. As units were vacated by their current

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1. Note that all of the communities with rent control are limited to five states -- California, Massachusetts, New York, New Jersey, and Maryland -- and the District of Columbia. We surveyed all five states, as well as 15 individual jurisdictions to determine the nature of state enabling legislation and local ordinances.

2. Because amenities cannot realistically be used to define luxury units, we do not present data on the amenities provided by D.C. rental properties.



residents, they could become exempt from controls if the maximum applicable rent ceiling upon turnover exceeded a cut-off for luxury units. Using either the top 10% or the top 5% of the current rent distribution to define "luxury" units, the following cut-offs would be established for 1987:

#### 1987 "Luxury" Rent Levels

	<u>Effic- iency</u>	<u>2-3 rooms</u>	<u>4-5 rooms</u>	<u>6+ rooms</u>
top 10%	\$550	\$625	\$800	\$1,300
top 5%	\$600	\$700	\$900	\$1,500

Of course, these cut-offs would have to be adjusted annually for inflation; otherwise the rents of non-"luxury" units would gradually creep up over time, until eventually all of the rental units in the stock qualified for the "luxury" exemption.

The effects of luxury decontrol on the District's rental housing market would be minimal. Since a disproportionate share of the highest rent units are exempt from controls, the 1987 rent levels listed above would apply to only 6% or 2% of the controlled stock, respectively -- approximately 600 or 200 units. The occupants of these units are almost exclusively affluent, white non-elderly singles or groups of unrelated adults who moved into their units within the last two years. Therefore, these households are not receiving significant monetary benefits from the existing system of controls, and would not be substantially affected by the removal of controls.

Since only a small number of existing units would be affected by luxury decontrol, the impact on housing supply in the District of Columbia would be purely symbolic. The majority of high rent units are either already exempt from controls or can be expected to change occupancy frequently, so that housing providers would probably experience only minimal revenue gains. And luxury decontrol would have no effect on the rent revenues for properties that are in deteriorated condition or those at risk of being removed from the stock. However, luxury decontrol might moderate perceptions that the District has a hostile regulatory environment, or that rent control provides benefits to affluent tenants at the expense of housing providers.

Despite the minimal impact of luxury decontrol on housing affordability and supply, it would complicate the administration of the rent control program. Like vacancy decontrol, luxury decontrol would exempt individual units within buildings that otherwise remain subject to rent control. In addition, DCRA would have to maintain an up-to-date schedule of luxury rent definitions, adjusted for inflation, and apply these definitions to the rent ceilings of individual units as providers applied for the luxury exemption for recently vacated, high rent units.

An expanded small-owner exemption would decontrol units owned by individuals whose total D.C. holdings amount to less than ten rental units. Currently, individual owners of fewer than five D.C. rental units qualify for the small-owner exemption. Only 16% of the controlled units in the District today -- about 16,000 units -- would qualify for this exemption, since the majority of units in the District's controlled stock are owned by large scale individual investors, partnerships, and corporations.

Unlike larger D.C. rental property owners, most of the small individual housing providers in the District do not consider real estate to be their primary source of income, and the most frequent reason they give for investing in rental housing is tax benefits. The controlled rental units owned by small individual investors are obviously in small properties, their rents are lower than average, and they are typically in reasonable physical condition.<sup>1</sup> Small individual investors are unlikely to obtain substantial cash flow from their holdings, but -- consistent with their investment motives -- currently realize after-tax rates of return that are above average.

Virtually all of the small owners that we surveyed (96%) indicated that they do not plan to invest further in D.C. rental housing, primarily because of the tax reforms enacted by the federal government in 1986. In fact, as discussed earlier in this chapter, our estimates of after-tax return on equity suggest that the 1986 Tax Reform Act may indeed reduce the returns that small owners receive by as much as 30%. Larger D.C. housing providers -- who do not rely as heavily on tax benefits to make their investments profitable -- will probably be less affected. If the small-owner exemption were expanded, these providers would raise rents substantially -- possibly by as much as 30% over the next several years. However, if these small rental properties remain subject to controls, the impacts of the 1986 Tax Reform Act may reduce profits sufficiently to result in the removal of units from the rental stock.

Another possible argument for expanding the small-owner exemption is that small, non-professional investors may be unduly burdened by the administrative requirements of rent control. Indeed, the District's small housing providers report more difficulty understanding the existing system of rent control than do larger investors in D.C. rental housing; only 42% of the small providers rated their understanding of the law as excellent or good, compared to 78% of all other owners. Since most small housing providers are not real estate professionals, and more than half manage their own properties, these individuals are substantially less familiar with the District's rent control program, and may have greater difficulty taking advantage of the opportunities

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1. All of the units owned by small providers in our sample of controlled properties received "A" ratings from the Housing Inspection Division.

available to them under the law. However, as discussed in Chapter 2, small and large properties are equally represented among petitions for hardship and voluntary rent increases, suggesting that small providers may be capable of taking advantage of the existing system when the need arises.

Incorporating household affordability as a factor in determining rent adjustments would represent an attempt to more fully address the District's housing affordability problems through the rent control program. As discussed in Chapter 1, 42% of renter households in the District currently pay more than 30% of their income for housing, and for one in ten District renters, housing expenditures consume more than three quarters of monthly income. The majority of households with excessive rent burdens -- and all of those whose high rents place them at risk of homelessness -- are poor (incomes under \$15,000). And although housing affordability problems would certainly be more severe in the absence of rent control, the share of renters with excessive rent burdens has risen dramatically since 1974 (from 27% to 42%).

We considered three alternative approaches for incorporating household affordability as a factor in determining rent adjustments. The first approach would incorporate the actual income of a controlled unit's current occupant into the rent adjustment calculation. For example, if a household currently pays more than 30% of income for rent, the housing provider might be limited to a smaller rent increase than the adjustment of general applicability -- or to no increase at all. Similarly, if a household pays close to 30% of income for rent, the housing provider might be limited to a rent increase that keeps the tenant's housing expense burden below the 30% level.

A rent adjustment process of this kind would be a bad idea for the District, despite its good intentions. First, the administrative burden of calculating and approving annual rent increases would increase dramatically. Under the current system, nine out of ten units take advantage of the increase of general applicability with only 8% petitioning for adjustments that require administrative approval. Thus the costs of rent control administration would increase dramatically, and the system of controls would be far less predictable and reliable than it is today.

A second serious disadvantage of an affordability-based rent adjustment process is that rent revenues for those providers who serve low and moderate income households would be substantially diminished. We know, for example, that the average level of subsidy under TAP is more than \$300 per month, and, in effect, the rent adjustment process outlined above would require housing providers to deliver much the same level of assistance as TAP to all low and moderate income renters in the District. For providers who serve low income tenants, rent revenues would not rise as rapidly as their operating costs, and D.C. would almost certainly begin to see the effects of deferred maintenance and the removal of units from the rental inventory.

Finally, housing providers would have strong incentives to evict existing tenants with low incomes, and to discriminate against prospective tenants whose incomes are low, thereby reducing the ability of the District's poorest households to obtain decent, affordable rental housing. In sum, such a system would disrupt the delicate balance that has been achieved in the District between the objective of reducing rent burdens and the need to keep rental housing sufficiently profitable to attract and retain investment.

A more limited strategy for incorporating renter incomes into the determination of rent adjustments would apply only to those rent increases that currently require administrative approval -- increases for substantial rehabilitation, capital improvements, changes in the level of services, and financial hardship. Since these adjustments already require administrative review and approval, the burden of incorporating housing affordability as a factor would not be great. And since these special adjustments typically produce above-average increases in rent levels, they are the most likely to create affordability problems for low and moderate income tenants.

Nevertheless, limiting rent adjustments on the basis of tenant incomes is an extremely risky policy. An important reason why the District's existing system of rent control has had so few adverse supply effects is that it provides several mechanisms for providers to improve housing quality and to maintain adequate levels of profitability. Limiting these mechanisms on the basis of tenant incomes may well result in the deterioration of some segments of the stock -- particularly those segments that serve low and moderate income households -- and in the removal of more units from the rental inventory. In addition, provisions that make it disadvantageous to serve low income tenants carry the danger of increasing the incidence of evictions and discrimination.

A final option for incorporating tenant incomes into the rent adjustment process would apply more broadly to all controlled units. Specifically, the formula for calculating the increase of general applicability could be modified to reflect increases in renter income levels as well as -- or instead of -- increases in operating costs. This approach would avoid many of the potential hazards involved in the two strategies outlined above, but it would still run the risk of generating adverse supply effects. Specifically, if tenant incomes continue to increase more slowly than operating costs (as they certainly have over the last decade and a half), provider revenues will not keep up with operating expenditures. While the existing system of controls appears to have moderated investor profits, such a system would gradually erode the profitability of investing in rental real estate in the District of Columbia, ultimately resulting in deferred maintenance and reduced supply.

### Fine Tuning the Existing Rent Control Program

Whether or not major modifications in the existing rent control program are implemented, the operation of the program could be substantially improved in two key respects. First, DCRA should develop a management information system for monitoring the District's rental housing stock. And second, the hardship, substantial rehab, and capital improvements petition processes should be streamlined to operate more efficiently from the perspective of tenants as well as housing providers. Both of these administrative enhancements would advance the objectives of rent control in the District. Together, they offer the potential to increase the coverage and consistency of rent control, ensure that the existing stock of rental units is not permitted to deteriorate, and offer housing providers a greater sense of control regarding their real estate investment decisions.

A comprehensive management information system is critical to more effective administration and enforcement of the existing rent control program. For example, by maintaining a systematic data base for the stock of rental housing units, the District could more effectively enforce the coverage of rent control program. Our analysis of the financial and ownership characteristics of rent controlled units in the District was based on data obtained from DCRA registration files. In reviewing these files, we found that a large share of D.C. rental properties are not registered. Similarly, our inventory of losses from the District's housing stock identified many properties that were registered with DCRA at the same time that eviction notices were filed. Thus, perhaps as much as one quarter of all rental units in the District are not registered with the Department of Consumer and Regulatory Affairs. If the existing system of rent control in the District of Columbia is to be fairly and effectively implemented, then these unregistered properties should be brought into the regulatory process.

An up-to-date information system would also enable DCRA to monitor trends in the costs of operating rental property in the District, and to ensure that the increase of general applicability keeps pace with provider costs. During the 1980s, the CPI-based adjustment process appears to have compensated providers adequately for increases in operating costs for most types of rental properties, and this is one of the central reasons why we have concluded that the existing system of controls has not had significant adverse effects on the availability and adequacy of rental housing. However, if operating costs (including interest and property taxes) begin to rise more rapidly than the CPI, the profitability of investment in rental housing will begin to be eroded, and the city can expect to see more deferred maintenance, deterioration, and ultimately, removals from the stock of rental housing.

Finally, an effective management information system would enable DCRA to forge a more effective enforcement linkage between the housing inspections process and the rent adjustment process.

Currently, we estimate that 10% to 15% of controlled units in the District experience annual rent increases even though they are not in substantial compliance with the local housing code. DCRA's Housing Inspections Division is currently in the process of improving its procedures for inspections and code enforcement, to increase coverage and to speed up the abatement process. At the same time, information links should be established between the housing inspection process and the rent regulation process, so that owners of properties with serious code violations are prohibited from implementing the increase of general applicability until they bring their buildings into substantial compliance.

In addition to better monitoring and enforcement, we recommend that DCRA streamline the hardship and capital improvements petition processes, so that they work more effectively from the perspectives of both housing providers and tenants. While moderating rent levels is rent controls primary goal, the District's existing program effectively balances this goal against the need to ensure providers a reasonable rate of return, and to encourage investment in property improvements. Both property owners and lenders are discouraged from investing in property improvements when delays and uncertainty cloud their revenue projections. Therefore, hardship, substantial rehab, and capital improvement rent adjustments should be reviewed and approved promptly whenever providers supply adequate documentation. This is not to suggest that providers should not be required to document their revenues, expenses, and planned improvements, or that tenants should not have an opportunity to challenge proposed increases. Instead, we recommend that the standards of documentation for all types of rent adjustment petitions should be rigorous and clearly specified. Then, for providers who supply adequate documentation, the review process should be prompt and predictable.

#### Expanding the Availability of Affordable Rental Housing

Rent control can moderate the rate at which rents increase, but -- no matter how effectively it is administered -- it cannot realistically be expected to eliminate the affordability problems confronting low and moderate income households. The poorest households in the renter population have income levels that are simply too low to make break-even rents affordable. Ensuring decent and affordable rental housing for all of the District's residents requires more direct measures -- to supplement the rents low and moderate income tenants can afford to pay, to preserve existing low-rent properties, and to produce additional, low and moderate cost rental units.

Clearly, the District government does not have either the resources or the capacity to single-handedly solve the problems of housing affordability and adequacy for all of its residents. Responsibility for achieving this goal should be shared by the federal government, and by the governments of other jurisdictions

in the Washington metropolitan area. In order to improve the housing circumstances of its low and moderate income residents, the D.C. government should assume a position of leadership in advocating expanded federal housing assistance efforts as well as collaborative efforts by the central city and suburban jurisdictions in the metropolitan area. In addition, the District itself possesses an impressive arsenal of programs for making rental housing more affordable, which it could be deploying in a more systematic and effective manner.

The remainder of this chapter provides an estimate of the overall magnitude of the need for housing assistance in the District, and then briefly outlines key elements of a strategy for meeting this need. As discussed in Chapter 2, two of every five unassisted renter households in D.C. have low or moderate incomes and live in housing that is either unaffordable, physically deficient, or overcrowded. In other words, 55,000 low and moderate income renters in D.C. need help to obtain decent housing that they can afford.

An overall strategy for meeting the needs of these households should include three key elements: 1) direct assistance, 2) preservation of the low-cost stock, and 3) production of additional, affordable units. The relative contribution of the District, the federal government, and neighboring jurisdictions in the metropolitan area varies with each of these three elements, each of which is now discussed more fully in turn.

**Direct Assistance.** Making rental housing affordable for low income households requires direct rent subsidy assistance to D.C. renters. As discussed in Chapter 2, 18% of all D.C. renters (28,000 households) receive rent subsidies through the public housing program, federally subsidized private housing projects, the federal Certificate and Voucher programs, and the District's TAP. Two major avenues are available to the District for expanding the number of low and moderate income households who receive assistance.

First, the condition and management of the District's public housing inventory should be improved so that the maximum number of households can be adequately sheltered in these units. This research effort did not include an assessment of the public housing program, so we are in no position to evaluate administrative and property management procedures there. However, summary data provided by the Department of Public and Assisted Housing (DPAH) clearly show that the public housing program in the District is not living up to its potential. Specifically, 2,567 of the 11,954 public housing units in the District are currently vacant -- a vacancy rate of 21%. Of these vacant units, 192 are uninhabitable and scheduled for demolition and 1,418 are scheduled for modernization. Still, however, 957 habitable units that are not scheduled for modernization stand vacant, while the waiting list for public housing units stands at 11,587 households. Clearly, the District can and should be doing

a better job of making public housing units available to needy households. If the public housing program completed its modernization program and achieved full occupancy of its inventory, about 2,300 households could be accommodated in public housing units.

In addition, as discussed in Chapter 2, the Tenant Assistance Program continues to be very slow in issuing the assistance that it has available. Currently, 1,095 households participate in TAP, while at current funding levels, a total of 3,400 to 3,500 households could be served. TAP's effectiveness can be dramatically improved by increasing the rate at which certificates are issued, and by helping recipients find housing units in which they can receive benefits.

Even if both TAP and the public housing program were working at full capacity, at least 48,000 low and moderate households would still live in deficient, overcrowded, or unaffordable rental units. Clearly, the District does not have the resources to provide assistance to all of these households. The annual cost of serving all eligible renters through the TAP program would exceed \$200 million, given current rent levels and payment standards.<sup>1</sup> However, if direct rent subsidies were offered on an entitlement basis to all low and moderate income renters whose housing is either inadequate or unaffordable, not all households would participate. Some would prefer not to move from their existing apartments, and others would find program benefits too small to justify the inconvenience of participation. Evidence from federal experiments with entitlement housing assistance programs suggests that perhaps 40% to 45% of all eligible households would actually receive benefits. If this reciprocity rate applied in the District, the annual cost of an entitlement rent subsidy program would come to between \$80 and \$90 million.

Even if the District could expand its TAP expenditures substantially, additional subsidy resources are clearly needed from the federal government. During the 1980s, federal housing assistance programs have operated at extremely low levels -- extending assistance to fewer than 100,000 additional households per year across the nation as a whole, compared to the late 1970s, when more than 300,000 incremental households received federal assistance annually. The housing problems of low income renters in the District -- and in other cities throughout the

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1. In the absence of rent control, the number of eligible households would be about 9,000 higher, increasing the annual subsidy cost of an entitlement program by as much as \$35 million.



U.S. -- cannot be adequately addressed until the federal government resumes a more active role.

Neighboring jurisdictions in the metropolitan area can also play a role in expanding the availability of direct rent subsidy assistance. While rents in the Washington suburbs are higher than those of the central city, rental units are generally larger, so that households who receive rent subsidies might be better able to find suitable units in the central city than in the suburbs. The federal Section 8 housing voucher and certificate programs have recently become "portable," which means that a household who receives federal assistance from an agency in one jurisdiction can use that assistance to pay for housing in any other jurisdiction in the metropolitan area. The District should take advantage of this feature of the federal Section 8 program, which currently assists 1,200 D.C. renters. Section 8 recipients should be informed of their right to seek units in the suburbs, housing search assistance should be provided to acquaint recipients with suburban housing opportunities, and D.C. should work to establish a metro-wide data base of affordable rental housing opportunities, possibly through the Metropolitan Council of Governments.

**Preservation.** The second key element in an overall strategy for expanding the availability of decent and affordable rental housing in the District should be the preservation of the existing stock. In particular, priority should be given to properties that currently serve low and moderate income households, particularly those that are physically and financially distressed. By intervening to help these projects address their deferred maintenance problems and regain sound financial footing, the District can reduce the number of low cost rental units that drop out of the housing inventory, thereby contributing to the availability of affordable housing. In some cases, rent increases will be necessary to enable these properties to survive. While these increases may be painful for current residents, if they are moderate and if they are accompanied by significant improvements in building conditions, they will probably be tolerable for most tenants. Those who clearly cannot afford the increased rents could be directly assisted through TAP or federal rent subsidy assistance programs.

The District has several well designed tools on hand for preserving and improving the existing stock of rental housing. The hardship, substantial rehab, and capital improvements petition processes allow owners of existing properties to obtain rent increases in cases of financial distress or to finance major capital improvements. As discussed earlier, these processes

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1. For an extensive review of federal housing policy efforts, and the challenges of the next several decades, see R.Struyk, M.Turner, and M.Ueno, Future U.S. Housing Policy: Meeting the Demographic Challenge, D.C.: The Urban Institute Press, 1988.

should be streamlined so that they are more understandable and accessible for both providers and tenants. The District's Multifamily Housing Rehab Program makes use of funds from a number of federal programs as well as D.C. appropriations to provide both interim and permanent financing for building renovations in multifamily rental properties. Similarly, the Single-Family Housing Rehab Program and the Single Family Investor-Owner Up To Code Rehabilitation Program provide comparable types of assistance for small residential properties, including rented houses and small rental buildings. And finally, the Distressed Properties Program provides for negotiated packages of tax abatement and financial incentives for occupied rental properties that are in severe financial distress and at risk of being removed from the rental housing inventory.

These tools should be deployed more strategically to preserve the largest possible number of low rent properties in the District. Data and processing linkages should be established between the Housing Inspections Division -- which can identify physically distressed properties, the Rental Accommodations and Conversion Division -- which reviews petitions for hardship and capital improvements rent increases, the Department of Housing and Community Development -- which administers the financing and forgiveness programs outlined above, and the Department of Public and Assisted Housing -- which administers TAP. Given limited subsidy resources, effective linkages between these agencies are critical, since they would enable the City to target the properties that need help most and to structure packages of assistance that will make a difference -- both to the survival of the targetted properties and to the well-being of low and moderate income tenants.

The District's Apartment Improvement Program provides a mechanism for promoting such linkages, for playing the necessary coordinating role, and for involving private sector investors and lenders in the preservation process. The Apartment Improvement Program functions through a 16-member Committee, which is composed of representatives from financial institutions, property owners, tenants, community organizers, and city officials. For distressed properties that participate in the Apartment Improvement Program, this Committee helps form a partnership of the building owners, lenders, and tenants who then negotiate a strategy for working out the building's problems. Negotiated solutions may include refinancing, moderate rent increases, equity contributions, tax or utility forgiveness or deferrals, city property improvement loans or grants, and city financed improvements to the neighborhood. This approach to the problems of distressed rental properties in the District should be strengthened and extended so that every property that is physically and financially at risk becomes involved in a systematic preservation plan.

**Production.** While preservation is the most cost-effective way of contributing to the availability of affordable rental housing, the stock of low and moderate cost housing also needs to be

supplemented through subsidized new construction and substantial rehabilitation. During the 1970s, the federal government played an active role in subsidizing low cost housing production, but these programs have been virtually eliminated during the 1980s. In the absence of federal production programs, the District -- like many other jurisdictions across the country -- has developed local mechanisms for promoting rental housing production.

The Land Acquisition for Housing Development Opportunities (LAHDO) Program encourages the production of new rental housing as well as the rehabilitation of vacant properties, by directly acquiring property proposed by a developer and leasing the land while selling any existing structures on the property at cost. In return, the developer must set aside at least 20% of the units in the property for low income occupancy. The federal Housing Development Grant Program (HoDAG) is sometimes combined with LAHDO, but also used independently to finance new construction and substantial rehabilitation of rental housing. Again, developers must set aside at least 20% of the units in the property for low income households. Finally, the Designated Units Component of the Tenant Assistance Program (TAP) is designed to encourage the production and rehabilitation of rental housing in the District. Under this program, developers build or rehabilitate properties on the assurance that a specified number of TAP certificates are, in effect, tied to units in these properties.

Without renewed involvement from the federal government, the District's capacity to finance low-cost housing production is clearly limited. Linkage between zoning variances for downtown office and commercial projects and the construction of low and moderate cost housing are currently being explored.<sup>1</sup> While efforts of this nature are clearly worth pursuing, the District's limited resources should be targetted toward minimizing the number of rental units lost from the stock every year rather than increasing the number of units that are added.

### Summary of Findings

This chapter explores possibilities for the future, including forecasts of the total demand for rental housing in the District during the 1990s, the capacity of the private market to respond to demand forces, alternatives to the existing system of rent control, and elements of a more comprehensive approach to the housing needs of low and moderate income renters in the District.

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1. See W.D. Keating, "Linking Downtown Development to Broader Community Goals: An Analysis of Linkage Policy in Three Cities," Journal of the American Planning Association, volume 52: 133-141 (spring 1986).

## Renter Households and the Rental Housing Inventory

We expect the District's stock of rental units to grow by as many as 700 units per year on average over the next decade if the Office of Planning's population forecasts are borne out.

But if the District's population continues to decline in size, or if national economic conditions generate renewed homeownership pressures, the size of the District's rental inventory could actually contract by about 100 units per year on average, and still produce vacancy rates of around 6%.

Even if developers expand the total size of the rental housing stock, in response to intensified demand pressures, low and moderate income renters in the District will continue to face a persistent shortage of affordable housing.

We do not expect rent control to play a determinative role in housing supply over the course of the next decade unless operating costs (including interest and property taxes) begin to rise more rapidly than the CPI.

Small properties may yield substantially lower returns during the 1990s as a result of the 1986 Tax Reform Act. But, since tax benefits do not play as important a role in the overall profitability of larger properties, these properties are likely to be less affected by the 1986 Tax Reform Act.

## Vacancy Decontrol

Vacancy decontrol represents a plan for the gradual phase-out of rent control.

The current pool of approximately 101,100 controlled units would be reduced only very gradually under a system of vacancy decontrols. After six years, as much as half of the controlled rental stock would still be subject to controls.

The immediate, short-term effects of vacancy decontrol would be minimal, but as decontrolled units began to dominate the market, prevailing rent levels increase by about 25%.

The share of households with unaffordable rent levels would increase substantially, particularly among elderly households and single-parent families.

As an expanding share of all units were decontrolled, provider revenues would gradually rise to roughly 33% above their current levels.

If as much as half of the increased revenue was allocated to property maintenance and improvements, then the quality of the existing rental stock would gradually be enhanced.

However, at least some of the increased rent revenues would almost certainly be absorbed by property owners, increasing the profitability of investment in D.C. rental housing.

Despite the increased profitability of rental housing investment, there is no evidence to suggest that the number of units available for rent would be any greater if vacancy decontrol was implemented.

Vacancy decontrol would complicate the District's rent control program tremendously, from the perspective of housing providers, tenants, and program administrators.

### **Luxury Decontrol**

Luxury decontrol represents an effort to target the benefits of rent control more closely to low and moderate income households.

If luxury decontrol is considered in the District, exemptions should be based on rent levels, as in other cities.

Using either the top 10% or the top 5% of the current rent distribution to define "luxury" units, would decontrol fewer than 1,000 rental units.

The occupants of these units are almost exclusively affluent, white non-elderly singles and groups of unrelated adults who moved into their units within the last two years.

These households are not receiving significant monetary benefits from the existing system of controls, and would not be substantially affected by the removal of controls.

### **Expanded Small-Owner Exemption**

An expanded small-owner exemption would decontrol units owned by individuals whose total D.C. holdings amount to less than ten rental units.

About 16% of the controlled units in the District today -- about 16,000 units -- would qualify for this exemption.

These units currently charge below-average rent levels, but are in better than average physical condition.

Decontrolling units owned by small housing providers would result in increased rent levels and increased profits.

Small housing providers may need an increase in rent revenues, since they are likely to experience a significant reduction in after-tax investment returns as a result of the Tax Reform Act of 1986.

Another possible argument for expanding the small-owner exemption is that small, non-professional investors may be unduly burdened by the administrative costs of rent control.

### **Incorporating Household Affordability**

We considered three alternative mechanisms for incorporating household affordability as a factor in rent adjustment determinations:

- 1) The most stringent mechanism would limit annual rent adjustments to prevent housing expenditures from exceeding 30% of a household's income.
- 2) A more moderate approach would be to impose such a limit only on hardship, capital improvements, and substantial rehab rent adjustments.
- 3) Finally, the factor used for automatic rent adjustments -- currently the CPI -- could be modified to reflect trends in renter income levels.

All three of these alternatives would disrupt the delicate balance between the goal of moderating rent levels and the need to allow housing providers sufficient profit that they will maintain the District's supply of rental housing.

Incorporating household affordability as a limit on rent adjustments would create incentives for housing providers to discriminate against low and moderate income households, prevent rents from keeping pace with operating costs, and ultimately make it more difficult for low and moderate income households in the District to find adequate rental units.

### **Fine-Tuning the Rent Control Program**

Whether or not major modifications in the existing rent control program are implemented, the operation of the program can be substantially improved in two key respects.

First, DCRA should develop a management information system for monitoring the District's rental housing stock. This would facilitate more effective enforcement of both rent control and the District's housing code.

Second, the hardship, substantial rehab, and capital improvements petition processes should be streamlined to operate more efficiently from the perspective of tenants as well as housing providers.

Both of these administrative enhancements would advance the objectives of rent control in the District. Together, they offer the potential to increase the coverage and consistency of rent control, ensure that the existing stock of rental units is not permitted to deteriorate, and offer housing providers a greater sense of control regarding their real estate investment decisions.

### **Expanding the Availability of Affordable Rental Housing**

Rent control can moderate the rate at which rents increase, but -- no matter how effectively it is administered -- it cannot eliminate the affordability problems confronting low and moderate income households.

Ensuring decent and affordable rental housing for all of the District's residents requires more direct measures -- to supplement the rents low and moderate income tenants can afford to pay, to preserve existing low-rent properties, and to produce additional, low and moderate cost rental units.

Currently, about 53,000 low and moderate income households in the District need help to obtain decent housing at rents they can afford. In the absence of rent control, the number of low and moderate income households with inadequate or unaffordable housing would exceed 60,000.

Clearly, the District government does not have either the resources or the capacity to single-handedly solve the problems of housing affordability and adequacy for all of its residents.

Responsibility for achieving this goal should be shared by the federal government, and by the governments of other jurisdictions in the Washington metropolitan area.

However, the District itself possesses an impressive arsenal of programs for making rental housing more affordable, which it could be deploying in a more systematic and effective manner.

Two major avenues are available to the District for expanding the number of low and moderate income households who receive assistance.

- 1) The condition and management of the District's public housing inventory should be improved so that the maximum number of households can be adequately sheltered in these units.

- 2) TAP resources should be fully utilized by increasing the rate at which certificates are issued, and by helping recipients find housing units in which they can receive benefits.







## DEFINITIONS



## DEFINITIONS

Affordable unit	Rental unit with a gross rent equal to or less than 30% of household's gross income
After-Tax Return	Cash flow plus appreciation, adjusted for federal income taxes
AHS	American Housing Survey, conducted by the U.S. Census Bureau
Capital improvements	Improvements that protect or enhance the health, safety and security of tenants, or the habitability of the rental unit
Cash Flow (or Net Income)	Rent reviewers minus all operating costs including interest and property taxes
Changes in services and facilities	Increases or decreases in related facilities or services that may be reflected in an adjustment in tenant rent
Civil Infractions Program	As yet to be implemented HID enforcement mechanism which will supplant criminal sanctions with civil fines
COG	Metropolitan Washington Council of Governments
Contract Rent	Monthly rent payment by tenant to housing provider, excluding any utilities paid directly by tenant
CPI	Consumer Price Index
DCRA	Department of Consumer and Regulatory Affairs
DHCD	Department of Housing and Community Development
DPAH	Department of Public and Assisted Housing
Emergency notices	Housing violation notices with compliance deadlines of 1 day or less
Equity	Total assessed value minus debt (or encumbrances)

Eviction protections	Procedural protections to ensure that tenants have adequate notice before eviction. Hearings can be held to examine the validity of the notice to vacate
Excessive rent burden	Gross rent (including utilities) greater than 30% of household income
Gross Rent	Full monthly housing cost, including any utilities paid by tenant
Hardship petitions	Petitions for a rent increase filed by landlords whose properties make less than 12% rate of return
HID	Housing Inspection Division, responsible for enforcement of the housing code
High income renters	Renters with gross income of \$50,000 or more
Inspection rating	A three grade classification (A, B, or C) system assigned to all HID inspected properties and related to building upkeep and compliance record of the owner
LAHDO	Land Acquisition for Housing Development Opportunities
Large individual owner	Individual with total DC holdings of 50 or more rental units
Large partnership	Partnership with total DC holdings of 50 or more rental units
Large properties	Rental properties with 50 or more units
Large units	Rental units with 6 or more rooms
Licensed properties	Any premises that is used for housing shall be licensed and registered with the Rental Accommodations and Conversion Division
Low income households	Households with gross income under \$15,000
Market Rent	Estimated gross rent in the absence of controls

Medium individual owner	Individuals with total DC holdings of 10 to 49 rental units
Medium sized properties	Rental properties with 10 to 49 units
Middle class families	Families with gross income of \$15,000 to \$24,000
Moderate income households	Households with gross income of \$15,000 to \$24,000
Net income	Total possible income from all sources minus operating costs and vacancy losses
Non-serious notices	Housing violation notices with compliance deadlines of more than 10 days
Operating costs	Sum of all costs including interest payments and property taxes
Overcrowded housing	Rental units with more than one person per room (not counting bathrooms and hallways)
Physically deficient	Units with one or more structural defects and/or three maintenance defects. The lack of complete plumbing; central heating; complete kitchen; water, toilet or heating breakdowns in the last 90 days for 6 hours or more are considered to be structural defects. Maintenance defects are classified as cracks and/or holes in walls, ceilings and floors; exposed electrical wiring; presence of rats or mice; unsafe common stairways.
Poor households	Households with gross income under \$15,000
Poor inspection ratings	Properties with "C" rating
Rent burden	Gross rent express as a percent of gross income
Rent ceiling	The maximum amount of rent a landlord may charge for a rental unit

Rent savings	Difference between actual rent paid and estimated "market" rent in the absence of rent control
Routine maintenance	Basic repairs and maintenance needed to provide decent and safe living accommodations for tenants
Serious notices	Housing violation notices with compliance deadlines of 10 days or less
Small individual owner	Individual with total DC holdings fewer than 10 rental units
Small/medium partnership	Partnership with total DC holdings fewer than 50 rental units
Substantial rehabilitation	Proposed rehabilitation equal to at least 50% of the assessed value of the building
TAP	Tenant Assistance Program is a rent subsidy program under the DC Rental Housing Act of 1985
Tenant petitions	Petitions filed with the Rental Accommodations and Conversion Division to challenge rental increases or violations of the Rental Housing Act of 1985
Vacancy increase	Rent increase allowed for a vacant unit- 12% or up to the level of comparable units in the same building
Voluntary agreement	Agreement entered into by the landlord and at least 70% of the tenants affecting rent ceilings

**ANNEXES**





## ANNEX A:

Summary of Findings  
for the  
Nine Original Study Items

1. The number of new or renovated units placed on the District's rental market after May 1, 1985.

Based on an exhaustive inventory of additions to and losses from the rental housing stock, we conclude that the number of units on the market increased by 1,631 between May 1, 1985 and April 30, 1987. This net increase resulted from the following flows:

Additions:

New Construction	1,003	
Substantial Rehabilitation	1,044	
Change in Number of Units	70	
Conversion from Owner-Occupied	106	
Conversion from Non-Residential	398	
Total Additions		2,621

Losses:

Removed from Use	152	
Demolished	11	
Change in Number of Units	29	
Conversion to Owner-Occupied	760	
Conversion to Non-Residential	38	
Total Losses		990

<u>Net Change</u>		1,631
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In Chapter 1, the section entitled "Changes in the Rental Housing Stock" traces the history of additions to and losses from the District's rental housing stock since the early 1970s.

2. The number of new or renovated units projected to be placed on the District's rental market through 1996.

The primary determinant of the number of units added to -- or lost from -- the District's rental housing stock over the next decade will be the number of households who choose to be renters within the District boundaries. The D.C. Department of Planning forecasts that D.C.'s total population will increase by more than 10,000 households by 1996. We anticipate that the share of these households who rent will remain at its current level (approximately 62%). If so, then the District's rental housing stock can be expected to grow by roughly 600 units per year on average. However, if the District's total population continued

to decline, as it has since the early 1970s, or if national economic conditions generate renewed homeownership pressures, the size of the District's rental inventory could actually contract by about 100 units per year on average, and still produce vacancy rates as high as 6%.

However, the fact that the total number of rental units is likely to be quite responsive to the aggregate demand for rental housing in the District does not mean that the housing needs of all D.C. renters will be met. The core of low and moderate income renters -- particularly the elderly and single-parent families -- will continue to face a shortage of affordable housing, regardless of the level of additions to the stock in the next decade.

To ensure that sufficient numbers of rental housing units remain available over the course of the 1990s, attention should be focused both on the number of units added to the stock annually and to the number of units removed from rental housing use. Between 1985 and 1987, about 500 units were removed from rental use annually, while 1,300 were added, resulting in a net increase of approximately 800 rental units per year. Strategies which minimize the number of units lost from the District's rental stock over the next decade can be just as effective for ensuring the availability of rental housing as strategies which maximize the number of units added to the stock. Moreover, since both new construction and substantial renovations are costly and require large-scale financing, the units produced will either charge high rents or require large subsidies to be affordable for low and moderate income households. In contrast, the preservation of existing units that already serve low and moderate income renters can generally be achieved at much lower costs.

The section entitled "Renter Households and the Rental Housing Inventory" in Chapter 4 focuses on expected trends in the need for and supply of rental housing in the District over the next decade.

### **3. An assessment of the effectiveness of the Tenant Assistance Program (TAP), and the projected cost of TAP in the absence of rent control.**

Altogether, 41% of the D.C. renters who do not already receive assistance under federal housing programs are eligible to participate TAP -- a total of 53,000 households. Approximately \$15 million in annual subsidies have been allocated for the program, enough to assist between 3,400 and 3,500 households, given current subsidy levels. However, as of January 1988, only 2,581 TAP certificates had been issued, and roughly half of these certificate holders (1,095 households) had succeeded in finding units in which they can actually receive benefits under the program.

TAP currently has a waiting list of over 10,000 households. The program is currently closed to new applications, other than

emergency cases, which are processed through the Department of Human Services. Less than one third of all the households who are eligible to participate in TAP know about the program. Participants appear to be among those with the most urgent needs for housing assistance -- they are poorer, more predominantly black, and less likely to be elderly than the population of eligible households:

	<u>Eligible Households</u>	<u>TAP Recipients</u>
Elderly	33%	12%
Black	74%	98%
Incomes --		
<\$15,000	77%	94%
\$15-\$24,000	23	6
\$25,000+	0	0

The recent introduction of new program variants may increase the rate at which households are enrolled in TAP, but additional efforts should be focused on both the rate at which certificates are issued and the share of certificate recipients that succeed in finding units in which they can actually begin to receive subsidy benefits. We recommend four important changes to increase the volume of certificates issued. The first of these is already in the planning stages:

Establish a one-stop application desk for all tenant subsidies. This will reduce the burden on needy households to go from office to office to apply for various assistance programs, and it will reduce the number of walk-ins to the TAP offices;

Centralize the scheduling of enrollment interviews and take into account the fact that roughly one third of scheduled appointments are likely to result in no-shows. The TAP manual suggests that enrollment interviews should be scheduled centrally, but currently TAP specialists schedule their own interviews, so that there is no way of knowing whether they are working as efficiently as possible.

Provide the TAP office with adequate clerical support so that specialists are not answering the phones and responding to individuals who walk into the office without appointments.

Reduce the burden on TAP specialists of responding to call-backs from TAP recipients with problems related to their current units, landlords, or neighborhoods.

If these administrative reforms are implemented, TAP staff will be able to issue certificates more efficiently, and their

supervisors will be in a better position to determine whether more specialists are needed (possibly on a temporary basis) to issue all of the available certificates as promptly as possible.

Even if a greater volume of TAP certificates are issued roughly half of the households who receive them can be expected to return them, unused, due to their inability to find a qualifying unit. This 50% success rate is also typical of the federal Section 8 program, which has had much longer to overcome administrative start-up programs. One way to address the relatively low success rate is to provide TAP recipients with more aggressive assistance in the housing search process. Currently, TAP staff provide certificate recipients with a list of buildings known to accept TAP recipients, and have taken some steps to promote the program among the city's housing providers. An alternative approach could include three important components:

Develop a comprehensive data base of available units throughout the city.

Aggressively promote TAP to housing providers.

Offer one-on-one housing search assistance to TAP recipients who need to move to qualify for assistance. This assistance can range from counseling on how to search for housing and how to make the most of an interview with a housing provider to actually accompanying individuals when they look for units.

These activities would not necessarily have to be performed by TAP staff. They might be performed jointly for TAP and the federal Section 8 certificate and voucher programs, or they might be contracted out to one or more of the non-profit housing counseling agencies that operate in the District of Columbia.

Even with housing search assistance, it is possible that a substantial share of TAP certificate holders (perhaps 30-40%) will not be able to find units in which they can receive benefits. One reason may be resistance to the program among housing providers. Only about half of the housing providers we surveyed indicated that they would be likely to participate in TAP if approached by a certificate holder. This resistance may diminish over time as TAP gains credibility among providers. Moreover, a larger share of District housing providers (accounting for 71% of the rental stock) would be willing to participate in TAP on behalf of an existing tenant, suggesting that the In-Place Component may be substantially more effective at achieving enrollment than the General Application Program.

In addition to the problem of resistance on the part of D.C. housing providers, the District's housing stock simply contains a limited number of units renting at or below the payment standards for both TAP and the federal Section 8 program. It is not necessarily that the payment standards are too low. The number of low and moderate cost housing units in the District is not

large enough to serve the combined number of low and moderate income households, and turnover occurs at an extremely low rate. Therefore, the long-term effectiveness of TAP may depend on the District's ability to induce the production of more moderate-cost rental units -- through the use of TAP and other subsidies -- to serve both TAP recipients and others with low and moderate incomes.

The cost of providing TAP assistance to all eligible households is estimated at \$225 to \$230 million annually under existing market conditions. The per unit cost would not be any higher in the absence of controls, since our estimates suggest that recently occupied units in the District rent for just as much as they would in the absence of controls. However, in the absence of controls, we estimate that an additional 9,000 households would be eligible for TAP, increasing the annual cost of an entitlement subsidy program by as much as \$35 million.

Past experience with federal housing assistance programs indicates that, even if certificates were offered on an entitlement basis, only about 40% to 45% of eligible households will participate, so that the 1988 cost to the District government of offering TAP to all eligible households would be between \$90 and \$103 million.

Chapter 2 provides a more extensive discussion and assessment of TAP. In addition, the final section of Chapter 4 outlines the key elements of a comprehensive approach for addressing the housing needs of low and moderate income renters in the District.

#### 4. The impact of rent control on the cost and supply of rental housing

Cost. We estimate that, in the absence of controls, D.C. renters would be paying about \$95 to \$100 per month more on average than they do today. This does not mean that, if controls were removed, all rents would immediately be raised by \$95 to \$100. Instead, it means that, in the absence of controls, prevailing rent levels would have risen more rapidly over the past decade and a half, and that, on average, rent levels would now be \$95 to \$100 higher.

The rent savings generated by controls moderate the problems of housing affordability faced by D.C. renters. In an uncontrolled market, the share of households paying more than 30% of their income for rent would increase from its current level of about 43% to more than 50%. Thus, while affordability problems in the District are severe today, a much larger number of renter households would pay excessive rent burdens in the absence of rent control.

Supply. Since uncontrolled rents would be \$95 to \$100 higher on average, we estimate that, in the absence of rent control, rent revenues to controlled units would be about 33% higher on

average. After adjusting for accompanying changes in property values, equity, interest costs, and property taxes, we estimate that D.C. housing providers would realize annual increases in net income ranging from about \$600 per unit in small properties to about \$1,350 per unit in large controlled properties. At the same time, annual appreciation gains would grow by amounts ranging from just over \$100 per unit in large properties to \$800 per unit in the smallest properties.

Since rent control significantly reduces rent revenues for the majority of D.C. units, some providers may be discouraged from adding new or rehabilitated units to the rental inventory, and others may allow the quality of the properties they own to deteriorate and ultimately remove units from the available supply. Moreover, even if investment in D.C. rental property is reasonably profitable, the existing climate of vigorous tenant protection -- including rent control, housing code enforcement, eviction protections, and condominium conversion restrictions -- may be sufficiently intimidating to cause some potential investors to turn to the neighboring suburban jurisdictions rather than to the District.

However, recent changes in the rental stock of other -- uncontrolled -- U.S. cities, as well as the opinions stated by housing providers who have recently added or removed units from the District's rental inventory, do not support the argument that rent control is responsible for reducing the supply of housing in the District of Columbia. In fact, we conclude that the existing system of controls has had relatively little impact on the supply of rental housing in D.C. Instead, two more global trends explain recent changes in the size of the District's rental inventory, as well as the existing shortage of affordable rental housing for low and moderate households.

First, during the 1970s, the demand for central city rental housing among middle and upper income households declined substantially -- in cities throughout the U.S. This decline was attributable both to tax and inflation incentives that made homeownership particularly attractive, but also to the expansion of suburban housing opportunities for minorities. Thus, unsubsidized rental production dropped and conversions to owner-occupied housing soared in many U.S. cities -- regardless of the regulatory environment. At the same time, the income levels of low and moderate income renters -- households who cannot afford the option of homeownership -- have not kept pace with the costs of producing and maintaining decent rental properties. So when units at the bottom of the rental stock are being removed from use, it is generally because market rents no longer support the investment. In other words, the resources of low income renters constitute the critical constraint on the profitability of rental housing investment.

Chapter 3 provides a more extensive analysis of a full range of hypotheses regarding the impacts of rent control on housing market outcomes in the District of Columbia.

5. An assessment of the present rent control program in terms of its ability to be understood, and its efficiency, economy, equity, and flexibility.

Understandability. Owners of almost 80% of controlled units in the District report that their understanding of the rent control program is "good" or "excellent. The provisions that appear to generate the greatest confusion among housing providers are those dealing with the timing of rent adjustments; owners of more than a third of controlled units indicated difficulty understanding these provisions.

Interviews with housing providers on the Advisory Committee appointed by the Mayor suggest that the technical details of rent controls -- particularly the computation and timing of rent increases -- are so complex that technical errors are extremely difficult to avoid. And if tenants challenge these errors through the formal petition process, the costs -- both in terms of penalties and legal expenses -- can be very high, even if the error was unintentional. As a result, some providers routinely pay lawyers to review their operations and to respond to tenant petitions.

Most tenants appear to have considerably greater difficulty understanding even the basics of rent control. While D.C. renters favor the existing system of controls by roughly three to one, almost 40% are unable to correctly indicate whether or not their units are controlled. Tenants in controlled units are more likely to know their control status than those who live in exempt units, and the share of households with accurate information increases systematically among those who have remained in the same units for several years.

Housing providers' and tenants' understanding of the rent control program are discussed in greater detail in Chapters 2 and 3, respectively.

Flexibility. The District's current system of controls is sufficiently flexible to allow housing providers to adjust to changing demand and supply conditions. There are several ways in which a unit's rent ceiling can be increased under the District's system of rent control. First, two types of adjustments are available to any accommodation that is licensed, registered, and in compliance with the District's housing code. These are 1) the increase of general applicability -- which allows the rent ceiling for a continuously occupied unit to rise by the previous year's Consumer Price Index (CPI), and 2) the vacancy increase -- which allows the rent ceiling for a unit that has been vacated to increase by 12% or to the rent ceiling for a comparable unit in the same property.

Most providers make use of the generally applicable rent adjustment process, with nine out of ten D.C. rental units

experiencing this type of increase in 1986. And for most types of rental property in the District, the rent adjustments of general applicability have kept pace with increases in operating costs during the 1980s. Even for units continuously occupied from 1981 through 1986, allowable rent adjustments would have kept pace with increases in the costs of operations for most types of rental properties. And since roughly 10% of units in the District turn over annually, most housing providers have the opportunity to increase their overall rent revenues at a somewhat higher rate than that of continuously occupied units.

In addition to the increase of general applicability and the vacancy adjustment process, housing providers can petition to "pass through" cost increases associated with capital improvements, substantial rehabilitation, or changes in services or facilities. And providers can obtain administrative approval for extraordinary rent increases necessitated by financial hardship, or secured by means of voluntary agreements with tenants. In 1986 about 8 percent of all controlled units in the District experienced additional increases in rent ceilings approved through one of the petition processes. Hardship petitions and voluntary agreements generally resulted in substantial increases in rent ceilings, while capital improvements increases were more moderate.

The operation of District's the rent control program, and the usage of various rent adjustment mechanisms are discussed in Chapter 2.

Efficiency, economy, and equity. The District's rent control program obviously does not represent a total solution to the problems of housing affordability, adequacy, and availability. However, the existing system of controls has moderated increases in rent levels for most households, particularly those who remain in their units for more than a year or two. We estimate that, in the absence of controls, the rent for the average D.C. unit would be between \$95 and \$100 per month higher, and roughly three quarters of D.C. renters would be paying higher rents than they do today. By reducing prevailing rent levels, the existing system of controls has made rental housing in the District more affordable than it otherwise would be.

However, not all D.C. renters benefit directly from controls. Because the District's rent control program allows larger rent increases when units change occupancy, the rent savings attributable to controls are greatest for households who remain in the same controlled units for more than a year or two. Recent movers, on the other hand, pay as much -- and possibly even more -- than they would in the absence of controls, since many housing providers raise rents to the highest allowable levels at the time of turnover. By targetting benefits to long-term stayers, rent control tends to provide the greatest rent savings to lower income renters, to elderly households, and to families with children. However, more affluent renters, as well as young singles and groups of young adults also obtain direct benefits



whenever they remain in controlled units for an extended number of years. And poor households who move are likely to pay rents that are just as high, or perhaps higher, as those that would prevail in an uncontrolled market.

Although rent levels in the District today are lower on average than they would be in the absence of controls, the rate of rent increases over the last decade and a half have generally kept pace with increases in operating costs. Thus, even for units that have been continuously occupied during the 1980s, the District's system of automatic rent adjustments appears to have compensated most housing providers adequately for increases in operating costs. And since about one in ten controlled units in the District change occupancy each year, most providers are able to increase their total rent revenues at a somewhat faster pace. Although the majority of controlled units in the District generate relatively low cash returns, after accounting for appreciation gains and tax benefits, the profitability of investment in D.C. rental housing appears to compare favorably to alternative investment opportunities.

While rent control has not caused the problems of housing availability and affordability in the District of Columbia, it certainly has not eliminated these problems either -- nor can it be expected to. Despite the rent reductions attributable to the existing system of controls, 43% of all renters in the District pay more than 30% of their income for housing, and about 10% pay more than three quarters of their income for housing, placing them seriously at risk of homelessness. And although rent control significantly reduces rent levels for those who remain in their apartments for several years, we estimate that recent movers pay rents as high or possibly even higher than they would in the absence of controls. As a result, poor households who move as well as newly forming households with low incomes face serious problems finding affordable rental housing in the District.

Chapter 3 addresses a full set of hypotheses about the impacts of rent control on the District's rental housing market.

## 6. The impact of rent control on small housing providers

About 16% of the District's controlled rental units (16,000 units) are owned by individuals whose total holdings amount to fewer than ten units. These individuals are not real estate professionals, and their primary reasons for investing in rental real estate are the tax advantages allowed under federal law before 1986. Average rent revenues among units owned by small housing providers are about thirty percent lower than the average for larger providers. But the quality of the units owned by small providers is above average -- none of the small providers in our sample owned properties with C inspection ratings.

Our analysis does not indicate that rent control per se affects small providers more adversely than larger property owners in the District. Tenant mobility rates, and hence, the impacts of rent control on rent levels, do not appear to differ systematically by type of provider or size of property. Small providers currently realize only minimal cash flow from their rental units, but their return on equity is substantially supplemented by property appreciation gains and, at least until 1986, by federal tax benefits. As a result, the estimated average after-tax return on equity for small providers would only be about one percentage point higher in the absence of rent control. For larger property holders, whose overall rates of return are much more dependent upon cash flow, rent control has a considerably greater impact on profitability.

However, some small providers, may be unreasonably burdened by the administrative requirements of rent control. The majority of these owners are not real estate professionals, and more than half manage their own properties. As a result, small providers appear to have greater than average difficulty understanding the rent control program. In fact, only 42% rated their understanding of the District's rent control program as as "good" or "excellent," compared to 78% of all other owners. Moreover, since small providers are less likely to be able to afford legal counsel on a regular basis, many may be discouraged from further participation in the D.C. rental market by the administrative burdens imposed not by price controls per se, but by the technical complexity of the District's rent control program.

#### 7. The number of District residents living in substandard housing and their location.

About 20% of unsubsidized D.C. renter households live in units that are physically deficient -- between 27,000 and 28,000 households altogether. Physically deficient units have been identified on the basis of specific, tenant-reported deficiencies, using a standard established by the U.S. Department of Housing and Urban Development. See Definitions for the specific deficiencies included. Of the 9,387 D.C. households who live in public housing, the Department of Public and Assisted Housing reports that 192 (2.1%) live in units requiring minor repairs, 419 (4.5%) live in units requiring moderate repairs, and 1,041 (11.1%) live in units scheduled for modernization. No data are available on the physical condition of privately owned, federally subsidized rental projects.

The share of unsubsidized rental units that are physically deficient is remarkably constant across rent levels and neighborhoods. Very low rent units (contract rent under \$200) have almost a 30% chance of being physically deficient, while very high rent units (contract rent over \$900) are about half as likely to be deficient. Not surprisingly, the incidence of deficiencies is highest in poor neighborhoods of the city, and

lowest in the city's more affluent areas. However, even in the most affluent neighborhoods of the city (ward 3) one in five renter households live in physically deficient units.

Incidence of Physically Deficient Rental Housing by Ward  
(unsubsidized rental units)

<u>Ward 1</u>	<u>Ward 2</u>	<u>Ward 3</u>	<u>Ward 4</u>	<u>Ward 5</u>	<u>Ward 6</u>	<u>Ward 7</u>	<u>Ward 8</u>
19.5%	17.0%	20.1%	21.2%	22.3%	21.8%	23.7%	19.4%

Chapter 1 provides additional details about D.C. renter households and housing conditions.

**8. An assessment of the enforcement of the District's housing code.**

This analysis substitutes for the original study item, which focused on the District's new Civil Infractions process for enforcing the housing code. Since the Civil Infractions program was not implemented until late in 1987, we conducted a base-line analysis of the existing housing code enforcement process.

All licensed residential properties in the District are subject to annual scheduled inspections. In addition to scheduled inspections, D.C. rental properties are inspected in response to complaints by tenants and/or neighbors. In fact, the vast majority of inspections actually occur as a result of complaints rather than through the scheduled inspections process. In both 1985 and 1987, the Housing Inspections Division (HID) fell short of its objective of conducting scheduled inspections in all licensed properties. Despite the limited coverage of the scheduled inspections, HID has handled a large volume of complaint-based inspections over the last three years. And the combination of housing code enforcement and rent control's requirement that properties must be in substantial compliance before rents can be increased annually appears to have been quite effective. The share of unsubsidized rental units that are physically deficient has declined from 26% to 20% since 1974, and most code violations are ultimately abated by property owners.

However, while the majority of code violations cited by District housing inspectors are ultimately abated by property owners, abatements generally do not occur within the times allotted by housing inspectors. Some phases of the abatement process could be substantially accelerated by means of more prompt action on the part of housing inspectors. First, notices often are not served until several days after an inspection has taken place, and the enforcement clock does not start ticking until service of notice has occurred. In addition, inspections and reinspections could be scheduled to coincide more closely with the designated abatement times, so that providers know that a housing inspector

will arrive to ensure that violations have been abated within the time specified. In some instances, reinspections appear to be hampered by tenants, who are unwilling to give up their keys, or to make themselves available to admit inspectors to their units. HID is currently experimenting with conducting some reinspections by means of telephone conversations with tenants as a mechanism for overcoming this problem. Because of delays in the inspections process, a significant share of violation notices are "cancelled" by housing inspectors each year.

See Chapter 2 for a complete description and assessment of the housing code enforcement process.

9. An assessment of the impact on the rental market of 1) vacancy decontrol, 2) luxury decontrol, 3) increasing the small landlord exemption, and 4) using family income as a component of a rent control formula.

Vacancy Decontrol represents a plan for the gradual phase-out of rent control. Following a voluntary move or legal eviction, any unit in substantial compliance with the local housing code would become exempt from controls. The current pool of approximately 106,000 controlled units would be reduced only very gradually under a system of vacancy decontrols. In the first year of vacancy decontrol, the impact would be small -- reducing the number of controlled units by about 10%, or 10,000 to 11,000 units. By the end of six years, approximately half of today's controlled rental units would be exempt -- with roughly 50,000 units remaining within the existing system of rent stabilization.

The impacts of vacancy decontrol on housing affordability and supply can be directly inferred from our analysis of the effects of rent control on market outcomes (see Chapter 3). In the short-term, the effects would be modest. Households who remain in their units would continue to be protected by controls, and movers would in all likelihood pay approximately the same rents that they do today, since newly occupied units currently rent for as much -- and sometimes more -- under the existing system of controls as they would in an uncontrolled market. In the longer term, as decontrolled units begin to dominate the market, prevailing rent levels would correspond to the estimated market rents discussed in Chapter 3, which are \$95 to \$100 higher on average than today's controlled rents. All households living in decontrolled units would be paying higher rents than they are now, except recent movers, who would be paying about the same amounts as they do today.

As an expanding share of all units were decontrolled, provider revenues would gradually rise to roughly 33% above their current levels. Providers who already experience a high degree of turnover would see relatively small revenue gains, while owners with more long-term tenants would gradually obtain substantially larger revenues. If as much as half of the increased revenue was allocated to property maintenance and improvements, then the

quality of the existing rental stock would gradually be enhanced, and it is possible that fewer units would drop out of the stock as a result of deferred maintenance and deterioration. However, at least some of the increased rent revenues would almost certainly be absorbed by property owners, increasing the profitability of investment in D.C. rental housing. Despite the increased profitability of rental housing investment, there is no evidence to suggest that the number of units available for rent would be significantly greater if vacancy decontrol was implemented.

Although vacancy decontrol would gradually reduce the number of units subject to controls, it would complicate the District's rent control program tremendously, from the perspective of housing providers, tenants, and program administrators. Specifically, almost all buildings that are currently controlled would continue to have some controlled units for at least six years, with the number of controlled units in any property likely to change every year. Therefore, housing providers and DCRA would be faced with the task of keeping track of which units in a given building remain subject to controls and which units are exempt. Tenants -- who are currently quite poorly informed about the control status of their units -- would certainly have even greater difficulty understanding their rights and circumstances, since different rent levels and different rules for rent adjustments would apply within the same rental building.

Luxury decontrol represents an effort to target the benefits of rent control more closely to low and moderate income households, compared to the existing system which generates benefits even for the most affluent renters. If luxury decontrol is considered in the District, exemptions should be based on rent levels, as in other cities. Defining a package of "luxury" amenities -- security system, air conditioning, or swimming pool, for example -- is simply too likely to include buildings that serve low and moderate income households as well as buildings that primarily serve the city's most affluent renters. Using either the top 10% or the top 5% of the current contract rent distribution to define "luxury" units produces the following cut-offs for 1987:

#### 1987 "Luxury" Rent Levels

	<u>Effic-</u> <u>ency</u>	<u>2-3 rooms</u>	<u>4-5 rooms</u>	<u>6+ rooms</u>
top 10%	\$550	\$625	\$800	\$1,300
top 5%	\$600	\$700	\$900	\$1,500

The effects of luxury decontrol on the District's rental housing market would be minimal. Since a disproportionate share of the highest rent units are exempt from controls, the 1987 rent levels listed above would apply to only 6% or 2% of the controlled stock, respectively -- approximately 600 or 200 units. The

occupants of these units are almost exclusively affluent, white non-elderly singles and groups of unrelated adults who moved into their units within the last two years. Therefore, these households are not receiving significant monetary benefits from the existing system of controls, and would not be substantially affected by the removal of controls.

Since only a small number of existing units would be affected by luxury decontrol, the impact on housing supply in the District of Columbia would be purely symbolic. The majority of high rent units are either already exempt from controls or can be expected to change occupancy frequently, so that housing providers would probably experience only minimal revenue gains. And luxury decontrol would have no effect on properties that are in poor condition or those at risk of being removed from the stock. However, luxury decontrol might moderate perceptions that the District has a hostile regulatory environment, or that rent control benefits affluent tenants at the expense of housing providers.

Despite the minimal impact of luxury decontrol on housing affordability and supply, it would complicate the administration of the rent control program. Like vacancy decontrol, luxury decontrol would exempt individual units within buildings that otherwise remain subject to rent control.

An expanded small-owner exemption would decontrol units owned by individuals whose total D.C. holdings amount to less than ten rental units. We estimate that 16% of the controlled units in the District today -- about 16,000 units -- would qualify for this exemption, since the majority of units in the District's controlled stock are owned by large scale individual investors, partnerships, and corporations.

There are two basic arguments for extending the small-owner exemption from rent control in the District. First, small owners are likely to be disproportionately affected by the Tax Reform Act of 1986, which substantially reduced the effective tax subsidies to investment in rental real estate. Virtually all of the small owners that we surveyed (96%) indicated that they do not plan to invest further in D.C. rental housing, primarily because of the tax reforms enacted by the federal government in 1986. And our estimates of after-tax return on equity suggest that the 1986 Tax Reform Act may indeed reduce the returns that small owners receive by as much as 30%. Larger D.C. housing providers -- who do not rely as heavily on tax benefits to make their investments profitable -- will probably be less affected. If the small-owner exemption were expanded, these providers would raise rents substantially -- possibly by as much as 30% over the next several years. Their profits would increase, maintenance might improve somewhat, but there would probably be no perceptible impact on the number of units in the District's rental stock. However, if these small rental properties remain subject to controls, the impacts of the 1986 Tax Reform Act may reduce profits sufficiently to result in the removal of units from the rental stock.

A second argument for expanding the small-owner exemption is that small, non-professional investors may be unreasonably burdened by the administrative requirements of rent control. Indeed, the District's small housing providers report more difficulty understanding the existing system of rent control than do larger investors in D.C. rental housing; only 42% of the small providers rated their understanding of the law as excellent or good, compared to 78% of all other owners. Most small housing providers are not real estate professionals; more than half manage their own properties, and many may not be able to hire lawyers on a routine basis. As a result, these individuals are substantially less familiar with the District's rent control program, and may have greater difficulty taking advantage of the opportunities available to them under the law.

Incorporating household affordability as a factor in determining rent adjustments would represent an attempt to more fully address the District's housing affordability problems through the rent control program. We considered three possible approaches for incorporating household affordability as a factor in determining rent adjustments. The first approach would incorporate the actual income of a controlled unit's current occupant into the rent adjustment calculation. A more limited strategy for incorporating renter incomes into the determination of rent adjustments would apply only to those rent increases that currently require administrative approval -- increases for substantial rehabilitation, capital improvements, changes in the level of services, and financial hardship. A final option for incorporating tenant incomes into the rent adjustment process would apply more broadly to all controlled units. Specifically, the formula for calculating the increase of general applicability could be modified to reflect increases in renter income levels as well as -- or instead of -- increases in operating costs.

While provisions of this kind are well-intentioned, they would almost certainly do more harm than good from the perspective of both housing providers and tenants. Specifically, they would discourage providers from accepting and/or retaining low and moderate income tenants; add to the complexity of the District's rent control program; and disrupt the features of the existing rent control program which enable housing providers to earn a reasonable return on their investment and recover the costs of property improvements. Low income renters would face even greater difficulty finding affordable housing than they do today, and properties that serve low income households would suffer from under-maintenance, deterioration, and eventual removal from the rental stock.

See Chapter 4 for a fuller discussion of these alternatives to the existing rent control program, and for our recommendations for improving the operation of rent control and for the outlines of a more comprehensive approach to the problems of housing availability, adequacy, and affordability in the District of Columbia.





ANNEX B:  
Surveys, Samples, and Analytic Methods

1987 Urban Institute Survey of D.C. and Suburban Renters

During the summer of 1987, The Urban Institute — with the assistance of Lawrence Johnson and Associates — surveyed a sample of renter households in the District of Columbia and the surrounding suburban jurisdictions.

Sampling and Survey Procedures. Sampling and survey procedures were designed to produce a random sample of 3,000 unsubsidized D.C. renter households. The basis for the sample was a random dialing technique employed in three geographic areas — D.C., portions of Maryland within the Capital Beltway, and portions of Virginia within the Capital Beltway. For each of these three areas, unique telephone numbers were selected for inclusion in the sample by systematically drawing from all working blocks of numbers in all telephone exchanges assigned to the area. A working block is defined as 100 contiguous telephone numbers containing three or more residential telephone listings.

The sample of telephone numbers included 17,316 D.C. telephone numbers, and 2,727 telephone numbers for each of Maryland and Virginia. These large sample sizes were established to ensure that 3,000 D.C. surveys and 600 suburban surveys were ultimately completed. For each of the three areas, the total sample was divided into several sample replicates to ensure that the ultimate sample of respondents was representative of the original sample of telephone numbers.

For each telephone number dialed, several questions were asked at the outset of the interview to determine whether the respondent was an unsubsidized renter household. If not, the interview was terminated. Due to the combination of unanswered telephones, non-working numbers, non-residential, owner- occupant, or subsidized respondents, and unwillingness to participate in the survey, the rate of completions was fairly low. Nevertheless, the target of 3,000 D.C. interviews and 300 interviews in each of Maryland and Virginia was achieved.

The survey was administered by Lawrence Johnson and Associates, using a Computer Assisted Telephone Interviewing (CATI) system. This system computerized the questionnaire itself, a list of telephone numbers to call, records of previous attempts to reach sampled numbers, and questionnaire responses. The CATI system was designed to prevent some of the most common interviewer errors, such as failure to follow skip patterns, and to detect illogical responses. Usually, errors of this kind have to be detected and corrected after data collection; the CATI system avoids many errors by only prompting the interviewer to ask questions that are relevant given responses to earlier questions, and by making range and logic checks during the process of data collection. In addition, since interviewers enter responses to the survey directly into the computer as the interview is conducted, potential transcription errors are minimized.

Interviewers were supervised at all times. To ensure that questions were being asked correctly, supervisors monitored a sample of the telephone interviews. In addition, supervisors reinterviewed a sample of each day's completed

interviews. In this verification interview, the supervisor asked whether anyone in the household had been interviewed about their housing, and reasked three simple short-answer items to confirm that the interview had in fact been completed.

When an interviewer encountered a respondent who did not speak English and who could not bring an English-speaking person to the telephone, a written record was made of the telephone number. This number was then temporarily removed from the automated dialing list, with a notation regarding the language that the respondent seemed to be speaking. When several such cases accumulated, an interviewer with appropriate language skills was called in to administer the questionnaires. Specifically, Spanish- and Vietnamese-speaking interviewers were available to conduct interviews. Respondents who could not understand these interviewers were dropped from the sample.

Consideration was given to administering a separate survey to a sample of households without telephones. This strategy was implemented in The Urban Institute's study of rent control in Los Angeles on the assumption that poor households are the most likely to lack telephones, and that the responses of households without telephones may be systematically different from those of households with telephones. In Los Angeles, however, we found that the inclusion of the non-telephone respondents in the household survey had no impact on the distribution of responses. Moreover, as discussed further below, the U.I. survey obtained a more than adequate number of responses from poor households. Therefore, we concluded that a survey of non-telephone households was unnecessary.

Sample Characteristics. The sampling and survey procedures produced a sample of 3,000 D.C. interviews that closely represents the unsubsidized D.C. renter population. Nevertheless, we found that the representativeness of the D.C. sample could be improved by re-weighting. The suburban samples were not re-weighted because they were small, and because their use was primarily for comparison purposes.

The raw data in the D.C. sample over-represent affluent households at the expense of low and middle income renters. The first two panels in Exhibit B.1 compare the distribution of households in our D.C. sample to the distribution of D.C. renter households in the 1981 Annual Housing Survey (AHS). Subsidized households — which are excluded from our sample — have been deleted from the AHS income distribution, but not from the other AHS distributions shown in this table. In addition, 1981 income ranges have been updated to 1987 dollars, using the D.C. all item Consumer Price Index.

Since it seems unlikely that the distribution of renter households by broad income category has changed significantly between 1981 and 1987, we conclude that our sample includes too many affluent households, and not enough moderate and middle income households. Nevertheless, our sample includes sufficient numbers of responses in each income range to yield reliable results. We hypothesize that the over-representation of high income renters may explain the apparent over-representation of college graduates, the slight under-representation of large households, and — possibly — the over-representation of efficiency units. Nevertheless, the distribution of 1987 survey respondents corresponds reasonably well to the distribution of AHS households on most household and dwelling unit characteristics.

**EXHIBIT B.1: Comparison of 1981 AHS and 1987 UI Samples**

HOUSEHOLD CHARACTERISTICS	1981 AHS		1987 Survey Raw Data		1987 Survey Weighted Data	
Income						
< \$15,000	54,400	38.9%	903	32.4%	1,085	38.9%
\$15-25,000	39,300	28.1%	784	28.1%	784	28.1%
\$25-35,000	30,400	21.7%	463	16.6%	606	21.7%
\$35-50,000	7,400	5.3%	297	10.6%	148	5.3%
\$50,000 +	8,300	5.9%	342	12.3%	166	5.9%
Education						
No HS Diploma	21,400	13.4%	314	10.5%	307	11.1%
High School	72,000	45.0%	885	29.7%	877	31.7%
Some College	23,600	14.8%	655	22.0%	614	22.2%
College Grad	42,900	26.8%	1,123	37.7%	968	35.0%
Household Size						
One Person	72,100	45.1%	1,334	44.9%	1,284	47.0%
Two People	41,300	25.8%	873	29.4%	776	28.4%
3-4 People	33,900	21.2%	613	20.6%	536	19.6%
5+ People	12,500	7.8%	153	5.1%	134	4.9%
DWELLING UNIT CHARACTERISTICS	1981 AHS		1987 Survey Raw Data		1987 Survey Weighted Data	
Year Structure Built						
Since 1981	N/A	—	31	2.8%	26	2.4%
1970-1981	7,800	4.9%	69	6.2%	108	9.8%
1960-1970	28,400	17.8%	211	19.0%	197	17.9%
1940-1960	55,800	34.9%	376	33.8%	365	33.1%
Before 1940	67,800	42.4%	455	41.0%	432	39.2%
Unit Size						
Efficiency	9,000	5.6%	286	9.5%	272	9.9%
2-3 Rooms	74,000	46.3%	1,245	41.4%	1,186	43.1%
4-5 Rooms	60,700	38.0%	1,168	38.9%	1,056	38.4%
6+ Rooms	16,100	10.1%	306	10.2%	236	8.6%
Total	159,800		3,005		2,750	

The deviation between our sample and the distribution of unsubsidized renter households reported in AHS is large enough to justify re-weighting. Exhibit B.2 presents the t- statistics that measure the significance of the differences between the adjusted AHS income distribution and our raw income distribution. In addition, this exhibit shows the weighting factors applied to correct the income distribution. Using these weighting factors, each high income response in the UI sample is counted as considerably less than one full household, while each low and middle income response is counted as slightly more than one household. All data presented in the body of this report are weighted.

## EXHIBIT B.2: Weighting the 1987 UI Sample

Income	1981 AHS		1987 Survey Raw Data		T- Statistic	Weight
< \$15,000	54,400	38.9%	903	32.4%	6.98	1.202
\$15-25,000	39,300	28.1%	784	28.1%	0.00	1.000
\$25-35,000	30,400	21.7%	463	16.6%	6.49	1.310
\$35-50,000	7,400	5.3%	297	10.6%	-12.27	0.497
\$50,000 +	8,300	5.9%	342	12.3%	-14.09	0.484

By correcting the income distribution, we expected to achieve a closer match with the AHS distributions of renter households by education, household size, and unit size, as well as a better distribution by ward. The third panel of Exhibit B.1 summarizes the weighted survey distribution. The process of weighting by income category had little effect on the other household, dwelling unit, and location distributions. However, the remaining discrepancies are not large enough to warrant a more complex, two-way or three-way weighting scheme. Moreover, comparisons of 1974 and 1981 AHS data suggest that D.C. has been experiencing significant shifts in the composition of the renter population, so that the differences between the 1981 AHS and 1987 UI samples may well reflect population changes rather than sampling errors.

Data Verification. To minimize respondent errors, we attempted to verify three key elements of the household survey by comparing household responses to city records. Specifically, for a subset of 1,319 D.C. respondents who voluntarily supplied their addresses, rent, control status, and housing quality data were obtained from city records. The verification of rent control status was extremely valuable, and is discussed further below. For rent levels and housing quality, however, we concluded that the city data were less reliable than the household responses. The primary reason for rejecting both the rent and the housing quality measures obtained from city records is that these data apply to properties, while our household survey is made up of individual dwelling unit responses. Thus, city records indicate the ceiling rent for units of a particular size in a property, while the UI survey provides the actual rent reported by a household for a particular unit. Similarly, city records provide a quality ranking for a whole property, while the UI survey provides evidence of specific deficiencies reported by a household for a particular unit.

Verification of Tenant Reported Control Status. All survey respondents were asked whether their units were controlled or exempt. For survey respondents who were willing to give their addresses, control status was verified against DCRA registration data. Altogether, control status was verified for 1,103 of the 3,000 households surveyed. As discussed in the body of this report and in Section II of the Technical Supplement, a large share of D.C. renters did not know their control status. Moreover, for the sub-sample of verified responses, only 60% of tenants had correctly identified their control status. The clear implication of this result is that tenant reported control status is not a reliable indicator of a unit's actual control status, and that tenant responses could not be used to distinguish controlled from exempt units for our analysis of the impacts of controls. Therefore, all elements of the analysis in which

control status is a factor are limited to the subset of cases for which verified control status was obtained from DCRA records. Tenant responses are only used in our analysis of which groups of tenants are most likely to have accurate information about the control status of their units. Fortunately, the sub-sample of cases for which control status was verified closely matches the overall sample of D.C. renter households, as shown by Exhibit B.3

### Financial Statements and Provider Questionnaire

The analysis of ownership and financial characteristics is based on data collected during the fall of 1987 on the financial characteristics of controlled rental properties in the District of Columbia and on the attitudes of D.C. housing providers toward investment in controlled rental housing. In all, the sample of financial statements covers 817 properties, and the housing provider questionnaire was returned for 244 properties. These data have been weighted to represent the distribution of controlled units in the District by the size of the building in which they are located.

Sample Design. Exhibit B.4 presents the number of rental properties and rental units by building size for the District of Columbia as a whole, based on a listing of these properties and their characteristics maintained in the District's Metropolitan Area Geographic Information System (MAGIS). This universe includes controlled and exempt properties, but excludes condominium and cooperative buildings in which some or all units are rented. A separate list of rental units in condo and co-op projects was also developed, as explained further below.

Lawrence Johnson and Associates, a sub-contractor to The Urban Institute, designed the sampling methodology for selecting a stratified random sample of 1,900 addresses from the MAGIS list of D.C. rental properties. Properties with fewer than 5 units were overrepresented in this sample, because most of these properties were expected to be exempt from controls, and very large properties were oversampled because they account for such a significant share of the rental housing stock as a whole.

In addition, a random sample of 100 rental units in condominium and 50 cooperative buildings was also selected from the MAGIS data files. This sample was not stratified by building size, but simply provides a random selection of rental condo and coop units.

Financial Data Collection. For the 1,900 sampled rental properties and the 150 condo and co-op addresses, U.I. and LJA staff examined registration data maintained by the D.C. Department of Consumer and Regulatory Affairs. For all cases in which a registration file could be found, the 1985 registration statement was reproduced, indicating control status, reasons for exemptions from rent control, and — for controlled properties — a 1985 financial statement. Registration files were found for 1,375 of the properties in our sample, and financial statements were obtained for 817 controlled properties. File data on the 150 rental condo and co-op units were less complete, probably because a large share of these units are not subject to controls, and because they change from renter to owner-occupancy with relative frequency. These data were not coded and computerized, due to their incompleteness and ambiguity.

EXHIBIT B.3

CHARACTERISTICS OF THE VERIFIED SUB-SAMPLE

	% of Full Sample	% of Verified Sub-Sample
Income		
< \$15,000	32.4%	33.8%
\$15,000-24,000	28.1	28.7
\$25,000-34,000	16.6	18.3
\$35,000-49,000	10.6	10.3
\$50,000+	12.3	9.0
Race		
Black	59.3	62.5
White	4.1	3.4
Hispanic	5.5	5.0
Other	31.1	29.1
Life-Cycle Group		
Non-Elderly Singles	40.7	43.7
Adult Groups	14.9	12.7
Elderly	12.2	12.0
Childless Couples	11.0	9.6
Husband-Wife Families	8.5	9.1
Female-Headed Families	12.8	12.9

EXHIBIT B. 4

CONTROLLED RENTAL PROPERTIES--SAMPLE CHARACTERISTICS

Building Size	<u>Actual</u>		<u>Sample</u>	
	Buildings	Units	Buildings	Units
1-2 Units	26828	30320	19	23
3-4	4188	15455	18	68
5-9	1277	8367	152	1023
10-19	1499	21735	128	1789
20-49	788	24285	100	3172
50-99	217	15325	31	2269
100-199	94	14053	51	6721
200+	69	22774	33	11777
Total	34960	152314	532	26842

The financial data for the 817 controlled properties with 1985 registration forms was coded and computerized by LJA staff. These data were then carefully reviewed by Urban Institute staff, and three types of errors were systematically corrected. First, some of the registration forms had been filled out incompletely or incorrectly by the housing providers. These errors were corrected by examining the form as a whole, and in a few cases, by calling the housing provider to verify essential information. Second, some of the forms were incorrectly coded or key-punched. And finally, some of the registration forms applied to multiple addresses, which are apparently treated as combined "rental projects" for accounting purposes. In cases where we could not determine the number of units to which a registration form applied, financial data had to be dropped from our sample. Altogether, a total of 194 cases had to be dropped, and 91 cases were combined into projects consisting of multiple buildings. The final data set consists of complete financial statements for 532 controlled rental properties — consisting of 26,842 units.

Because we sampled at different rates based on the size of rental properties, and because financial data were not available for all of the properties in the sample, we have calculated weights for all of the rental properties in our sample, to reflect their probability of being selected. As shown in Exhibit B.5, property weights were assigned to each building size class to reflect the actual distribution of controlled properties by building size. Thus, each property's weight is the reciprocal of its probability of being selected from all controlled properties.

In our analysis, all data are reported on a weighted per unit basis. Thus, financial and other characteristics are adjusted for the number of units in the property, and weighted to reflect both the property's contribution to the controlled D.C. housing stock, and its probability of being in our sample. This means that our analysis and results focus on the average controlled unit, or the distribution of controlled units, rather than on buildings — which contribute varying numbers of housing units to the stock.

Provider Questionnaire. To supplement the data gathered from DCRA registration forms, questionnaires were mailed (in November 1987) to the owners and/or managers of all the controlled rental properties for which financial data were available. These questionnaires were designed to gather additional information about ownership form, size of holdings, reasons for investment in D.C. rental property, attitudes toward the rental market, the regulatory environment, and the D.C. Tenant Assistance Program (TAP), and plans for future rental housing investment. Because of the length of the questionnaire and its importance to our analysis, an aggressive follow-up effort was pursued to maximize the number of completed forms. Specifically, all survey recipients were called within two weeks of the date when questionnaires were mailed to ensure that survey forms had been received and were being completed; staff responsible for these call-backs were well informed about the study and the role of the provider survey in the study design, and were trained to answer questions and respond to concerns about the questionnaire; all of the providers who owned and/or managed more than 15 of our sample properties were contacted directly by Urban Institute research staff, who stressed the importance of their responses to the objectives of the study as a whole, and offered assistance in the completion of the questionnaires; altogether, survey recipients received at least three call backs if they did not return their questionnaires within a 6-week response



## EXHIBIT B. 5

## CONTROLLED RENTAL PROPERTIES--SAMPLE WEIGHTS

Building Size	Share Units Controlled	Estimated Number Controlled Units	Sample Weight
1-2 Units	0.46	14038	610.35
3-4	0.46	7126	104.80
5-9	0.75	6275	6.13
10-19	0.86	18770	10.49
20-49	0.91	22109	6.97
50-99	0.90	13846	6.10
100-199	0.81	11317	1.68
200+	0.82	18634	1.58

Note: The share of units in each building size category that are controlled is obtained from our survey of renter households (see Technical Memorandum #1, March 1988). The estimated number of controlled units in each size category is obtained by multiplying the share that are controlled by the total number of units from Exhibit B.1, and the sample weight for each size category is obtained by dividing the total number of controlled units by the total number of sample units.

period; in addition, intensive assistance in completing the questionnaires was provided to respondents with particularly large numbers of sample properties.

This follow-up strategy was effective in generating completed questionnaires for a total of 244 controlled properties — accounting for 12,801 units. In other words, supplemental property descriptions and attitudinal data were obtained for 46% of the properties and 48% of the units in our sample. Moreover, as shown in Exhibit B.6, the properties for which surveys were returned are comparable — with respect to size and inspection rating — to the sample as a whole. In other words, no obvious classes of controlled rental properties were under-represented in the provider survey.

### **Rent Estimation Methodology**

This section details the methodology used for estimating what D.C. rents would be in the absence of controls. The methodology consists of four basic steps:

- 1) Estimate the relationship between housing unit attributes and rent levels in 1974 — before the imposition of rent control in the District of Columbia.
- 2) Using this relationship, estimate what units now available for rent in D.C. would have rented for in 1974.
- 3) Increase these pre-control rent estimates to reflect the rate of rent inflation typical of uncontrolled central cities between 1974 and 1987.
- 4) Adjust these final market rent estimates to reflect for locational rent differences that prevail today.

Housing Unit Attributes and Rents — 1974. The methodology we have adopted assumes that the relative value or cost of different types of rental units would have remained reasonably constant over the 1974 to 1987 period, had it not been for the imposition of rent control. In other words, the proportionate effect of an extra bedroom, or a better quality unit on rent would have remained the same, even though overall rent levels would certainly have increased. Therefore, our first step is to estimate the relationships that prevailed before 1974 between housing unit attributes and unit rents in the District of Columbia.

Exhibit B.7 presents the results of a multivariate regression equation expressing gross rent as a function of unit attributes.\* The estimated regression coefficients in this equation can be interpreted as the "prices" of the various attributes. The objective of a regression equation of this kind is to explain as much of the observed variation in rents as possible, so that the equation can be used for predictive purposes. Therefore, we experimented with several alternative specifications, and the equation presented in Exhibit B.7 represents the one with the greatest explanatory power and the most significant coefficients.

EXHIBIT B.6

PROVIDER SURVEY RESPONDENTS

Building Size	<u>Sample Properties</u>		<u>Survey Respondents</u>	
	Number	Percent	Number	Percent
1-2 Units	19	3.6	2	.8
3-4	18	3.4	12	5
5-9	152	28.6	72	30
10-19	128	24.1	61	25.4
20-49	100	18.8	37	15.4
50-99	31	5.8	13	5.4
100-199	51	9.6	26	10.8
200+	33	6.2	27	7.1

## EXHIBIT B.7

## 1974 GROSS RENT REGRESSION EQUATION -- D.C. UNITS

Attribute	Coefficient	Standard Error
Intercept	6.027**	.040
Single-Family House	-.151**	.018
Duplex	-.318**	.024
3-4 Unit Building	-.337**	.017
5-9 Unit Building	-.268**	.016
10-19 Unit Building	-.206**	.014
20-49 Unit Building	-.194**	.018
Efficiency	-.609**	.030
2-room unit	-.484**	.026
3-Room Unit	-.306**	.021
4-Room Unit	-.198**	.024
5-Room Unit	-.081**	.020
No Complete Bathroom	-.528**	.031
1 Bathroom	-.263**	.030
Central City	-.023	.012
Recent Mover	.020	.019
Moved in 1-2 Years Ago	.122**	.012
Moved in 2-3 Years Ago	.079**	.013
Moved in 3-4 Years Ago	.050**	.015
Moved in 4-5 Years Ago	.069**	.023
Househead Head is Black	-.122**	.023
Househead Head is White	.090**	.023
R <sup>2</sup>	49.49	

Note: The dependent variable is the natural logarithm of gross rent.  
 \*\*indicates significance at the 99% confidence level.

Source: 1987 UI Tenant Survey

1974 Rents for 1987 Rental Units. The next step is to use the equation outlined above to estimate what the units that are available in D.C. today would have rented for in 1974. To predict a unit's 1974 rent, its attributes — values for all of the explanatory variables in the regression — are "plugged into" the regression equation. In other words, the value of each attribute is multiplied by the corresponding coefficient, and the results are summed to arrive at a predicted rent. This techniques was used to estimate 1974 rents for all of the units in our 1987 sample of D.C. households.

There are two ways in which these 1974 rent estimates can be used. First, they provide the basis for our estimates of 1987 rents in the absence of controls, for the 1974 to 1987 period. More specifically, the ratio of a unit's 1987 rent to our estimate of what the same unit would have rented for 1974 reflects rent inflation, controlling for any changes in unit quality. We compared constant quality rent inflation indexes for D.C. and the surrounding suburbs to the rate of inflation in median rents, and found virtually no difference. This reassured us that the change in median rent levels is a reasonable approximation of a constant quality rent inflation index for other central cities.

Inflating 1974 Rents to 1987. The third step in our methodology is to inflate the 1974 rents for 1987 units upwards to reflect the average rate of rent inflation that would have prevailed in D.C. in the absence of controls. As discussed in the body of this report, examination of rent trends in the Washington suburbs and in other central cities in the Northeast and Mid-Atlantic regions suggests that rents in D.C. would have increased by about 9.5% per year on average in the absence of rent control. The estimated 1974 rents for all 1987 D.C. units were inflated at this rate to yield 1987 estimates of rents in the absence of controls.

Adjusting for Location Differences. Finally, we adjusted the 1987 market rent estimates for variations in rents among D.C. wards. More specifically, neighborhood conditions clearly play a role in determining rent levels; two otherwise comparable units located in different surroundings may well have very different rent levels. Our 1974 regression equation does not include a location variable because none was available in the AHS data. However, ward identifiers are available for a large share of the D.C. units in our 1987 sample. We concluded that the relative rents of housing units in different wards — after controlling for unit size, quality, and length of tenure — are probably about the same today as they would be in the absence of controls. In other words, there is no reason to believe that rent control has affected ward rent differentials. Therefore, we estimated the relative price of a comparable housing unit located in each of the District's eight wards. These price adjustment factors, presented in Exhibit B.8, are based on the coefficients for location variables in a gross rent regression estimated for D.C. rental units

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\* Actually, the dependent variable in our regression equations is the natural log of gross rent. This means that the coefficients reflect the percent change in rent attributable to a unit change in any of the various explanatory variables.

EXHIBIT B.8

RENT ADJUSTMENT FACTORS -- BY D.C. WARD

WARD	ADJUSTMENT FACTOR
1	0.9392
2	1.0541
3	1.0656
4	1.0621
5	0.9197
6	1.0391
7	0.9658
8	0.9357

SOURCE: Urban Institute Calculations

in 1987. These factors are applied to the estimates of 1987 market rents obtained from the 1974 gross rent regression. Specifically, the estimated market rent of each 1987 unit is adjusted up or downward to reflect the relative advantages or disadvantages of the ward in which it is located.

### Components of Inventory Change

This section outlines local records used to inventory additions to and losses from the District's rental housing stock from May 1985 through April 1987. These data were assembled in the fall of 1987.

Sources and Handling of Inventory Additions Data. Additions data were culled from Certificate of Occupancy records kept by the D.C. Department of Consumer and Regulatory Affairs (DCRA) for the period from 5/1/85 to 4/30/87. Certificates of Occupancy were chosen as the best source of inventory additions data because:

- 1) they best reflect the date that a unit is ready to come on the market;
- 2) they more selectively record actual additions, in contrast with typical building permit data which document units authorized or planned but not always completed; and,
- 3) they provide rich property information in a form that was useful and relatively accessible for our study purposes.

Records on a rental property's present and previous use, present and previous number of units, and reason for obtaining a Certificate of Occupancy provided the basis for categorizing each addition by component in our inventory change model. We verified the larger additions and clarified any ambiguous records by telephone with the owner or agent listed on the Certificate of Occupancy. Several records were consolidated into one in cases where the additions or buildings could be determined to be part of a single project.

The figures on the number of additions will slightly undercount (rather than overcount) the actual number that occurred because of the nature of the data source and because we conservatively counted only verified additions. Specifically,

- 1) only those who filed for a Certificate of Occupancy are included in the data—though all are required to do so, some activity always goes on outside official records;
- 2) roughly 15 days of the daily Certificate issuance log (our entry to the actual permit files) were unavailable;

- 3) several possible small inventory changes were left unclarified (and therefore excluded) because of the difficulty involved in checking them (owner could not be reached, etc.)—intensive effort was made to check the larger changes, and many of the remaining ambiguous records are believed to involve ownership change only;
- 4) a conservative assumption was made about single family dwellings converting to 2-unit flats—where the prior tenure of the single family dwelling is unknown, it is assumed that only one rental unit was added to the inventory even though the owner may have moved (thus actually adding two rental units).

A best guess correction, taking into account all of the above factors except activity outside legal channels, might add only another 125 units, or less than five percent.

Sources and Handling of Inventory Losses Data. All units leaving the rental inventory are required to go through the evictions office at DCRA, even where the tenant has already vacated the unit. Section 501 of the Rental Housing Act of 1985 governs these removals. We collected data from the required filings with DCRA and the Notices to Vacate where the reason given was one of the following:

- 501(d) "to recover possession of the rental unit for the person's immediate and personal use and occupancy as a dwelling";
- 501(e) "to sell the rental unit...for the immediate personal use and occupancy by another person";
- 501(g) "for the purpose of immediately demolishing the housing accommodation in which the rental unit is located";
- 501(i) "for the immediate purpose of discontinuing the housing use and occupancy of the rental unit."

Restrictions too detailed to cover here accompany each provision. Further required information provided the basis for assigning each loss to a component in our inventory change model. Housing providers are also required to indicate their registration and/or exemption status under rent control. Information on mergers, which require structural alterations and recertification, came from Certificates of Occupancy.

Again, the count of losses is unlikely to be exact. While most instances of non-compliance would involve evictions or notices to vacate where the tenant was somehow undesirable to the housing provider and the unit was subsequently re-rented, an undetermined number of actual losses from the inventory take place outside of District records, and would be difficult if not impossible to document. On the other hand, we are aware of at least one instance where a properly filed notice to vacate did not lead to a loss from the inventory, because the owner's reasons for removing the units were negated by a voluntary rent increase negotiated with tenants.



Sources and Handling of Condominium Registration Data. Separate data were collected on condominiums newly registered with DCRA. We were able to study this limited number of properties extensively, tracing each from registration log to application log to the D.C. Municipal Automated Geographic Information System (MAGIS) and the private LUSK directories. This process allowed us to determine as nearly as possible the percent of each property's units that are rented and the appropriate component of inventory change involved. Registrations involving new construction, conversion of non-rental properties, or rehabilitation of vacant properties may add units to the city's rental inventory, whereas those involving the conversion of apartment units may remove some units from the rental inventory. As condominiums are legal entities involving the form in which title is held, condominium registration data should be complete. Conversion and sale is not possible without being registered. MAGIS' determination of the tenure status of each unit is based on whether or not the address to which the assessment and property tax bill are mailed corresponds to the property address.

To determine whether these condominium-associated components of change should supplement our Certificate of Occupancy and Evictions data, how much the sources overlap, and to what extent the date ranges are comparable, we cross-checked the data sources. Those additions which were not already listed or which were found to have Certificates of Occupancy outside of the relevant date range were discarded, and the remainder added to the additions file. Loss data was similarly supplemented. In all, condominium records added about 10 percent to both the addition and loss files.

Geographical Analysis. To take full advantage of the detailed property information gathered from our intensive data collection effort from District records, The Urban Institute contracted with the Computer Mapping and Spatial Analysis (CMSA) Laboratory at the University of Maryland. The addresses of properties where additions and losses occurred were digitized, linked with other data about each property, and overlaid onto District Ward boundaries using the CMSA Laboratory's sophisticated geographic information system, ARCINFO.

Digitizing the property addresses of rental additions and losses allowed visual analysis of the geographic distribution of stock change activity in the District by component and size. It also enabled us to produce rental inventory change statistics by ward, important information which would otherwise not have been available.

Except for tenure change from rental to owner-occupied, all sites where rental units were either added or lost were digitized. Instances of tenure change, while not representing overwhelming number of units, contained more sites than the other ten components combined. Thus, a 25% sample of these sites was deemed more than sufficient to establish the geographic distribution of this activity. See Section III of the Technical Supplement for complete results of the mapping analysis.

Telephone Interview Procedure. Components of inventory change accounting for more than 15% of additions or losses were deemed worthy of more detailed study. Survey instruments guided the in-depth interviews with

housing providers. Of particular interest were the motivations of housing providers' supply decisions, their opinions of rent control and the regulatory environment, subsidy programs, and building and tenant characteristics. Project resources, the small size of some of the components, and the difficulty of contacting owners limited the number of surveys for each component and dictated the largely reportorial—as opposed to statistical—tone of the discussion of survey results.

Between the three main components of additions surveyed, 17 interviews were conducted with housing providers together responsible for 26% of all additions to the D.C. rental inventory between May 1985 and April 1987. Interviews of four owners responsible for new construction covered 10% of newly constructed units; the remaining owners could not be contacted or would not participate. Interviews of seven owners responsible for the rehabilitation of non-residential structures covered 42% of these units. Interviews of six owners responsible for the rehabilitation of vacant structures covered 39% of these units. Differences between components were not significant enough to remark on in the text, given the small sample.

Between the two main components of losses surveyed, 11 interviews were conducted with housing providers together responsible for 6% of all losses to the D.C. rental inventory between May 1985 and April 1987. Interviews of four owners responsible for retrievable losses covered 24% of these units. Interviews with seven owners responsible for tenure change losses covered 3% of these losses; the similarities of these seven small owners made further interviewing unnecessary. The significant differences between the responses of owners in each of the two components are noted in the text.

### **Estimating Investment Returns for Controlled Properties**

Property Appreciation. Property appreciation is an essential element of profit to investors in rental real estate. Each year, the cash returns realized by an investor are essentially supplemented by the increase in property value. However, appreciation gains can only be realized by selling or refinancing the property, which obviously does not happen every year. Therefore, many measures of return to investment in rental real estate discount appreciation benefits, to reflect the fact that they will not be realized until sometime in the future. For this analysis we have adopted a simpler approach. Since we have no data on how frequently D.C. rental properties are sold or refinanced, and since our primary interest is in comparing the profitability of different classes of rental real estate, we have not discounted the value of appreciation gains. Instead, using data on average assessed property values in 1982 and 1987, we have estimated an average annual appreciation rate for each building size category. These annual rates are then applied to average per unit property values for different types of controlled rental units to yield an annual estimate of the dollar value of appreciation gains. Exhibit B.9 presents average assessed property values for 1982 and 1987, obtained from the District's Metropolitan Area Geographic Information System (MAGIS). These values have been used to estimate an average annual rate of property appreciation for each building size category.

EXHIBIT B.9

AVERAGE ASSESSED VALUE BY BUILDING SIZE--1982 & 1987

<u>Building Size</u>	<u>1982</u>	<u>1987</u>	<u>Average Annual % Change</u>
1-2 Units	\$ 85,120	\$103,722	4.03%
3-4	66,072	97,071	8.00
5-9	101,832	133,057	5.49
10-19	140,670	172,827	4.20
20-49	355,656	445,486	4.61
50-99	1,100,507	1,357,675	4.29
100-249	3,290,420	3,641,775	2.05
250+	8,778,525	8,306,554	-0.01

Federal Tax Benefits. Until 1986, the differential tax treatment of competing investment opportunities often played a central role in shaping investor decisions. Housing, in particular, has been the beneficiary of at least two decades of preferential tax treatment. The two primary tax benefits available to investors in rental housing were accelerated depreciation and a reduced tax rate on long term capital gains. We have applied a set of fairly conservative assumptions about the tax treatment applicable prior to 1986 to approximate the after-tax return on investment in different types of D.C. rental properties. As discussed earlier, the goal of these assumptions is to allow us to compare different classes of property under different economic and regulatory assumptions, not to produce definitive measures of provider profits. The after tax return on equity has been calculated as:

$$\text{Return} = (\text{Income} - \text{Expenditures} + \text{Appreciation} - \text{Taxes}) / \text{Equity}$$

where

Income = total actual income per unit

Expenditures = total operating expenditures plus interest per unit

Appreciation = average annual rate of appreciation times per unit value

$$\text{Taxes} = t(\text{Income} - \text{Expenditures} - \text{Depreciation}) + c(\text{Appreciation})$$

t = marginal tax rate — tested at both 35% and 50% ; c = capital gains tax rate — half the marginal tax rate ; Depreciation =  $(1/15)$  Depreciable Basis  
Depreciable Basis = 85% \* Value

Exhibit B.10 presents appreciation and tax calculations for several key types of controlled rental units.

Impacts of Rent Control. To estimate the impacts of controls in returns to rental property investment, we simulated the effects of market rent levels on pro forma financial statements of properties in different size categories. The first step was to convert our market rent estimates into rent revenue estimates for controlled providers. The market rents estimated using the hedonic methodology outlined earlier are \$95-\$100 higher on average than actual gross rents. However, after limiting the sample to controlled units, and subtracting utilities paid directly by tenants, we found that contract rents for controlled properties would average about 33% higher in the absence of controls. This average applied consistently across building size categories. Therefore, we applied a 33% increase to gross rent revenues to the average pro forma financial statement for each building size.

Higher rent revenues produce a second key change in a property's financial statement—higher property value. We retained the existing rent-to-value ratios for each property size category in order to obtain estimates of property values in the absence of controls. As a result of increased property values, property taxes, interest costs, equity, and appreciation benefits also increase. Again, we retained the existing relationships

## EXHIBIT B.10

## CALCULATING AFTER-TAX RETURN ON EQUITY

For The Average Controlled Unit in a Building With:				
	1-2 Units	3-4 Units	20-49 Units	100-249 Units
Net Income	-\$181	\$110	\$578	\$1,153
Equity	\$33,394	\$10,981	\$10,370	\$10,668
Income/Equity	-0.54%	1.00%	5.57%	10.81%
Appreciation Rate	4.03%	8.00%	4.61%	2.05%
Appreciation	\$2,441	\$1,805	\$567	\$349
(Inc+App)/Equity	6.77%	17.44%	11.04%	14.08%
After Tax Income (@ 50%)	\$3,455	\$2,048	\$1,063	\$1,320
After Tax Income (@ 35%)	\$3,097	\$2,008	\$1,088	\$1,374
After Tax Return (@ 50%)	10.35%	18.65%	10.25%	12.37%
After Tax Return (@ 35%)	9.27%	18.28%	10.49%	12.88%

between property taxes and value, debt and value, interest costs and debt, and rate of appreciation. Results are presented in Exhibit B.11.

Tax Reform Act of 1986. The impacts on investment returns of TRA 1986 are extremely complex, and sensitive to the circumstances of individual investors. However, two key features of the recent tax reform have been incorporated into our pro forma financial statements--restricted depreciation schedules and reduced tax rates. As shown in Exhibit B.12, we modified our basic calculations of after tax return on equity to reflect much slower depreciation schedules and lower marginal tax rates.

### **Data Gathering Procedures for Analysis of TAP**

Data for the assessment of the Tenant Assistance Program was obtained from several different sources.

- 1) Information from The Urban Institute Tenant Survey was used to estimate the size and characteristics of the TAP-eligible population.
- 2) Information on TAP applicants was drawn from the computerized preapplication file maintained by DHCD. This file contains basic demographic data for all household assigned a waiting list number.
- 3) Information on TAP recipients was drawn from TAP program records. These consist of a file folder for each TAP recipient, organized alphabetically and maintained in a retriever system. Individual files include: pre-applications, applications, income verification data, requests for lease approval, housing unit inspection records, subsidy calculation worksheets, lease and lease addenda, and any subsequent documentation. Variables of interest were collected from the files and computerized by ICF, Incorporated. Every third case was selected, for a total sample size of 312 cases.
- 4) Information on program operations and issues was obtained through interviews with TAP and DHCD staff and other interested parties. Key contacts include:
  - o Ann Avelino, TAP Program Chief: all aspects of program operations and performance.
  - o Conway Wilson, TAP Program Deputy Chief: program operations, management, and records system.
  - o Knox Hayes, DHCD: performance of TAP, recent legislative changes, and future issues.
  - o Jenna Thomas, DHS: DHS role and responsibilities under the Emergency component.
  - o Rick Harris, DHCD: information on projects and subsidies for the designated unit component.

EXHIBIT B.11

CALCULATING AFTER-TAX RETURNS  
IN THE ABSENCE OF RENT CONTROL

For the Average Controlled Unit in a Building With:

	1-2 Units		3-4 Units		20-49 Units		100-249 Units	
	Actual	Market	Actual	Market	Actual	Market	Actual	Market
Revenues	\$4,573	\$6,082	\$3,053	\$4,060	\$4,179	\$5,558	\$4,811	\$6,399
Value	\$60,534	\$80,510	\$22,564	\$30,010	\$12,308	\$16,370	\$17,010	\$22,623
Equity	\$33,394	\$44,414	\$10,981	\$14,605	\$10,370	\$13,792	\$10,668	\$14,188
Property								
Taxes	\$692	\$920	\$273	\$363	\$201	\$267	\$239	\$318
Interest	\$1,416	\$1,883	\$1,003	\$1,334	\$384	\$511	\$480	\$638
Appre- ciation	\$2,441	\$3,246	\$1,805	\$2,400	\$567	\$754	\$349	\$464
Total								
Expend	\$4,754	\$5,766	\$1,805	\$2,400	\$3,601	\$4,676	\$3,658	\$5,147
Net								
Income	-\$181	\$316	\$110	\$348	\$578	\$882	\$1,153	\$1,252
Income/ Equity (Inc+App)/	-0.54%	0.71%	1.00%	2.39%	5.57%	6.40%	10.81%	8.82%
Equity	6.77%	8.02%	17.44%	18.82%	11.04%	11.86%	14.08%	12.09%
After-Tax Return	10.35%	10.97%	18.65%	19.34%	10.25%	10.66%	12.37%	11.38%

# EXHIBIT B.12

## CALCULATING AFTER-TAX RETURN ON EQUITY SUBJECT TO TRA 1986

For The Average Controlled Unit in a Building With:

	1-2 Units	3-4 Units	20-49 Units	100-249 Units
Net Income	-\$181	\$110	\$578	\$1,153
Equity	\$33,394	\$10,981	\$10,370	\$10,668
Income/Equity	-0.54%	1.00%	5.57%	10.81%
Appreciation Rate	4.03%	8.00%	4.61%	2.05%
Appreciation (Inc+App)/ Equity	6.77%	17.44%	11.04%	14.08%
After Tax In- come (@35%)	\$2,124	\$1,596	\$946	\$1,247
After Tax Re- turn (@ 35%)	6.36%	14.53%	9.12%	11.69%



- o Ms. Coleman, Section 8 Program Division: comparison of Section 8 and TAP operations, staffing, and performance.
- o Ruth O'Sullivan, Quadel Consulting: information on program procedures development and staffing issues; perspectives on program performance.
- o Tom Borger, Borger Management: provider perspectives on TAP.
- o Michael Barnet, University Legal Services: role of ULS in initial pre-application outreach; ongoing activities; perspectives on TAP performance.

### Estimation of Operating Expense Escalation

The rental increase of "general applicability", or automatic increase, is linked to changes in the Consumer Price Index for Urban Wage Earners and Clerical Workers. Operating costs, however, may depart from general price trends. Therefore, the automatic rent increases may over- or under-compensate for real changes in operating costs. Moreover, given the different operating cost profiles of buildings of varying size, some property types may be relatively disadvantaged under this adjustment mechanism. This analysis estimates the change in operating costs for rental properties according to building size classification.

To estimate changes in operating costs for rental properties of different size classifications, we estimated the general price changes for each operating cost item between 1981 and 1987, then weighted these data by their shares of operating costs for properties in our 8 building size categories.

Operating Cost Components. We did not attempt to price each component of operating costs, choosing rather to focus on those items comprising the bulk of total operating expenses. Neither did we fully price each component according to actual usage—on a per job basis, for example, in plumbing repair—but relied on general price trends for labor or other standard cost units.

Service and Maintenance Costs. On the advice of a housing provider representative on the Rent Control Advisory Committee and a representative of the Property Managers Association, we consulted several large contractors in each category of maintenance typically performed on rental property to obtain changes in skilled labor rates for each type of job. As labor rates represent the bulk of the cost of each maintenance activity, changes in labor costs should accurately reflect changes in overall per-job costs. Maintenance categories included:

- o Painting/Decorating
- o Plumbing
- o Heating/Ventilating/Air-conditioning (HVAC)
- o Elevator Repair and Maintenance
- o Roofing
- o Groundskeeping

For all categories except groundskeeping, we collected data on changes in hourly rates from one or two large contractors. Groundskeeping labor costs are assumed to track the minimum wage.

To each hourly rate, we added an estimated cost for Workmen's Compensation insurance, Supplemental Security Income (social security), and Unemployment Insurance. Workmen's Compensation was valued at the midpoint of the range of rates provided by a major carrier, and was costed in an amount equal to the hourly wage. Unemployment Insurance was assumed to be the average for the District as reported by the District Office of Employment Security. Social security was applied at the statutory rate.

Exhibit B.13 shows the estimated hourly rates, and total percent change in rates, for each maintenance category. The percent increases across categories show remarkable uniformity.

### EXHIBIT B.13

#### Estimated Hourly Labor Rates by Maintenance Category

1981, 1987

<u>Category</u>	<u>1981 Rate</u>	<u>1987 Rate</u>	<u>Percent Change</u>
Plumbing	\$38.90	\$45.40	+16.7%
HVAC	40.00	51.00	27.5
Elevator	57.20	73.70	28.8
Roofing	34.30	43.10	25.7
Electrical	32.00	40.80	27.5
Painting	22.90	28.40	24.0
Grounds	3.20	4.30	34.4
Average	\$32.64	\$40.96	25.5%

Utility Costs. Utility cost data were estimated using the Consumer Price Index for this component for the Washington, D.C. SMSA. From January 1981 through December 1987, the Fuel and Other Utilities Index increased 30 percent.

Insurance. Insurance costs vary with the rate charged, and the amount of required coverage. Rates vary with the type of property being insured, and are dependent on factors such as building size, age and condition of the structure, quality of original construction, presence of an elevator, any special fire prevention features, and location. Of course, the range of property types in the District is wide. However, for purposes of comparison, unique building characteristics are ignored. Only building size rate differentials are considered. Fire insurance rates by building size are presented in Exhibit B.14.

**EXHIBIT B.14**  
**PROPERTY INSURANCE RATES**  
**BY BUILDING TYPE**  
(Per \$100 coverage)

Building Size (Units)	Joisted Masonry		
	1981 Fire	1987 Fire	Pct. Chng
<u>Building:</u>			
Up to 10	.297	.330	+11.1%
11 to 30	.396	.437	10.3
Over 30	.51	.56	9.8
 <u>Contents:</u>			
Up to 10	.297	.330	+11.1%
11 to 30	.341	.378	10.9
Over 30	.374	.414	10.7

Note: Joisted Masonry selected because it represents the upper bound in the percent change in rates. Rate increases for other construction classes—frame, non-combustible, masonry non-combustible, and modified fire resistive—have been slightly lower.

Source: Coverage Lines Manual, ISO Commercial Risk Services, Inc., 1983 and 1987. 1983 rates unchanged from 1981.

Given the consistency in the direction of rate change, we can apply the average changes for these property categories more generally to other types of rental property.

In addition to the change in rates, the amounts of required coverage differ as well. For fire insurance coverage, we assume that coverage changes are directly proportionate to changes in property assessed value. For different categories of building size, we computed the change in median assessed value from 1981 to 1986 as supplied by the District's Planning Office, and extrapolated the trend to cover the additional year. We then used these percent changes, together with the changes in rates, to produce a total estimated change in insurance costs by building size. These are shown in Exhibit B.15.

# EXHIBIT B.15

## ESTIMATED CHANGES IN INSURANCE COSTS BY BUILDING SIZE 1981-1987

<u>Size Category</u>	<u>Percent Change</u>
1-2	+35.4%
3-4	94.3
5-9	41.5
10-19	38.2
20-49	40.1
50-99	32.7
100-249	36.2
250+	25.9

Property Taxes and Other Cost Items. Property tax rates did not change over the period. The percent change in property taxes is the same as the change in median assessment for each size category. Exhibit B.16 shows the change in median assessment for each building size category.

# EXHIBIT B.16

## CHANGE IN MEDIAN ASSESSED VALUATION BY BUILDING SIZE CATEGORY 1982-1987

<u>Units in In Structure</u>	<u>Percent Change</u>
1-2	22.0%
3-4	75.0
5-9	27.5
10-19	24.5
20-49	26.8
50-99	20.3
100-249	23.5
250+	14.1

Other principal operating cost items include management fees, assumed to remain constant over the period, and administrative costs, including legal fees, telephone, and advertising. We have not attempted to price the cost changes for these latter items.

Operating Cost Shares. The estimated cost changes for each component of operating costs must be weighted by their relative shares of total operating costs for each building size. These weights are presented below.

# EXHIBIT B.17

## OPERATING COST COMPONENTS AS A PERCENT OF TOTAL OPERATING COSTS BY BUILDING SIZE

COST ITEM	BUILDING SIZE (N of Units)							
	<u>1-2</u>	<u>3-4</u>	<u>5-9</u>	<u>10-19</u>	<u>20-49</u>	<u>50-100</u>	<u>101-250</u>	<u>250+</u>
Service & Maintenance	22%	24%	25%	23%	21%	20%	17%	18%
Administrative	16	9	7	8	9	7	9	12
Utilities	9	32	34	41	38	40	36	34
Operating	11	9	10	10	16	16	19	19
Fees & Insurance	19	7	7	5	8	4	7	7
Property Taxes	21	14	12	8	6	8	8	6
Management Fees	3	5	7	6	5	5	4	4

Source: Calculated by The Urban Institute based on 1985 Registrations data.

With the exception of single- and two-unit properties, cost ratios are roughly similar across building size categories for most expenditure items. One- and two-unit buildings typically contain individually-metered rental units, accounting for the low share of operating expenses attributable to utility cost for that building type. Conversely, Fees and Insurance, and Property Taxes comprise a higher share of total operating expenses, reflecting high per-unit assessed values.

Rental Property Total Operating Cost Increases. For properties in each size category, the increase in each cost item is weighted by the percentage of total operating costs represented by that item. A weighted average is then computed. Exhibit B.18 shows the resulting estimated operating cost increase for each building size.

## EXHIBIT B.18

### ESTIMATED OPERATING EXPENSE INCREASE BY BUILDING SIZE 1981-1987

<u>Building Size</u>	<u>Percent Increase</u>
1-2	31%
3-4	41
5-9	33
10-19	31
20-49	35
50-99	30
100-249	30
250+	29
Automatic Rent Increase	31%

#### Petition Data Collection Methodology

All data on the number and disposition of petition filings by year, and the physical and financial characteristics of properties for which petitions were filed, were obtained from records maintained by the Rental Accommodations and Conversions Division (RACD).

Outcomes Data. RACD staff provided the basic counts of petitions filed in each year from 1982 to 1987. Urban Institute research staff compiled from RACD logs the disposition of all housing provider petitions filed in 1986; no log of tenant petition filings is maintained.

In addition to collecting information on petition outcomes, Institute staff compiled an inventory of those housing provider petition types most frequently filed—hardship, capital improvement, and voluntary agreements, for 1986. This inventory consisted of the petition I.D. number, ward and number of units of the property for which the petition was filed, and the percent increase in rent ceiling requested, and approved, for hardship petitions and voluntary agreements, and the monthly dollar increase in rents for capital improvements petitions filers. To support more extensive analysis of hardship petition filings, Institute staff compiled inventory data for all 1985 and 1987 hardship petitions.

Tenant petition data is not routinely kept by RACD. Institute staff sampled 25 petitions for which a hearing was held, and recorded a description of the complaint, and the outcome of the hearing.

Financial Characteristics of Petitioning Properties. Analysis of the financial characteristics of petition filings was conducted on a sample basis. For hardship and capital improvements petitions, and voluntary agreements, 25 1986 petitions of each type were randomly sampled based on filing date. Institute staff then obtained copies of the 1985 Registration forms for sampled properties. If no form was available, the form for the next property in order of filing date was obtained. These data were compared to data for all controlled properties as recorded from Registrations data.

In addition to the basic financial analysis conducted for each petition type, supplemental analysis on hardship petition filings examined the relationship between property appreciation rates as reflected in assessed values, and the locational distribution of 1985-1987 petitioners. From the Metropolitan Area Government Information System (MAGIS) we obtained median assessed values for single and multi-family properties in each census tract in Tax Years 1982 and 1987; calendar years 1981 and 1986. Institute staff coded the census tract of each hardship petitioner, and then examined whether the number of properties filing or the approved percent increase in rent ceiling was linked to rates of property value appreciation. Regression analysis produced insignificant results.

### **Housing Code Enforcement Histories**

During December 1987 and January 1988 The Urban Institute collected information on housing inspections conducted in 1985 for a sample of rental properties in the District.

Sampling and Data Collection Procedures. The search for 1985 housing inspection records began with the addresses of 814 rent controlled properties which had a 1985 registration form filed with the Rental Accommodation and Conversion Division (RACD). Each address was typed into the Housing Inspection Division's computer to ascertain the building's housing code rating. HID's inspection files were then searched to locate inspection records for all 1985 inspections conducted on these properties. A total of 785 inspection records were located for 319 properties. The remaining 495 properties had no record of any 1985 inspections in their files.

The following information was obtained from each inspection record:

1. inspection case number assigned to the particular inspection.
2. type of inspection — license, complaint, or inspector pick-up.
3. date of inspection.
4. number of violations.
5. date of service of notice of violation.
6. number of days given to correct violations.
7. description of violations (if the compliance period was 10 days or less).
8. reinspection dates and number of violations abated at each reinspection.
9. disposition of the notice of violation:

- a. notice abated by owner and date of abatement
- b. notice abated by city, date of referral to Assessment Branch, date of abatement by city, and cost of repairs
- c. notice referred to Corporation Counsel and final outcome of case
- d. notice cancelled by HID with date and reason for cancellation

**Sample Characteristics.** The initial sample of 814 are rent controlled buildings and are weighted to overrepresent large buildings. However, the inspection rates generated by the flow sample data do not vary greatly by building size category (except for 20-49 unit buildings). Thus, re-weighting the flow sample data in order to project inspection and code violation rates for the entire population is not particularly useful.

Moreover, there is good reason to be cautious about projecting the flow sample data to the HID population of licensed buildings. A significant number of 1985 inspection records may have been missing from the inspection files of the 814 buildings that comprised the initial sample. Large differences between wards in the percentage of sampled buildings that had at least one 1985 inspection record raise this concern. As shown in Exhibit B.19, this percentage was roughly twice as large in Wards 1 and 8 as it was in the other wards. Yet, the intensity of inspection activity — measured in terms of the average number of inspections per inspected building — was almost as high in Wards 2 and 5 as it was in Wards 1 and 8. One possible explanation for this seeming incongruity is that more complete inspection records were maintained for Wards 1 and 8 than for Wards 2 and 5, with the result that a significant number of inspected buildings were excluded from the flow sample data for Wards 2 and 5.

Missing inspection records are likely to influence the flow sample data in two different ways. First, a number of buildings that erroneously showed no 1985 inspection record would be improperly excluded from the sample of inspected buildings. Second, the average number of inspections per inspected building would be understated.

#### EXHIBIT B.19

##### DISTRIBUTION OF INSPECTIONS BY WARD

	WARD								TOTAL
	1	2	3	4	5	6	7	8	
Number of Bldgs. in Initial Sample	110	115	69	96	77	99	115	132	814
Number of Bldgs. with a 1985 Inspection Record	73 66%	36 31%	21 30%	35 36%	25 32%	20 20%	34 30%	75 56%	319 39%
Number of Inspections	210	95	46	71	65	36	49	213	785
Average Inspect. per Inspected Sample Building	2.88	2.64	2.19	2.03	2.60	1.80	1.44	2.84	2.46

Source: HID 198 Files for 319 Flow Sample Properties



## ANNEX C:

### Contents of the Technical Supplement

- I. CONDITIONS AND TRENDS IN THE D.C. RENTAL HOUSING MARKET:  
WHAT'S BEEN HAPPENING?
- II. RENT CONTROL IN THE DISTRICT OF COLUMBIA: THE TENANTS'  
PERSPECTIVE
- III. COMPONENTS OF INVENTORY CHANGE IN THE D.C. RENTAL HOUSING  
STOCK
- IV. FINANCIAL AND OWNERSHIP CHARACTERISTICS OF CONTROLLED RENTAL  
UNITS IN THE DISTRICT OF COLUMBIA
- V. ASSESSMENT OF THE TENANT ASSISTANCE PROGRAM
- VI. OPERATION AND ADMINISTRATION OF THE DISTRICT'S RENT CONTROL  
PROGRAM
- VII. HOUSING CODE ENFORCEMENT IN THE DISTRICT OF COLUMBIA
- VIII. THE SPECTRE OF HOMELESSNESS: PROFILE OF A POPULATION AT  
RISK

The Technical Supplement sections explain analytic methods and present additional details on major components of our study structure. All of the key results and conclusions from these sections have been incorporated in the final report.

