Policy Analysis

Cato Institute Policy Analysis No. 127: The Source of America's Housing Problem: Look in Your Own Back Yard

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Executive Summary

The housing problem--particularly the shortage of housing for the poor--emerged as one of the major domestic issues of the 1980s and threatens to continue well into the next decade. The signs are everywhere. Homelessness has been a major concern for nearly 10 years. Rents have been absorbing ever-increasing portions of poor people's incomes. In some cities, the rental vacancy rate has reached a dangerously low 3 percent or less.

Added to that atmosphere has been the drama of scandal. The allegation that former Republican officials were able to obtain large kickbacks by helping to steer federal housing funds to favored developers has fueled the suspicion that the whole problem starts at the top. In October 1989, when 40,000 demonstrators descended on Washington and marched to demand "housing now," carrying placards that condemned Samuel Pierce and Deborah Gore Dean, a familiar social chord was struck: People want housing, but the government won't give it to them. Corruption and venality are to blame.

When articulated clearly, that argument usually indicts the federal government's housing policies on three counts:

> (1) Federal housing assistance was reduced unmercifully during the 1980s. In 1981 the Department of Housing and Urban Development had budget authorizations of $32.2 billion; by 1989 they had been slashed to a mere $6.9 billion--a reduction of 78 percent.
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> (2) The federal government has abandoned its 50-year-old commitment to build public housing. In 1979 Congress authorized nearly 55,000 new units of public housing. In 1984 the number of units authorized was zero, and it has averaged less than 7,400 since then. That drastic reduction in public housing construction during the Reagan years caused homelessness to increase.
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> (3) What little money remained in federal housing programs' budgets was misappropriated--either entrusted to embezzlers or squandered on political favoritism. Between $2 billion and $4 billion was stolen from HUD by private contractors, and HUD lent well-connected developers millions of dollars' worth of Section 8 moderate-rehabilitation program funds. Although intended for the poor, many of the rehabilitated homes ended up being occupied by members of the middle class.

Unfortunately, few of the charges made in that three-part argument are true, and the ones that are true are largely irrelevant. Authorizations of federal housing funds decreased during the 1980s, but in constant dollars, outlays increased by more than 65 percent. Nor has there been a reduction in the construction of public housing, even though

Congress authorized far less during the Reagan administration; a large number of previously authorized units have been brought on line.

Finally, the alleged misappropriation of Section 8 moderate-rehabilitation program funds is certainly reprehensible, and the stolen money should be recovered if possible. But that scandal is little more than a side show to the housing situation. Section 8 had long been infamous for creating an account that serves as a slush fund and benefiting the middle class. It was precisely for those reasons that the Reagan administration tried to eliminate it.

What is most significant, perhaps, is that in the wake of the HUD scandals, few Americans are aware of a great accomplishment of the Reagan administration: the long-awaited introduction of a true housing voucher. Largely because of its partisanship, the press has taken little notice of that development except to condemn it once in a while. Nevertheless, the voucher program is a remarkable success and is rapidly revolutionizing housing assistance. Moreover, unlike previous programs, it is practically immune from corruption because the vouchers are awarded to tenants rather than housing providers.

Clearly the argument that the federal government is the source of the nation's housing problem is flawed. Let us consider the three-count indictment of Reagan-era federal housing policies at length.

Reagan-Era Budget Cuts

The statement "HUD's budget authorizations have been cut by almost 80 percent, from $32 billion in 1981 to only $7 billion in 1989" has been repeated so often that it will probably soon be nominated for a postage stamp. Yet few critics seem to understand that authorizations are not outlays; they are only commitments to spend money. Authorizations can decrease enormously while outlays are increasing and vice versa. The two are only marginally related.

From 1937 through 1973 federal housing programs focused almost entirely on housing construction. When Congress authorizes a new unit of public housing, it includes all the funds that will be used to pay off a 40-year mortgage. Nonetheless, the total amount is credited to the year in which the unit is authorized. Such authorizations tend to create the impression that large sums are to be spent on housing immediately when in fact that may not be the case.

Under Section 8 of the Housing and Community Development Act of 1974, Congress created housing certificates that obligate the government to subsidize the rental of private apartments for 15 years. That system allowed Congress to cut back on housing authorizations--not because less money was being spent on housing but because money was being committed for a shorter period.

Fifteen years turned out to be a long time for a tenant to stay in one place, so Section 8 construction and rehabilitation certificates have been awarded to landlords and developers rather than tenants. They have also been handed out in blocks, a practice that virtually assures the success of a project. That is why Section 8 certificates have become such coveted possessions and have been fought over so ferociously.

Finally, in 1984, Congress implemented the Reagan administration's plan to create five-year vouchers that are awarded to tenants and remain in force if they move. That triggered a shift from provider-oriented programs to a recipient-oriented program. The voucher program has expanded rapidly--and would have expanded even more rapidly if Congress had not remained wary and cut the housing authorizations requested by the Reagan administration in half every year. Vouchers have become the centerpiece of HUD's low-income housing assistance.

Like the shift from 40-year mortgage subsidies to 15- year housing certificates, the shift from the certificates to 5-year vouchers enabled Congress to reduce HUD's budget authorizations. Such reductions have created the mistaken impression that federal housing assistance has been cut. In fact, annual outlays increased from $5.7 billion in 1980 to $13.8 billion in 1988. The number of families being served by HUD housing programs rose from 3.1 million in 1980 to 4.2 million in 1988. Moreover, a housing voucher costs the government only about $4,500 a year, whereas a new unit of public housing costs it $9,000 a year.

Public Housing

The second count in the indictment of Reagan-era federal housing policies charges that the number of new public housing units authorized plummeted during the past 10 years. The figures certainly back up that contention. (See Table 1.)

Table 1 Units of Public Housing Authorized	
Year	Units Authorized
1977	31,764
1978	56,245
1979	54,914
1980	36,677
1981	35,921
1982	12,099
1983	2,740
1984	0
1985	7,312
1986	5,314
1987	9,801
1988	7,000

Source: Department of Housing and Urban Development.

Considering the Reagan administration's vow to get the government out of housing construction, that decrease is not surprising. What invalidates the argument that it caused homelessness to rise is, once again, that authorizations are not outlays.

In fact, it generally takes four to eight years for a new unit of public housing to come on line. Some authorizations dating from the Ford administration are still in the pipeline. Even though the number of units authorized fell sharply during the past decade, the 1980s were actually boom years for public housing construction, as previously authorized units came on line. (See Table 2.)

Table 2 Units of Public Housing Constructed	
Year	Units Constructed
1977	5,192
1978	10,134
1979	10,763
1980	15,109
1981	32,485
1982	27,611
1983	27,041
1984	24,058
1985	19,093
1986	14,867
1987	10,415

1988	9,146

Source: Department of Housing and Urban Development.

The Scandals at HUD

Finally, there is the charge that federal housing funds were misappropriated. Two kinds of misappropriations are said to have occurred. First, it is alleged that private contractors who sold houses insured by the Federal Housing Administration pocketed between $2 billion and $4 billion instead of returning it to HUD when FHA foreclosed on the mortgages--a dead loss for the Treasury. If nothing else, the disappearance of such a huge sum, virtually unnoticed, illustrates what a vast, sprawling bureaucracy HUD has become.

Second, it is alleged that Deborah Gore Dean, who was executive assistant to the secretary of HUD and administered the discretionary fund of the Section 8 moderate-rehabilitation loan program, lent money to favored Republican developers to finance the renovation of homes for middle-class people, not poor people.

If those allegations are true, they merely illuminate longstanding failings of federal housing policies. The use of Section 8 money as a slush fund is not new. Section 8 was the principal fundraising tool in President Jimmy Carter's 1980 reelection campaign. A Carter contributor in Chicago received 35 HUD grants. Seventy percent of Carter's Massachusetts campaign contributions came from Section 8 developers, who received 90 percent of the state's Section 8 grants the following year.

Likewise, the programs established under Sections 235 and 236 of the Housing Act of 1968 also caused subsidies to drift up to the middle class. Housing certificates, issued in Section 8 programs, were supposed to solve that problem, but it was precisely because the construction program and the rehabilitation programs were still being abused that the Reagan administration eliminated the former and tried to eliminate the latter.

In fact, perhaps the best way to gain some perspective on the current situation is to consider how the Section 8 programs came about in the first place.

Housing in the Great Society

By 1968 there was widespread dissatisfaction with the urban renewal programs established under Title I of the Housing Act of 1949 and the public housing programs established under the Housing Act of 1937, which had resulted in "vertical slums" and a variety of social problems. Accordingly, President Lyndon Johnson sought to help poor people buy homes and find affordable apartments by means of a public-private partnership in the provision of housing. The programs established under Sections 235 and 236 of the Housing Act of 1968 were intended to accomplish that objective.

Under Section 235, FHA, which had confined its mortgage- insurance operations almost entirely to the suburbs, was urged to serve inner-city residents as well. Investors were encouraged to build or renovate houses and sell them to low-income families, who would have FHA-guaranteed mortgages.

Under Section 236, nonprofit organizations and professional developers were given incentives to construct apartment buildings and rent some of the units to poor elderly people and low-income families. (The professional developers were to operate on limited profits.) An investor would pay only 1 percent of the interest on a 30-year mortgage, and the federal government would subsidize the rest of the interest. In addition, the tax laws were revised so as to make Section 236 investors eligible for accelerated depreciation write-offs.

Johnson envisioned the creation of 600,000 units of housing for the poor in each of the next 10 years--even though the rate had never exceeded 40,000 units a year. With typical bravado, he called the 1968 act "the Magna Charta of housing." To everyone's great surprise, Johnson's Republican successor, President Richard Nixon, did his best to meet that goal. During Nixon's first four years in office 1.3 million units were created. Yet by early 1973 the programs established under both Section 235 and Section 236 were in disgrace.

The Section 235 fraud is generally considered the biggest scandal in housing history. Fast-buck artists bought decaying inner-city houses, gave them paint jobs, and sold them to urban homesteaders at inflated prices. The FHA officials who approved such deals often received kickbacks from the sellers. Within a few years most of the houses started to fall apart--heating systems collapsed, water pipes burst, electrical wiring burned out. Unacquainted with the obligations of home ownership, the buyers sometimes went to their banks and demanded repairs. Finally, facing thousands of dollars' worth of repair bills, many of them abandoned their homes, leaving FHA holding the bag.

By 1973, 20 percent of the mortgages issued under Section 235 had gone into default. Moreover, 26 percent of the new and renovated homes were judged unfit for sale. Finally, it had been established that only 13 percent of the people who had bought homes were poor. The subsidies had somehow drifted up to the middle class. The construction and renovation programs were quickly halted, but their eventual cost to the government was about $2 billion.

The Section 236 program met a similar fate, primarily because its architects were woefully ignorant of the economics of real estate. The chief attraction of a real estate investment is its long-term value. A well-constructed building can reasonably be expected to last for about 75 years and will appreciate in value for most of that period. That is why banks are willing to write long-term mortgages. By keying housing investments to accelerated depreciation write-offs, however, Section 236 shortened the lifetime of an investor's stake to 5 to 10 years, which by real estate standards is not a very long time. When a Section 236 project began to run into management and maintenance problems, the owner--having already taken most of his depreciation write-off-- would often bail out, leaving FHA holding the bag once again.

Section 236 also became infamous for the failure rates of nonprofit organizations, often held to be the salvation of the nation's housing problem. A phenomenal 65 percent of the low-income-family projects and 33 percent of the poor-senior-citizen projects run by nonprofit groups went bankrupt. Professional developers also failed, at rates of 31 percent and 7 percent--still high compared with their rate of 2 percent when operating on unlimited profits. In addition, studies indicated that only 43 percent of the tenants of Section 236 projects were poor. The program was abolished in 1974.

By 1973 virtually every federal housing program had proved to be seriously flawed. Public housing projects had shown an unfortunate tendency to concentrate low-income members of minority groups, thus magnifying social pathologies. In the 1950s and the 1960s, when public housing authorities started to build high-rise projects--for perfectly sensible economic reasons--things got even worse. Such projects tended to become instant ghettos, headquarters for violent crime and drug traffic.

Section 235 and Section 236 had been designed to solve those problems. Yet by 1973 it was obvious that they had failed as well. Something else had to be done. Within the space of eight months in 1972-73 three leading scholars published incisive critiques of federal housing programs for the poor.(1) All three authors recommended that housing construction and renovation be replaced by a rent certificate program encompassing all low-income families. One of the experts, Richard Muth, argued that allowing such certificates to be spent on both privately and publicly produced housing would avoid much of the waste inherent in the production of public housing, substantially increase the average benefit per family, and widen the housing choices available to poor families.

Section 8 Certificates

Congress, sobered by the scandals of Sections 235 and 236, decided to follow that advice. In January 1973 President Nixon made the decision easier by suspending all federal housing programs through an impoundment of funds that was upheld by the courts. He told Congress to come up with a more workable plan. Even as the Nixon administration disintegrated in the throes of Watergate, Congress was being forced to rethink its approach to housing issues. The result was the Housing and Community Development Act of 1974, signed by President Gerald Ford three days after he took office.

Under Section 8 of the act, Congress created a mechanism that may seem to resemble a housing voucher but is actually very much like the old construction subsidies: a housing certificate that covers the difference between a tenant's rent and 25 percent of his monthly income for 15 years. Although such a certificate is awarded to the tenant, he has very little latitude in using it. Government officials have to approve his apartment. If it does not meet their standards, either the landlord has to make repairs or the tenant has to move. Otherwise he is no longer eligible for a certificate.

Section 8 established three programs: existing housing, construction, and substantial rehabilitation. A fourth program, moderate rehabilitation, was added in 1978. In the existing-housing program, tenants received the certificates and could apply them to the rent on their current apartments (if approved by the government) or apartments to which they moved. In the construction and rehabilitation programs, however, large blocks of housing certificates were often given to developers and renovators in order to encourage housing investment. Such an investor would then assemble tenants (usually with the help of a public housing authority) to live in the new or renovated building.

Thus, the Section 8 construction and rehabilitation programs differed very little from what had gone before. The 15-year housing certificates simply replaced the mortgage subsidies established under Section 236. When the Reagan administration came into office in 1980, it found that the government was already committed to $250 billion worth of construction under Section 8 and public housing authorizations.

Ironically, while those commitments were piling up, housing analysts were beginning to question whether any new construction (aside from the construction in the private sector) was really required to meet the nation's housing needs.

In 1937, when the first public housing program was established, tenements and slums still loomed large in the public's consciousness. For generations housing reformers called for building codes that would set higher standards for new housing and provide a legal justification for tearing down the old. That campaign culminated in the urban renewal of the 1950s and the 1960s, an attempt to demolish whole neighborhoods in the hope that something better would rise in their place.

Urban renewal soon proved to have its own difficulties, including a tendency to force minorities out of their homes without offering them anything in return. By the 1970s, however, a boom in suburban housing construction had completely changed the urban market. Many cities had acquired a surplus of housing. Instead of overcrowded slums, urban blight--the decay and abandonment of sound housing--was the problem. Given those conditions, the construction of public housing was far less important than the maintenance of existing housing.

That evaluation was confirmed in a report issued by the President's Commission on Housing in 1982. Of the six million tenants paying more than 35 percent of their incomes in rent, the report found, only two million were living in substandard housing. The report concluded that instead of building more public housing, the government should compensate for low tenant income by providing income supplements in the form of housing vouchers.

As a result of such recommendations, the Reagan administration eliminated the Section 8 construction program and even tried to rescind some of the construction certificates that had already been issued. It also tried to eliminate the Section 8 substantial- and moderate-rehabilitation programs. When Congress blocked that attempt, the administration expanded the existing-housing program instead.

The Voucher Program

In 1984 the Reagan administration persuaded Congress to introduce the far more flexible five-year voucher. By 1988 there were 221,000 vouchers in circulation, and each year the administration had asked Congress to authorize 100,000 more (although Congress had regularly trimmed the authorization to 50,000).

One of the most notable results of the transition to vouchers is that federal housing subsidies are now targeted to the poor better than ever before. In 1974 only 16 percent of the households receiving federal housing assistance had incomes under $5,000 (in 1987 dollars), whereas 6 percent of the households being assisted had incomes between $20,000 and $25,000. By 1987 the percentage of recipients in the lowest income category had nearly doubled, while the percentage of recipients in the higher income category had been cut in half. (The 1987 figures were 31 percent and 3 percent.) A longtime failing of federal housing programs--assisting the wrong people--has nearly been eliminated.

Vouchers have other advantages as well. Unlike public housing subsidies, they do not create ghettos for poor people and minorities; recipients can spend them anywhere. Moreover, vouchers allow housing assistance providers to avoid the often-arduous task of siting public housing projects in the face of community opposition.

Such resistance can have extremely inequitable results. Los Angeles, for example, has very little public housing because a California law requires that a public referendum be held to approve proposed sites. Yet Yonkers, New York, which had built thousands of public housing units, was sued by the Justice Department because it hadn't sited any of them in middle-class neighborhoods. With vouchers, low-income families are far less likely to encounter opposition to their presence and can obtain better housing in better neighborhoods.

Perhaps most important, low-income families have been stating that they would rather receive vouchers than be placed in public housing projects, according to housing assistance providers. Yet even in the face of such evidence, the press --convinced that it knows more about the poor than the poor know about themselves--has continued to plug public housing. In September 1989, after the San Jose Public Housing Authority reported that applicants were turning down public housing in favor of vouchers, the San Jose Mercury News editorialized that

> while rare in county projects, crime problems are more common at market-rate apartment complexes. So the folks taking vouchers are more likely to end up with a drug-dealing neighbor, and less likely to find a landlord willing to help. . . .
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> [San Jose projects are] not perfect, but they're better-than-average rental housing. . . . For most prospective elderly tenants, they're a much safer deal than a voucher.(2)

Thus, the biggest housing story of the 1980s--aside from homelessness itself--is the successful transition from the old construction subsidies to the more flexible and equitable vouchers. But the press, wedded to the old ways, has either ignored that accomplishment or denigrated it.

In the light of Section 8's origins, it is easy to see that the HUD scandals, although satisfying melodrama, are nothing more than a reprise of the scandals that always occurred when federal programs awarded subsidies to housing providers rather than tenants. Political connections, payoffs, campaign contributions--all have long helped direct housing funds to the right people. James Watt, Carla Hills, former senator George Murphy, and the late John Mitchell (none of whom got any money from the Treasury) were only playing the very old game of steering federal housing subsidies toward favored developers.

If there is a lesson to be learned from the Section 8 scandals, it is that the old construction programs were not phased out quickly enough.

The Real Housing Crisis

If government spending cuts and federal housing programs are not to blame, then, what has caused the housing crisis? And does such a crisis really exist? There indeed seems to be a housing crisis, but it takes different forms in dif- ferent parts of the United States. Consider the following:

> -- In Detroit, abandoned buildings have become a major housing problem. Two nights before Halloween Detroit youngsters celebrate Devil's Night, when dozens of abandoned wood- frame buildings are burned to the ground. In the early 1980s, when the city lost tens of thousands of jobs, FHA found itself holding 17,000 foreclosed mortgages on Detroit homes. It was able to reduce its inventory only by demolishing many of the buildings. Empty houses have proved to create a social problem as well; they serve as convenient headquarters for drug dealers.
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> -- San Francisco's apartment vacancy rate has descended to a microscopic 1.8 percent, the lowest rate in the United States. A "tent city" for homeless people was set up in the Tenderloin district, and every night 175 people sleep in Civic Center Plaza. The homeless population, estimated at 6,000, is one of the largest in the nation. San Francisco has had rent control since 1979. The antidevelopment ethos is so strong that the city allows the equivalent of only one office building to be constructed each year. In 1989, when he announced a $16 million master plan for dealing with homelessness, Mayor Art Agnos said that the problem was caused by federal budget cuts.

> -- Houston's freedom from zoning and other municipal regulations has set off the biggest apartment construction boom in the nation. Combined with a collapse in oil prices, it has produced a vacancy rate of nearly 20 percent. One of the losers was George Bush, whose investment in a "troubled Houston apartment complex" was mentioned several times during the 1988 presidential campaign. Meanwhile, tenants have enjoyed a renters' market. Desperate landlords regularly offer two months of free rent in an attempt to get tenants' names on one-year leases. Luxury apartments rent for $350 a month.
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> -- In 1987 alone there were 24 no-growth referendums on municipal ballots in California, 20 of which were passed. After the 1988 elections proponents of no growth started to plan a statewide strategy. Some California residents have been too restless to wait. In Redwood City, south of San Francisco, vigilantes burned down the single-family homes under construction at 20 sites, causing $2 million worth of damage, shortly after the city council lifted a two-year building moratorium. Home prices in California, which were at the national median in 1970, have risen to almost twice that figure since then.
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> -- When the recession of the early 1980s pushed San Diego's vacancy rate down to 4 percent, housing activists put rent control on the ballot. For the second time in eight years San Diego voters turned it down, by a resounding 2 to 1 margin. Developers responded by launching an apartment construction boom that within two years had pushed the vacancy rate back up to more than 6 percent and raised the rate of vacancies in inexpensive apartments from 1.8 percent to 3.3 percent. The city also reinterpreted its zoning ordinance to permit the operation of hotels made up of "living units," each of which was to consist of a single room with a shared bath or kitchen. Developers responded by building six of the newly authorized hotels, significantly reducing homelessness. "I'd say the most important thing we've done in providing housing for the poor is to not alienate the development community," said Frank Landerville, director of the Regional Task Force on the Homeless. "Builders are still enthusiastic about San Diego, and that provides housing at all income levels." As a result, the city's rate of homelessness has been one of the lowest in California.
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> -- In New York, where the housing market has been tight for almost 50 years, rioting broke out when police officers tried to evict homeless people from Tompkins Square Park on the Lower East Side. New York's rental vacancy rate has hovered around 2 percent for two decades. During that period the city has lost almost 400,000 apartments to abandonment-- enough to house nearly a million tenants. Homeless people have virtually taken over railroad and bus terminals and often line the streets three and four deep, begging for money. In 1987 Mayor Edward Koch announced a $4.5 billion plan to create 252,000 units of city-financed housing, half of which would be reserved for people with low incomes and nearly all of which would be located in buildings that the city had confiscated from private landlords.

It is obvious that housing markets have varied widely from city to city. Some cities have been plagued by high abandonment rates and high vacancy rates. Other cities have had little abandonment and extremely low vacancy rates--and have scrambled to find every available space. Still other cities, particularly New York, have had high abandonment rates and low vacancy rates.

It is also obvious that the undesirable conditions in such vastly different housing markets have not resulted from federal actions. They have varied according to the housing policies pursued by local governments. The housing crisis is not a national phenomenon. It is a local problem brought about by local regulations.

Local regulatory ordinances generally fall into two categories: zoning and rent control. Let us see how each of them has affected housing markets.

Zoning

Zoning was first used in New York City in 1915, to keep the garment district from spreading into uptown residential areas. It has since become one of the most widely practiced forms of market intervention. As Richard Babcock noted in 1966,

> No one is enthusiastic about zoning but the people. . . . The judges find zoning a monumental bore, most

> lawyers consider it a nuisance, and the planners treat it as a cretinous member of the planning family. . . . Yet thousands of officials regard zoning as the greatest municipal achievement since the perfection of public sanitary systems. . . . By the test of acceptance in the marketplace, zoning has been a smashing success.(3)

Among the professed goals of those who advocate zoning are planning for future development, separating incompatible uses, and clustering compatible uses. Yet anyone who has attended a meeting of a municipal zoning board knows that there is really only one motivation for zoning: keeping out development that people don't want.

Apartment complexes, factories, stores, schools, churches-- almost every imaginable land use is likely to be opposed by people who live in the vicinity on the grounds that it will generate traffic, affect the quality of life, and change the character of the neighborhood. Even new single-family homes-- once the signature of suburbia--have increasingly come under attack. One of the most common confrontations occurs when a developer subdivides property and constructs tract homes in stages; people who buy in Stage I immediately start opposing the construction of Stage II homes.

Such opposition is generally motivated by economic considerations. Having invested what often amounts to a major portion of his life savings, a home owner wants to protect the value of that investment. He can do so by keeping undesirable uses at a distance. Because a home's value is largely dependent on its seclusion and its environmental amenities, most home owners don't want to see another subdivision going up next door either. Enter zoning, which gives people control over other people's property. Exclusionary zoning appeals to most home owners because it has a desirable result: it causes the value of their homes to appreciate rather than decline. They tend to interpret that outcome as virtue rewarded.

The losers in the zoning game are those who cannot participate--outsiders, low-income residents, potential residents. Although they are unorganized and have no say in zoning discussions, they will suffer when housing prices are driven up, often beyond their means. Members of those groups do have one proxy, however, who represents their interests during such discussions: the developer. That is why developers are hated in all suburban communities.

That zoning is not necessary for any purpose other than to shut out unwanted development can be seen from the experience of Houston, the nation's sixth-largest city. Houston has no zoning, yet none of the catastrophes predicted by zoning proponents have occurred there. Gas stations have not invaded residential neighborhoods, factories have not set up shop across from schools, and home owners have not opened barbershops in their living rooms. Houston has as many exclusive residential neighborhoods as any other city in the nation.

The reason is that private covenants and restrictions have essentially replaced zoning in Houston. A developer of a suburban subdivision will issue deed restrictions specifying that the parcels of land in that subdivision cannot be used for anything except single-family homes. If he does not, banks will not lend him money. That practice protects residential neighborhoods in Houston as much as zoning does elsewhere.

The difference is that Houston residents cannot restrict the use of property on the next block or halfway across town. As a result, builders are able to create a mixture of residential, commercial, and industrial development. Condominium complexes are so common in Houston that their prices start at about $40,000. New apartments are everywhere. In fact, realtors have complained that the city has an investor-led market and that developers are building there not because they are responding to a demand for new housing but because it is so much easier to build there than anywhere else. Whatever the cause, housing in Houston is extremely affordable and homelessness only a minor problem.

During the 1960s and the 1970s social critics kept up a drumbeat of salvos against zoning, largely because they perceived it as a means of excluding minorities. That analysis is somewhat incorrect; the rationale for zoning is primarily economic.

During the 1970s residents of suburbia, apparently in response to that criticism, embraced environmentalism. When the focus of the debate shifted from discriminating against minorities and the poor to protecting trees and other natural resources, some critics of zoning seem to have been silenced --or even converted to enthusiastic supporters. As late as 1973 Anthony Downs of the Brookings Institution argued that black ghettos could be eliminated by breaking down zoning barriers and thus dispersing a city's poor black population into middle-class neighborhoods.(4) By 1979 Bernard Frieden had pointed out that residents of suburbia were not trying to exclude blacks alone; they were trying to exclude everyone. In its bland, small-scale applications, Frieden noted, environmentalism had become a "ready rationale for the defense of privilege"; suburban communities were justifying no-growth policies on environmental grounds.(5)

Still, the view that no growth is a benign or even desirable suburban phenomenon seems to have carried the day. Moreover, although concern over homelessness has grown ever more acute over the past decade, no one has attributed it to zoning and no-growth policies. Instead, people have blamed Washington.

Rent Control

Rent control, the second category into which local regulatory ordinances fall, is another market intervention that benefits established residents of a community while imposing penalties on newcomers, outsiders, and potential residents. Rent control plays a surprisingly large role in the nation's housing affairs, essentially dominating the markets on the East and West coasts. The reason rent control receives so little national attention and is rarely recognized as a prevalent pattern is that it is almost always perceived as a local issue.

Rent control, of course, is a pure price control. It is axiomatic among economists that price controls produce commodity shortages. As Assar Lindbeck, chairman of the Nobel economics committee and an avowed socialist, warned the American New Left in 1971,

The effects of rent control have in fact been exactly what can be predicted from the simplest type of supply-and-demand analysis--"housing shortage" (excess demand for housing), black markets, privileges for those who happen to have a contract for a rent-controlled apartment, nepotism in the distribution of the available apartments, difficulties in getting apartments for families with children, and, in many places, deterioration of the housing stock. In fact, next to bombing, rent control seems in many cases to be the most efficient technique so far known for destroying cities, as the housing situation in New York City demonstrates.(6)

Over 200 American municipalities have rent control. More than half of them are small communities in northern New Jersey, which significantly affects the already-overregulated New York metropolitan area. Most of the large suburbs of New York City, including Yonkers, White Plains, New Rochelle, Garden City, and Mt. Vernon, have rent control. Such principal New Jersey cities as Newark, Paterson, and Jersey City also have rent control.

Boston, Brookline, and Cambridge, Massachusetts, have rent control, as do Hartford and several smaller Connecticut cities. Washington, D.C., has it, as does Takoma Park, Maryland, a 19th-century suburb just beyond the District of Columbia's border.

Los Angeles, San Francisco, Oakland, and San Jose as well as Berkeley, Santa Monica, West Hollywood, Palm Springs, and several other small California cities have rent control. San Diego and Sacramento are the only major cities that have rejected it.

Remarkably, in 1984 every American city with rent control had a vacancy rate of less than 3 percent, whereas every American city without rent control except Worcester, Massachusetts, had a vacancy rate of more than 4 percent.(7) Apologists for rent control argue that the vacancy rates were already low when it was imposed, but census results indicate that Boston, Washington, Newark, Los Angeles, and San Francisco all had much higher rates in 1970.

In fact, housing shortages were not an issue during the 1970s, when rent control was imposed. The principal purpose of such legislation was to control inflation. Boston, Washington, and Newark acquired rent control by extending President Nixon's general wage-and-price freeze of 1971. California cities adopted it in the late 1970s, after Howard Jarvis promised tenants a rebate from Proposition 13; when the rebate didn't materialize, a statewide rent control movement developed. More than half of California's population now lives under rent control.

Economists' routine prediction that rent control would produce housing shortages, then, has been borne out by the low vacancy rates in rent-controlled housing markets. What has not been generally recognized, however, is that a large percentage of a tenant population--perhaps even a majority-- can reap considerable long-range benefits from rent control. In fact, a tenant who is willing to stay put, even as living conditions deteriorate, can obtain what amounts to a lifetime annuity. Many New York City tenants with modest incomes are able to buy homes in the country, do part-time work, or pursue artistic avocations because they have rent-controlled apartments. Only when tenants move do they experience the adverse consequences of rent control. Until then the problems are diverted to newcomers, outsiders, and minorities.

The reason is once again the long life expectancy of housing. As Ludwig von Mises pointed out, every form of socialism is capital consumption. In the case of housing, however, there is a great deal of capital to be consumed. A community's housing stock usually represents its principal capital investment. As a result, tenants living in a well- built apartment house can pay below-market rents for as long as 30 years before the building begins to fall down around their ears.

When price controls are placed on a relatively short- lived commodity such as gasoline, the ensuing shortages are evenly distributed. Such shortages result in general dissatisfaction and may even produce pressure for deregulation. But rent-controlled apartments can be consumed by the same people for decades. Tenants who are protected by strong leases-- almost always an adjunct of rent control--can achieve virtual lifetime immunity from market forces.

On the other hand, tenants who were outside the market when rent control was imposed and tenants whose apartments are not covered by the rent control regulations do much worse. In practice, rent control is rarely imposed on all apartments. Instead, the government leaves a "hole in the market" through which excess demand can escape. Ironically, the rents of apartments in the deregulated sector will rise higher than they would if rent control laws were not in effect. (Imported oil was the hole in the market through which Americans' excess demand for oil escaped, and U.S. price controls raised world oil prices to unsurpassed levels.)

Under rent control, the deregulated sector is likely to include small buildings whose mom-and-pop owners are not regarded as "real" landlords. Many cities also practice vacancy decontrol, which usually consists of allowing apartments to reach market value the first time they are vacated, then reregulating their rents. Other cities exempt new construction, although they are often forced to repeal that exemption when tenants of new buildings become a powerful political faction.

Such exemptions create a secondary market in which prices are higher than they would be if rent control laws were not on the books. Supplementing the secondary market is a black market in which regulated apartments change hands by means of "key money" and other bribes. Anyone who tries to break into the primary market or move from apartment to apartment is funneled into those submarkets and ends up paying higher- than-market prices.

As a result, under rent control a transfer of income from one tenant to another is just as likely as a transfer of income from landlord to tenant. A 1985 study of the Los Angeles rental market found that while longtime tenants of rent-controlled apartments were paying about $18 a month less than tenants of comparable unregulated apartments in neighboring communities, relatively new tenants of rent-controlled apartments were paying $15 a month more. The study concluded that the biggest transfers of income were from tenants who moved frequently to those who stayed put.(8)

Because so many people are disadvantaged by rent control, it might appear that the losers could be mobilized into a constituency for its repeal. Unfortunately, they are more likely to argue that the regulations should be extended to include them as well. That argument is also likely to prevail. San Francisco eventually abolished vacancy decontrol. Toronto exempted new construction when it established rent control in 1975, but the gap between the haves and the have-nots became so wide that the city repealed the exemption, recapturing thousands of apartments for regulation. In New York, the tides of regulation, deregulation, and reregulation have ebbed and flowed so many times that the current housing laws are almost incomprehensible to everyone except the most practiced specialists. New York now has two different forms of rent control plus ordinances covering a bewildering variety of special cases.

The regulation of rents, of course, is a blatant violation of property rights. Moreover, as Downs pointed out, rent controls would be unconstitutional even if they were benefiting only the poor and hurting only the rich (which is clearly not the case).

Presumably, rent controls are adopted to serve a basic public purpose: the protection of tenants from experiencing unfair rent increases. . . .

> However, as a general principle, it is undesirable for government to protect one private group against undue injury attributable to circumstances beyond its control by forcing another private group to transfer resources to the first one. If protection is indeed in the public interest, taxpayers should pay for such protection through normal means of taxation. Reliance on rent controls comes perilously close to--and may even amount to--a government taking of one group's resources to aid another group, without compensating the first group.(9)

In sum, there can be very little doubt about where the housing crisis originates--it is a function of local, not national, politics. If General Motors had to negotiate with every municipal planning board in the nation to get permission to sell automobiles in that municipality, we would be experiencing a car shortage as well as a shortage of affordable housing.

That anything can be done about the housing crisis is far more dubious. There is very little hope of reform at the municipal level. No city is likely to give up its zoning powers voluntarily; in fact, most of the "reform" movements are striving to increase those powers. Municipal officials are constantly accused of "selling out" to developers by failing to keep zoning tight enough. Neither is there a real constituency for abandoning rent control. For that reason, any change that occurs will probably originate at the state or federal level.

Those who have long preached about the evils of federal intervention may be reluctant to argue that the federal government should start overriding local governments' housing regulations. Moreover, any attempt to abolish rent control in a city such as New York would probably be met with the same kind of massive public resistance that accompanied school desegregation in the South.

The courts, an apparent alternative, have been tried many times. There have been several omnibus antizoning suits and a few attempts to chip away at rent control. All have failed. In its last major zoning decision, in 1974, the Supreme Court ruled that a town's zoning ordinance could forbid three or more unrelated people from renting a single- family home. The majority opinion was written by Justice William O. Douglas, who was joined by Chief Justice Warren Burger.

Nor does a successful antizoning case at the state level offer much cause for optimism. In the well-known Mt. Laurel decision, the New Jersey Supreme Court ruled that the state had the power to override a town's zoning barriers to provide more low-income housing. Instead of basing that decision on property rights, however, the court based it on the state's ownership of "all the land." Although the decision required residents of New Jersey communities to accept their "fair share" of low-income housing, the judge went out of his way to assure them that developers would not be given free rein. In practice, the Mt. Laurel decision has produced little more than a smattering of "affordable," builder-subsidized units, which have quickly been snapped up by young couples, single mothers, municipal employees, and other groups that are given special preference or have inside information. It has done very little to help the poor or even expand the housing market.

Hence, there is no assurance that anyone would be very anxious to solve the housing problem even if it was convincingly identified as a local issue. Exclusionary zoning is not being practiced because politicians are corrupt or because the public is being misled. It is being practiced because it is exactly what the vast majority wants. As noted earlier, the benefits of zoning are reaped by established residents of a community, while the adversities are shunted onto newcomers, outsiders, and minorities. A community can go on zoning out development for decades and the majority will barely feel the consequences.

It can also take decades for large numbers of people to experience the adverse consequences of rent control--although that is now on the verge of happening in New York City. A community with rent control can essentially go on subsidizing tenants until their buildings start to fall apart.

Thus, one can legitimately ask, Is there any hope of solving the housing problem? Strangely enough, the debate touched off by the Housing Now! march on Washington may offer an opportunity to start doing so. Now that concerned citizens have been willing to bring the issue to the nation's capital, perhaps it will finally be discussed honestly there.

Rent control is obviously ripe for a national debate. Most of its benefits are bestowed on the middle class, and it allows cities to wall themselves off and become virtually impenetrable to outsiders. In a recent study issued by the Manhattan Institute, Peter Salins and Gerard Mildner argued that the whole nation is suffering because cities on the East and West coasts restricted their housing markets while their job markets were expanding. Salins and Mildner suggested that community development block grants be awarded only to cities that had submitted plans for phasing out rent control.(10) (Paris and London are getting rid of their much older rent control systems in order to join a unified Europe.)

The National Affordable Housing Act, sponsored by Sens. Alan Cranston (D-Calif.) and Alfonse M. D'Amato (R-N.Y.), may offer another opportunity to start solving the housing problem. Although it contains a wrong-headed proposal to lower the down payments on FHA mortgages (thereby further endangering that already-troubled agency), the bill would require cities applying for Housing Opportunity Program funds to "list all policies that affect return on residential investment" and "provide a plan for eliminating the negative effects of those policies"--which would generally mean getting rid of rent control.

Similar provisions could serve to discourage exclusionary zoning. Very few, if any, communities could be induced to follow Houston's example and give up zoning completely, but such destructive practices as declaring construction moratoriums and prohibiting multifamily occupancy could be curbed.

Finally, it seems at least remotely possible that people of good will in every community may eventually be brought to the realization that solving the housing problem requires something far more difficult than just complaining about federal policies or sending angry demonstrators to Washington. It means making the most difficult adjustment of all: accepting change in their own back yards.

Footnotes

(1) Anthony Downs, Federal Housing Subsidies: Are They Working? (Lexington, Mass.: Lexington Books, 1972); Henry J. Aaron, Shelters and Subsidies: Who Benefits from Housing Policies? (Washington: Brookings Institution, 1972); and Richard Muth, Public Housing: An Economic Evaluation (Washington: American Enterprise Institute, 1973).

(2) "A Housing Deal," San Jose Mercury News, September 11, 1989.

(3) Richard Babcock, The Zoning Game (Madison: University of Wisconsin Press, 1966), p. 3.

(4) Anthony Downs, Opening Up the Suburbs (New Haven: Yale University Press, 1973).

(5) Bernard Frieden, The Environmental Protection Hustle (Cambridge: MIT Press, 1979).

(6) Assar Lindbeck, The Political Economy of the New Left: An Outsider's View, 2d ed. (New York: Harper & Row, 1977), p. 39. Emphasis added.

(7) William Tucker, "Where Do the Homeless Come From?" National Review, September 25, 1987, p. 35.

(8) Hamilton, Rabinovitz, Szanton, & Alschuler, Inc., and the Urban Institute, "Rental Housing Study: The Rent Stabilization System--Impacts and Alternatives" (report to the City of Los Angeles, Rent Stabilization Division, 1985), exhibit 2-12 following p. 32.

(9) Anthony Downs, Residential Rent Controls: An Analysis (Washington: Urban Land Institute, 1988), pp. 23-24.

(10) Peter D. Salins and Gerard C. S. Mildner, "A Proposal to Expand Housing and Economic Opportunities by Deregulating America's Rental Housing" (Manhattan Institute, New York, 1989), pp. 8-9.