

# Statewide Rent Controls: Preliminary Considerations

Philip Adams

Nishant Aggarwal

Pablo Balsinde

Shuwen Fang

Michael Wiley

Anna Wu

*for future work with the Lift  
the Ban Coalition*

02/04/2018

— the —  
PaulDouglas  
— institute —

[www.pauldouglasinstitute.org](http://www.pauldouglasinstitute.org)

## THE PAUL DOUGLAS INSTITUTE MISSION STATEMENT

The Paul Douglas Institute is a student-run, public policy think tank based at the University of Chicago. Inspired by the life and work of professor and Senator Paul H. Douglas, we channel public policy interest on campus into solution-orientated research projects that allow students to make an impact on the legislative process. To this end, we use a multidisciplinary approach to produce rigorous, data-driven social science research that is innovative, practical, and free from political affiliation. We often work with legislators and civic organizations and are fully open to commissions and partnerships.

## TABLE OF CONTENTS

I. Introduction	4
II. Policy Recommendations	4
III. Rent Control Structure	5
IV. Applicability of Rent Control	6
V. Reserve Accounts	6
VI. Tax Credits	7
VII. Alternative Policies	8
VIII. Political Considerations	9
IX. References	10

## I. INTRODUCTION

Rent control policies have been illegal in Illinois since 1997, when they were banned at the state level by ALEC-sponsored legislation. With the rise of grassroots efforts such as the Lift the Ban Coalition, coupled with support by top 2018 gubernatorial candidates, some form of rent control in Illinois is likely in the future, whether this might be at the local or at the state level. What exactly these controls will look like—who they will affect, how they should be implemented—are the subject of this paper. It will also consider alternative solutions to affordability issues, including zoning practices. We hope that an objective and thoughtful examination of the options will foster a constructive debate, ultimately leading to the best possible policy for Illinois.

## II. POLICY RECOMMENDATIONS

In summarizing the arguments of this paper, we propose the following recommendations:

1. Consider rent control mechanisms beyond second generational ones (percentage increases above inflation).
2. Adapt population Tiers to secure that rent controls reach targeted communities.
3. Design reserve account requirements and waivers to better accommodate local and unit particularities.
4. Evaluate the feasibility of tax credits given the difficulty of assessing fair market returns and state budget constraints.
5. Consider complimentary policies to promote a fairer housing market, including affordable zoning requirements and cooperative housing financing initiatives.
6. Maintain the sovereignty of local municipalities in operating their own rent controls and its related intricacies.

### III. RENT CONTROL STRUCTURE

Under the current proposal, the rent control would be implemented in a relatively traditional way: by putting a percentage cap on rent increases on top of inflation (1% and 2% respectively on top of the Consumer Price Index for Tier 1 and Tier 2 households). There is little doubt this form of “second generation” rent stabilization is fairer to landlords than an absolute cap on rent, since by allowing for increasing rent we are allowing that companies earn a return on their investment and cover their increasing operating expenses (Gilderbloom and Markham 2008).

But some of the critiques one nevertheless often hears from anti-rent control advocates have to be taken seriously, since they are grounded in some truth. For example, it has been shown that second generation rent controls increase vacancies (Wilhelmsson et al. 2011) and significantly decrease capital investment and supply (Diamond et al. 2018) which leads to further price increases and welfare losses which would not have otherwise occurred without the rent control. Many argue that the societal gains from the preservation of communities are worth the economic inefficiencies, but how these societal gains are distributed needs to be clarified.

To start, it has been shown that the type of rent control in question increases segregation in housing (Glaeser 2003), and it is becoming increasingly clear that the economic benefits of these rent controls disproportionately go to wealthier tenants (Öst et al. 2014; Kattenberg and Hassink 2017). The communities that these controls target may receive some gains, but there are significant concerns that in doing so we may be perpetuating larger wealth inequalities.

Below, we discuss other measures that other jurisdictions have taken to make sure rent controls benefit the targeted communities. At the structural level, however, the most important trend has been the transition from rent controls to tenancy controls, in which a landlord can raise rent as he wishes if the apartment becomes vacant. Often called “third generation” rent controls (Arnott 2003), they constitute an improvement with respect to second generation controls, since they better long-term community members; though it is important to note that it will only do so if they contain provisions to protect current residents from being pushed out.

At the same time, despite their benefits, it has been shown that tenancy controls do not fix all of their predecessor’s shortcomings (Arnott and Shevyakhova 2014). Moreover, issues would arise with the reference year being that of legislative introduction. The legislative introduction base year would incentivize landlords to find new tenants with artificially shorter time horizons for currently decontrolled apartments and vacancies, such that they know they will have the capacity to raise rents in the future (Nagy 1997).

Because of these inefficiencies and unclear societal benefits, we call for a deep reconsideration of the rent control mechanism discussed at the beginning of this section. Instead of using decade-old mechanisms that discourage investment and perpetuate inequalities, we should consider new and innovative proposals to secure fair housing that go beyond a premium on top of inflation.

For example, the British organizer Generation Rent has proposed a rent control system where, instead of capping the amount landlords can raise rent, jurisdictions could charge increasing amounts of taxes on landlords to the extent they decide to increase the rent beyond a certain threshold (Generation Rent 2016). Another interesting idea is the creation of a secondary built-to-rent home market which would be completely attached to the CPI for long periods of time, such that landlord market power would vanish (Davies et al. 2017).

All of these are, at the very least, interesting and promising ideas, but they take time to explore and select, especially given the impact particularities of local real estate markets can have in the success of a given policy (Oertel 2016). What is clear, however, is that there are better options than the traditional second generation rent control; the question is which of these to choose.

## IV. APPLICABILITY OF RENT CONTROL

Placing an income limit on the applicability of the control is a good idea, and is in line with policies in other jurisdictions. However, as it is currently proposed, the statute leaves open opportunities for individuals who do not necessarily need rent protections to acquire them. Individuals who are wealthy but do not have an income greater than 60% or 120% of the Average Median Income would be eligible for rent protections under the current proposal.

Additionally, we feel that altering the threshold for the control based on household size should be considered. For example, an examination on the impact of family size on actual subsidy size in rent controlled properties in New York showed that there are increasing gains from a rent control with family size (Linneman 1987). It might be valuable to attempt to control for this effect through threshold adjustments based on family size, particularly given that AMI figures already exist on a household size basis.

Since one of the aims of this policy is to protect communities and prevent gentrification, another policy to consider is one similar to that of New York, where controlled leases require that the resident has been living in the apartment for a certain period or inherited the lease from a longtime resident. However, in the case of New York, this policy allows individuals with high incomes who have inherited controlled leases to benefit from rent protections, which is undesirable.

It is clear that Illinois' response to affordability issues should target low-income people. Because rent control is a policy that targets property, not people, it may not be the most efficient solution, especially when it comes to the issue of homelessness. It has been found that rigid rent control policies can increase both shelter and street populations (Grime 1996). Because rent regulation hinders investment and supply, homelessness increases as a result of a lack of available housing.

The question must be answered: who is this policy attempting to protect? It is not enough to strive for low-cost living. In designing the most effective policy, we have to understand who is affected and how.

## V. RESERVE ACCOUNTS

Reserve accounts are, in principle, a beneficial proposition. They ensure speedy repairs for tenants and save landlords from scrambling for cash during an emergency (LRE 2018). In areas with large populations or frequent natural disasters, they are often, quite literally, a life saver. In fact, Illinois already has in place a budget requirement for condominium associations. The Condominium Property Act states:

“All budgets adopted by a board of managers on or after July 1, 1990 shall provide for reasonable reserves for capital expenditures and deferred maintenance for repair or replacement of the common elements” (765 ILCS 605/ 2015).

As a result, we think the reserve accounts proposition, that the “Reserve account must be maintained for repairs and capital improvements of at least 10% of the increment after customary housing expenses (e.g. mortgage principal and interest, property tax, utilities)” is a thought in the right direction. That said, the proposition, as stated, is imperfect.

Firstly, we take issue with the 10% requirement. How exactly was that percentage decided? Policy should be

guided by rigorous theory and empirical evidence. We suggest that the capital reserve requirement be decided by taking into account the following factors: building financials, health, and operating factors. A building built in 1922 is likely to require more repairs than one built in 2012. As a result, a one-size-fit-all requirement does more harm than good, and therefore, building operators should be allowed to set a reserve amount depending on individual circumstances and needs, guided by an easily understandable equation (Dittmer 2015). A very crude equation would look something like this

$$CR = \theta F + \alpha A + \beta P$$

where,  $\theta$  and  $\alpha$  are weights placed on financials, age, and operating factors, such that  $\theta$  increases with the age of the building and so on.

Secondly, “repairs” and “capital improvements” are very different things. Repair refers to the act of improving something that was damaged, whereas capital improvement refers to improving something that is not damaged. It’s the difference of replacing a broken light bulb with a new one versus replacing a halogen light bulb with an LED one. We think reserve accounts should be maintained solely for repairs and emergencies, not capital “improvements” (NSM 2018). Whereas a capital reserve requirement for repairs ensures proper service to tenants and protects their rights to a good living environment, a capital reserve requirement for capital improvements breaches the rights of the landlord to modify, or not, his property at his will. This should be called a “repair” reserve, not a capital reserve (CPS 2018).

All in all, we think that the reserve requirements proposal is a step in the right direction. It is something that has already been implemented at certain levels for condominiums and such buildings, and therefore can be applied to a more general housing market. The idea simply needs to be fleshed out with more specific details, keeping in mind that it should benefit and respect both tenants and landlords.

We think there are two alternatives to this policy that are worth considering. Landlords could be allowed to raise the price of the housing unit by a certain percentage spent on maintenance every six months and thereby cover the costs, while also profiting in the long run.

Secondly, we think that an alternative policy in which landlords are given tax credits equivalent to the amount spent on maintenance would be a win-win approach, in that it would not make repair work raise housing prices and simultaneously incentivize landlords to make repairs. This ensures timely repairs, stable rents, and unburdened landlords. At the same time, we do think that this credit could be a major burden on the state budget (around \$460 million).

## VI. TAX CREDITS

If we assume that the goal is to provide equitable housing and ensure housing access, then tax credits are a good step in that they compensate landlords with the money they would have lost because of a rent control; all the while keeping housing prices affordable for tenants. Tax credits ensure low prices and fair compensation at the same time. There are already several examples of this, such as the Low Income Housing Tax Credits (OCC 2014). That said, a policy that relies on calculating the fair market rent that “would have been” in a world without a rent control policy works better in theory than in the real world. Instead of all agents being rational and there being no information asymmetries, several agents are acting in tandem against each other and often with limited (and sometimes privileged) access to information. All this leaving aside that home pricing models often assume housing quality to be a constant, and that housing quality itself is often measured using market prices (Kain and Quigley 1970).

As a result, we think attempting to find a fair return might be a misguided approach which might put the entire rent control policy at risk. We think it is possible to compensate large housing developers by waiving certain mandated fees and payments, such as property registration fees for future developments, because in this case the state simply gives up revenue gains as opposed to losing money (which would be beneficial because of loss aversion). At the same time, such a method would not work with owners of small housing units. It would be possible to apply this to small housing units by waiving, say, a speeding ticket of a landlord, but that opens a whole Pandora's box of social issues and legal ramifications. Subsidies are not an option, too, given the current Illinois budget crisis (Bosman and Davey 2017). And, additionally, tax credits, subsidies, and waivers all work under a presumption that we can, with a reasonable degree of accuracy, calculate the fair market rent, when in reality we cannot.

In conclusion, because we cannot calculate, within a reasonable degree of accuracy, the fair market rent, any policy to compensate housing unit owners will be lacking, and therefore any rent control policy that aims to either set a price ceiling or control the percent price increase should be considered carefully.

## VII. ALTERNATIVE POLICIES

We emphasize the importance of paying attention to the particularities and regulations of the market in question in order to construct the most effective rent stabilization mechanism. Below, we outline some policies that, at relatively low costs, would reshape the real estate market so as to make it fairer.

The first complimentary policy to mention is the proper enforcement of whatever rent stabilization mechanism we implement. This is important to emphasize, given that, fraud and evasion have been found to be especially common in rent control systems as strict as the one first proposed (Constantatos 2007).

Turning to more active policies, inclusionary zoning policies require new housing developments to include a set percentage of units for low- to middle-income residents. In Highland Park, for example, builders are required to set aside 20 percent of their units at a lower rate (CMAP 2008). The aim of these policies is to ease the financial burden on low-income renters and to remove barriers to affordable housing on municipalities that do not have the means to provide rent subsidies.

A report by Chicago Metropolitan Agency for Planning found that inclusionary zoning “could produce a significant number of units, have a positive effect on increasing transit ridership, and bring people closer to work” (CMAP 2008). The report also found that these policies have the most positive effect on areas with quality transit and limited current access to affordable housing.

These zoning policies will be crucial in providing the necessary infrastructure for a more equitable market, but we must also promote more equitable and innovative forms of living. Chicago's experience with mixed-income housing has proven widely controversial and disappointing (Chaskin and Joseph 2015); instead, and specially given the deep connections between housing inequalities and wealth inequalities (Albouy and Zabek 2016), we recommend promoting housing cooperatives.

In cooperatives, the ownership of the “landlord” company is distributed among residents. Cooperatives have a good record of acquiring, owning and operating distressed properties, including single-family homes. Consequently, we should explore financing initiatives. For example, the U.S. National Association for Home Care and Hospice funds cooperatives in distress through mortgages, pricing the home based on the tenant's financial circumstances (NAHC 2008).



## VIII. POLITICAL CONSIDERATIONS

The recent political strategic shift towards greater centralization of housing policy to the state level is, at the very least, puzzling. In contrast with Europe, U.S. rent control policies have been executed almost exclusively at the local level (except statewide bans promoted by the American Legislative Council). In our opinion, one can hypothesize that the traditionally local character of rent control initiatives is attributable to the U.S.'s institutional structure. Large cities have been systematically underrepresented (and have therefore been systematically unsuccessful in achieving their interests) throughout American history (Gerald and Kousser 2013). So, given that rent controls are a predominantly urban issue, we can understand that rent controls up to now have been carried out at the city level.

We can see how this dilution of municipal power would occur where sovereignty over rent controls to be given over to larger jurisdictions. Firstly (and keeping in mind the Lift the Ban Coalition is mostly Chicago centered), the passage of a statewide rent control law would require the votes of rural legislators, who represent areas with higher percentages of homeowners and would therefore have less at stake. These legislators would potentially even be hurt, since rent controls tend to depress home-ownership rates (Bourassa and Hoesli 2010).

Leaving aside strategic issues, representational difficulties seem even more pressing. Firstly, the proposal of a group of county representatives setting the course of negotiations and controlling the drafting of the bill seems implausible. Unless this group would be proportionally sized according to population, urban voters would be grossly underrepresented since Cook County has almost half of the state's population and a majority of its urban population. And even then, it seems strange that a representative from a rural county would have a say over a policy that is aimed at a population outside of their own jurisdiction.

Moreover, the intricacies around issues like reserve account waivers, for example, are highly linked to local contexts, which legislators are unlikely to be sensitive to. At the same time, the stringency of a rent control is intimately tied to the power balance in its regulatory board (which operates the day-to-day of the control including things like waive granting); such that, for example, the typical board in New Jersey (with a moderate control) has two tenant seats, two landlord seats, and a homeowner seat. The structure of these boards would presumably be determined by the state, such that in effect the state would be settling matters that require deep knowledge of local conditions. To accommodate for this, one could propose that counties determine the structure of their own boards, but that would entail a sovereignty of counties that is hard to sustain: what if a county decided to fill all the positions of the board with landlords, leading to a lack of enforcement of the rent control? Would they be violating the proposed law?

Lastly, at the level of analyzing different policies, were a county to be a fundamentally sovereign and operational entity, one would attempt to model savings and capital investment at the county level. But, most importantly, we would not capture the gentrification and the displacement because these would all be internal to the county; yet these two phenomena are the fundamental problems to be analysed in order to develop sound housing policies.

Municipalities, and not an obscure relationship between the state and counties, should be the fundamentally sovereign entity when discussing rent control policy. With the rental rate of Cook County at its highest level since 1990 (Institute of Housing Studies 2013), it is crucial that we carefully consider all available solutions. First- and second-generation rent controls have proven controversial and may not compare to today's innovative options. Moreover, an obscure state-county relationship is not the proper response to affordability issues. Municipalities should act as the fundamental and sovereign entity over rent control policy.

## IX. REFERENCES

- Albouy, David, and Mike Zabek. 2016. "Housing Inequality." NBER Working Paper No. 21916.
- Arnott, Richard., and Elizaveta Shevyakhova. 2014. "Tenancy Rent Control and Credible Commitment in Maintenance." *Regional Science and Urban Economics*, no. 47: 72-85.
- Bosman, J. and Monica Davey. 2017. "Everything's in Danger: Illinois Approaches 3rd Year Without Budget." *The New York Times*. <https://www.nytimes.com/2017/06/29/us/illinois-state-budget-impasse.html>
- Bourassa, Steven, and Hoesli, Martin. 2010. "Why Do the Swiss Rent?" *The Journal of Real Estate Finance and Economics*, no. 40: 286-309.
- Chicago Property Services. 2018. How Much Should Condo Associations Have in Reserves? Chicago Property Services. [www.chicagopropertyservices.com/condo-associations-reserves/](http://www.chicagopropertyservices.com/condo-associations-reserves/)
- Chicago Metropolitan Agency for Planning. 2008. Inclusion Zoning Strategy Report. [www.cmap.illinois.gov/documents/10180/55940/Inclusionary+Zoning+Report.pdf/eb7168d8-0eef-4dbb-aefc-d6e4fa80ef84](http://www.cmap.illinois.gov/documents/10180/55940/Inclusionary+Zoning+Report.pdf/eb7168d8-0eef-4dbb-aefc-d6e4fa80ef84)
- Chaskin, Robert and Mark Joseph. 2015. *Integrating the Inner City: The Promise and Perils of Mixed-Income Public Housing Transformation*. Chicago: The University of Chicago Press.
- Condominium Property Act, 765 ILCS 605/ 2015.
- Constantatos, Christos. 2007. "Excessive Rents and Non-compliance with Price Ceilings." *South-Eastern Journal of Economics*, no. 5: 225-231.
- Davies, Bill, Charlotte Snelling, Ed Turner and Susanne Marquardt. 2016. "Lessons from Germany: Tenant Power in the Rental Market." Institute for Public Policy Research. <https://www.ippr.org/files/publications/pdf/lessons-from-germany-jan17.pdf>
- Diamond, Rebecca, Timothy McQuade and Franklin Qian. 2018. "The Effects of Rent Control Expansion on Tenants, Landlords, and Inequality: Evidence from San Francisco." NBER Working Paper No. 24181.
- Dittmer, Pamela. 2015. "Operating, reserve funds must be kept in separate accounts." *Chicago Tribune*. [www.chicagotribune.com/classified/realestate/ct-mre-0315-condo-living-20150309-column.html](http://www.chicagotribune.com/classified/realestate/ct-mre-0315-condo-living-20150309-column.html)
- Generation Rent. 2016. "The Rent's Too High: 21st century rent control." *Generation Rent*. [https://d3n8a8pro7vhmx.cloudfront.net/npto/pages/1186/attachments/original/1418644476/Rent\\_Control\\_v6.pdf?1418644476](https://d3n8a8pro7vhmx.cloudfront.net/npto/pages/1186/attachments/original/1418644476/Rent_Control_v6.pdf?1418644476)
- Gerald, Gamm and Thad Kousser. 2013. "No Strength in Numbers: The Failure of Big-City Bills in American State Legislatures, 1880-2000." *The American Political Science Review*, no. 107: 663-678.
- Gilderbloom, John. and John Markham. 2008. "Moderate Rent Control: Sixty Cities over 20 years." *Journal of Urban Affairs*, no. 18: 409-430.
- Glaeser, Edward. 2003. "Does Rent Control Reduce Segregation?" Harvard Institute Research Working Paper No. 1985.
- Grimes, Paul and George Chressanthis. 1996. "Assessing the Effect of Rent Control on Homelessness." *Journal of Urban Economics*, no. 41: 23-37.
- Institute for Housing Studies. 2013. "The State of Rental Housing in Cook County." DePaul University Institute for Housing Studies. [https://www.housingstudies.org/media/filer\\_public/2013/04/22/ihs\\_2013\\_cookcounty\\_state\\_of\\_rental\\_housing.pdf](https://www.housingstudies.org/media/filer_public/2013/04/22/ihs_2013_cookcounty_state_of_rental_housing.pdf)
- Kain, John and John Quigley. 1970. "Measuring the Value of Housing Quality." *Journal of the American Statistical Association*, no. 65: 532-548.
- Kattenberg, Mark and Wolter Hassink. 2017. "Who Moves Out of Social Housing? The Effect of Rent Control on Housing Tenure Choice." *De Economist*, no. 165: 43-66.
- Linneman, Peter. 1987. "The effect of rent control on the distribution of income among New York City renters." *Journal of Urban Economics*, no. 22: 14-34.
- Lofty Real Estate. 2018. "Property Management: Why Reserve Funds are Important," Lofty Real Estate. [www.loftyrealestate.com/property-management/why-reserve-funds-are-important-when-managing-a-property/](http://www.loftyrealestate.com/property-management/why-reserve-funds-are-important-when-managing-a-property/)
- Nagy, John. 1997. "Do Vacancy Decontrol Provisions Undo Rent Control?" *Journal of Urban Economics*, 42: 64-78.
- NAHC. 2008. "NAHC Takes Lead on Addressing Housing Crisis." *Cooperative Housing*. <https://coophousing.org/>

pdf/NAHC%20CHBDec08.pdf

- NS Management. 2018. "Associations, Big and Small, Must have Two Funds". NS Management. [nsmanagement.net/associations-big-and-small-must-have-two-funds/](http://nsmanagement.net/associations-big-and-small-must-have-two-funds/)
- Oertel, Christopher. 2016. "Impact of Public Policy Measures on the German Real Estate Market." In *Essays in Real Estate Research*, edited by N. Rottke and J. Mutl. Wiesbaden, Germany: Springer Gabler.
- Office of the Comptroller of the Currency. 2014. "Community Developments." Office of the Comptroller of the Currency Community Affairs Department. <https://www.occ.gov/topics/community-affairs/publications/insights/insights-low-income-housing-tax-credits.pdf>
- Öst, Cecilia., Söderberg Bo and Mats Wilhelmsson. 2014. "Household allocation and spatial distribution in a market under ("soft") rent control." *Journal of Policy Modeling*, 36: 353-372.
- Wilhelmsson, Mats, Roland Andersson and Kerstin Klingborg. 2016. "Rent Control and Vacancies in Sweden." *International Journal of Housing Markets*, 4:. 105-129.

— the —  
PaulDouglas  
— institute —

**The Paul Douglas Institute**  
5801 S Ellis Ave  
Chicago, IL 60637

[www.pauldouglasinstitute.org](http://www.pauldouglasinstitute.org)