# Viewpoint

## Tom Bethell

# No Growth–No Vacancies

THERE IS A TENDENCY in Washington to see all economic and regulatory problems as federal in origin, with state and local contributions often relegated to a minor or nonexistent role. And this makes sense, too. In the first place, most people in Washington who concern themselves with public policy issues do not have time to think much about local matters, which therefore tend to dwindle away into molehills compared to the regulatory mountain ranges of the federal establishment —the Clean Air Act, the National Environmental Policy Act, affirmative action, the Occupational Safety and Health Administration, and so on.

In addition, there are good reasons for being more concerned about the problems of regulation at the federal level. Above all, local obstacles to economic activity are easier to overcome, in one important respect, than nationwide obstacles. The former can be circumvented, after all, by U-Haul truck and interstate highway; the latter may well require ocean liner or tramp steamer. When citizens have to emigrate in order to work (as now appears to be the case in Mexico), a nation is indeed in a bad way.

In this respect, then, the fragmentation of government jurisdiction is beneficial, because people always tend to seek out the jurisdiction having the lowest level of taxation and regulation. Local governments thus compete with one another, "bidding" for residents (taxpayers). The lowest bidder, in a sense, sets the marginal price of government, which will then constrain the price of government in all other jurisdictions.

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Put another way, when people start moving in large enough numbers from Brooklyn and the Bronx to Dallas and Houston, then the governing authorities in New York are compelled to start thinking about the costs they are imposing on their (dwindling) band of taxpayers. And probably nothing *will* concentrate the minds of office holders so effectively as vanishing taxpayers.

That is the beneficial aspect of fragmented government. But there is also a bad side. When the geographical scope of government is small, the number of people needed to influence its decisions diminishes accordingly. And so a small but determined band can impose regulations that will prevent almost anything from happening. This, in fact, was one of the most underemphasized stories of the U.S. economy in the 1970s.

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We can see this problem more clearly if we think of nuclear waste disposal. People do not want nuclear wastes in their neighborhood. So if each neighborhood is vested with the power of government, and the entire country is simply a patchwork quilt of such neighborhoods, there will be prohibitions against waste disposal sites everywhere. But we have to put nuclear waste somewhere. The same problem would not arise if there were only one all-encompassing federal government, because the small number of people who would object to a nuclear waste site in a given spot would not (one may presume) have an equivalent degree of influence over a government that represented so many more people.

**Explaining Rent Control**

Local governments can, therefore, impose severe constraints upon the economic life of the citizenry, as I discovered during a recent visit to California where I was "writer-in-residence" at the Los Angeles *Herald Examiner*. I was forced to stop thinking about President Reagan's economic proposals, the defense budget, and other Washington matters, and start thinking about local and regional affairs. My aim was to try to provide an economic explanation of events, insofar as this was possible. This entails trying to find out *why* things are the way they are, and laying bare the incentive structure that produces a given status quo.

One of the first things I decided to look into was housing prices, a favorite topic of conversation in Los Angeles. "Pretend you are a wealthy visitor wanting to buy a house in Beverly Hills!"—someone recommended to me. "Find out what a million dollars will buy!" In a way, this was typical of an attitude that is common among journalists. I was being encouraged to *exclaim* about the high price of houses, not *explain* them.

I also became interested in the high cost of apartment rents in the greater Los Angeles area. Here, of course, I immediately encountered the familiar story of rent controls. In Los Angeles the city council had enacted a rent control ordinance in 1978. And in Santa Monica—a separately incorporated city fifteen miles or so from downtown L.A.—the voters had adopted by referendum a particularly severe form of rent control in 1979. In addition, Santa Monica would soon have city council elections, with a slate of business-backed moderates running against four candidates (Santa Monicans for Renters' Rights) loosely affiliated with Tom Hayden's Campaign for Economic Democracy, and dedicated to implementing an even greater degree of government control over the local economy.

One day I went to see Charles Isham, the executive vice-president of the Los Angeles–Western Cities Apartment Association. He owns two twelve-unit apartment buildings, one in Los Angeles and one in Santa Monica. Isham told me that the typical apartment owner in the Los Angeles area is the smallest of small businessmen, usually a husband and wife who have sunk their life savings into one apartment building, in one unit of which they also live. Many of these owners are members of black, Oriental, or Hispanic minorities. However, the hostility to property rights of those who agitate for rent control is so great that they are quite unmoved by the racial or ethnic status of the property owners.

Isham seemed to regard the whole problem of rent control as nearly insoluble: politicians, he said, think in the short run (up to the next election), while the adverse effects of rent control only emerge in the long run. But he continued to hope that the California Supreme Court would ultimately uphold the constitutionality of property rights. Meanwhile, he said, the number of apartment units in Santa Monica had dwindled by about 3,000 since the enactment of rent control.

I took this information to Dennis Zane, one of the Renters' Rights candidates for the Santa Monica city council election. He told me that I had cause and effect the wrong way around. The number of apartment units began to decline before rent control came in. And that, he argued, is why there is rent control: as rents for the diminishing apartment supply rose, so did the pressures to do something about it politically.

In response to this point, Isham said something that really *explained* rent control. He attributed it to the no-growth laws that had been passed in L.A. and Santa Monica (and in many other California cities) several years earlier.

"My twelve-unit building in Santa Monica was constructed in 1965," Isham said. "If I were building it today I could not have more than six units, because now you can only build on 50 percent of the lot. It used to be about 80 percent. Consider someone who has a parcel of land. The clock is running on his mortgage costs. He is only allowed to build six units. And he also has to provide underground parking and other features—perhaps elevators—which make the units more expensive to build and maintain. To recover the builder's costs, rents might have to be as high as $2,000 per month. People can't afford to pay that. But they will buy condominiums, because of the tax break and the equity buildup." In other words, changes in the law created incentives for condos and disincentives for apartments.

The result was that apartment construction fell off immediately, and rental prices on the dwindling stock of apartment units were promptly bid up by a continuing wave of new arrivals. To arrest this price rise, rent controls were enacted, and at that point no further apartment construction was undertaken at all. (See Readings, page 55.)

The foregoing applies to Los Angeles as well as Santa Monica (with local differences in the details of the no-growth laws). The rental market in L.A. is in much better shape, however, because the rent control law there includes the important feature of "vacancy decontrol." Thus prices are ultimately set at the margin and it is not necessary to "queue up" for a vacancy. New renters merely pay higher and higher prices, because there is no new supply. Indeed, checking at city hall, I could not find *even one* privately financed apartment building under construction in L.A. today. One wonders what the city will be like as a place to live in ten years hence. Probably more and more like New York today. There will be a lot of nice places for rich people, but nothing for poor people who are just arriving and trying to make their way.

And when you come to think of it, it is in just this spirit that the no-growth laws were enacted in the first place. No-growth laws are used by the "ins" to fend off the "outs." People who live in a neighborhood or city and find it pleasant, except to the extent that newcomers create overcrowding and spoil the view, are inclined to pull up the drawbridge by enacting no-growth laws. In the long run, however, such laws will undermine a local economy. An economy can be regarded as a pyramid, or ladder, and a ladder without lower rungs is useless. It is the same with cities: making life difficult for working-class newcomers will eventually ravage the entire economy.

### Fixing One Bad Scheme with Another

In Santa Monica the situation is far worse because the rent control law permits only small annual rent increases—computed as a percentage of the purchase price (which of course could have been relatively tiny in the 1960s). Thus rents are far below market value. In such a situation you get a large number of applicants for each apartment vacancy. Who decides who gets these vacancies? The owner, for now, but Isham reported there were plans to set up a new scheme, a "selection committee" that would allow the politicians in city hall to decide who would be favored with inexpensive places to live. And of course they would be strongly inclined to favor their friends—the very people who organized on behalf of rent control in the first place (with the help of money from the Law Enforcement Assistance Administration and Comprehensive Employment Training Act, as it turned out).

By the way, the pro-rent control radicals—Santa Monicans for Renters' Rights—won all four seats in the city council election, and their first move was to impose a six-month moratorium on most new construction in the city. This of course was largely superfluous, because developers were already running away from Santa Monica as fast as they could—to places like Houston and Dallas, where they have a better chance of achieving a rate of return on their investments higher than the going interest rate.

Rent control is a disaster—as almost everyone except the dedicated socialist knows by now. But the truth is that, even if all rent control laws in the L.A. area were abolished, apartment construction would still not resume. The no-growth laws would also have to go.

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Another regulatory scheme that has emerged at the local level in the wake of the rental housing shortage is "inclusionary zoning." This has already been implemented in Orange County and in areas of Los Angeles controlled by the California Coastal Commission. And it will shortly appear in Santa Monica in more extreme form. "Inclusionary zoning" means withholding construction permits until the developer agrees to rent or sell a certain percentage (15 percent in Orange County) of condo units in the new building to low-income buyers at a fraction of the market price. As Isham pointed out, this is likely to lead to considerable social tension. Living next door to one another in identical units there will be one family paying $1,000 a month and another family paying a fraction of that. Moreover, the criteria whereby the low-income families are admitted might by the same token bring welfare and its attendant crimes and disorders into buildings partially occupied by middle-class families paying the full price (in more senses than one). A recent case in Orange County illustrates further difficulties. Units selling for about $150,000 were apportioned to selected applicants for as little as $25,000. (And the housing authorities, not the owners, made the selections.) But those with incomes low enough to qualify for the "inclusionary" units had incomes *too* low to qualify for mortgages. Moreover, the local assessor insisted on valuing the units at true market value, resulting in equally unaffordable property taxes. So the selected beneficiaries still could not afford the units, which stand empty. In response, the politicians are now demanding that the units be "sold" for an even lower price.

## Growing Elitism

What about the housing market in Los Angeles? First of all, the average price of a new house in L.A. is about a third higher than the national average. Furthermore, whereas fully 46 percent of California's residents could afford to buy a median priced home in 1976, that figure is down to 7 percent today. Of course, interest rates are largely to blame for the latter statistic. But when we look at the house price itself, we find that local ordinances once again must bear a large portion of the blame. What happened in California was that cities, including L.A., adopted regulations increasing the permissible lot size. In this way, of course, the "era of limits" that we heard so much about in the early 1970s became a kind of self-fulfilling prophecy.

An official in L.A.'s Department of Building and Safety explained it to me this way: "Ten years ago a builder could easily get a subdivision zoned R-1, which allowed you to build a house every 5,000 square feet. Now the city planning department is looking at 10,000 or even 15,000 square feet. Instead of granting R-1 zoning, it insists on 'residential estate zoning,' which usually doubles the amount of space required per house."

In L.A. you often hear it said that "we are running out of space." Less often do you hear it said that local governments have *decreed* this outcome by requiring that each new house occupy *more* space. And what has been the effect? Typically land costs account for about a third of the final house price. Is it surprising that, when the size of the lot is doubled, houses cost one-third more than the national average?

This is a product of elitism pure and simple. Requiring larger lots makes life harder for newcomers and the poor, by making it impossible to build inexpensive houses. In support of this view, an August 1980 report from the housing director of L.A.'s Community Development Department sounded the theme of "growing elitism." Noting that the public has been demanding regulation as a means of preserving the environment, it explained that "this is often just a rationalization or facade for an attitude that says: 'I have mine and I really don't want anyone else in my community.' " This attitude, as the report went on to point out, has also been reflected in delays and rejections of construction permits, brought about by "environmental and no-growth obstructionism" in the form of endless appeals, injunctions, moratoriums, and study sessions. "Only a few years ago developers could expect to process a piece of raw land into a building project within 90 days with virtually no risk of failure. Today that 90 days may take two or three years, with failure and major project modifications occurring one-third of the time, and density reductions now a part of every subdivision approval."

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I USED TO TRY to make some of these points to journalists—by way of explaining why housing prices were so high. Many of the journalists were interested, because they, too, wished they could afford to buy a house. But do you know what they would say to me? "Tom," I heard them say more than once, "what you are giving us is the businessman's point of view." ■