GOVERNMENT CREATED THE HOUSING CRISIS. GOVERNMENT CAN SOLVE IT.

Suggestions from a New York real estate attorney

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FOR AN EXAMPLE of how the good intentions of big government can produce extremely bad results, one needn't look further than the rental housing market in New York City.

We have government-sponsored financing for low-cost housing. We have special housing bonds. We have public-private construction projects. We have government agencies to help the private sector and nonprofits produce lower-cost housing. We have inclusionary mandates. Yet rental housing in New York remains more expensive than practically anywhere else in the country and suffers from a perennial "crisis" of affordability.

Earlier this year, New York revived a variation on its previously expired 421a tax abatement, first enacted in the 1970s to encourage new rental housing construction. Today's version offers developers a tax break with a present value equal to one-half to two-thirds of the entire cost to build the project—assuming the developer jumps through some hoops that seek to help labor unions and deliver more "affordable" and rent-regulated housing.

Through these and other measures, officials claim to be trying to solve the problem of high rents. But the discussion always starts from the premise that government should do more. Rarely does anyone ask whether government should instead do less, even though decades of ill-considered policy caused the housing disaster that New York faces today.

Nonregulated rents in New York City are indeed extraordinary. Small one-bedroom apartments in Manhattan cost around $3,500 a month and generally rise over time, although a recent construction boom has led to a slight downward drift near the top of the market.

The culprit for high prices cannot be the free market, because New York hasn't seen a free market in rental housing since World War II. Instead, a panoply of laws, regulations, and programs create distortions, complicate development, and make it difficult to build new housing except at the very high end. If we're serious about making New York and other major cities more affordable for renters, here are a few things to reconsider.

ZONING: About 100 years ago, municipal officials decided to separate different uses of property from each other so we wouldn't end up with slaughterhouses next to nursery schools. From that small seed of good intentions has grown a massive forest of land use regulations that limit and delay development and constrict the housing market, driving up housing costs. In New York City, every discretionary approval for a substantial project creates a veto opportunity for the local city councilmember. These opportunities are often exploited to preserve the values of existing buildings by blocking competition. Thus, zoning and approvals attract a substantial constituency and—surprise—politicians listen.

HOUSING FORMATS AND BUILDING CODES: Building codes require a certain minimum size and quality of residential units. Anything smaller or of lesser quality simply can't get built. In New York, single-room occupancy hotels once provided affordable housing to thousands of people. Then the city and state made it illegal to build that sort of housing, and also passed laws prohibiting anyone who owned such buildings from raising rents or tearing them down. The building code includes a variety of restrictions designed to improve the quality of housing, such as minimum size standards for apartments, but this makes it impossible to move forward with very inexpensive residential construction. What's wrong with providing very small housing units for people with very small incomes?

ENVIRONMENTAL IMPACT REVIEW: Many substantial development projects must endure an extended inquiry called an environmental impact review. This process has grown far longer and more complex over the years. It has in large part become a tool for those who own existing properties to slow down or stop the development of new ones.

LANDMARKING: After historic Pennsylvania Station was demolished in the 1960s to make way for the hideous Madison Square Garden, New York City implemented a robust landmarking program that now preserves by law some 35,000 old—and not so old—structures. When enormous numbers of sites are blocked from redevelopment, the remaining land becomes ever more valuable, and new housing becomes even more expensive. Plus, landmarked buildings create major economic challenges for their unfortunate owners when major repairs become necessary. We should cut back on landmarking, limiting it to genuinely special structures. Perhaps the landmarking experts can redirect their time and energy to identifying the 10 percent of existing landmarks that most merit preservation.

REAL ESTATE TAXES: New York City has a bizarre real estate tax structure in which multifamily rental buildings pay a much higher annual rate (about 4.5 percent of value) than single-family houses or condominium apartments (about 1 percent of value). For rentals, the city seeks to capture up to a third of the owner's gross revenue just through real estate taxes, an enormous bite. Of course, the more you tax something, the less of it you get. The high real estate taxes on multifamily rentals mean that building such structures, except at the highest end of the market, is economically difficult without tax abatements or other incentives doled out by the government.

RENT REGULATION: In an ordinary housing market, people move as their needs change, developers demolish and replace obsolete buildings, and the market adjusts to population shifts. But because New York City has been under a "temporary" housing emergency for 74 years, government officials decide how much rent landlords can charge; property owners must by law offer below-market lease renewals for life; and thousands of buildings are removed from availability for redevelopment. Some owners actually leave apartments vacant because regulated rents can't support the capital improvements needed to avoid penalties for violating housing codes.

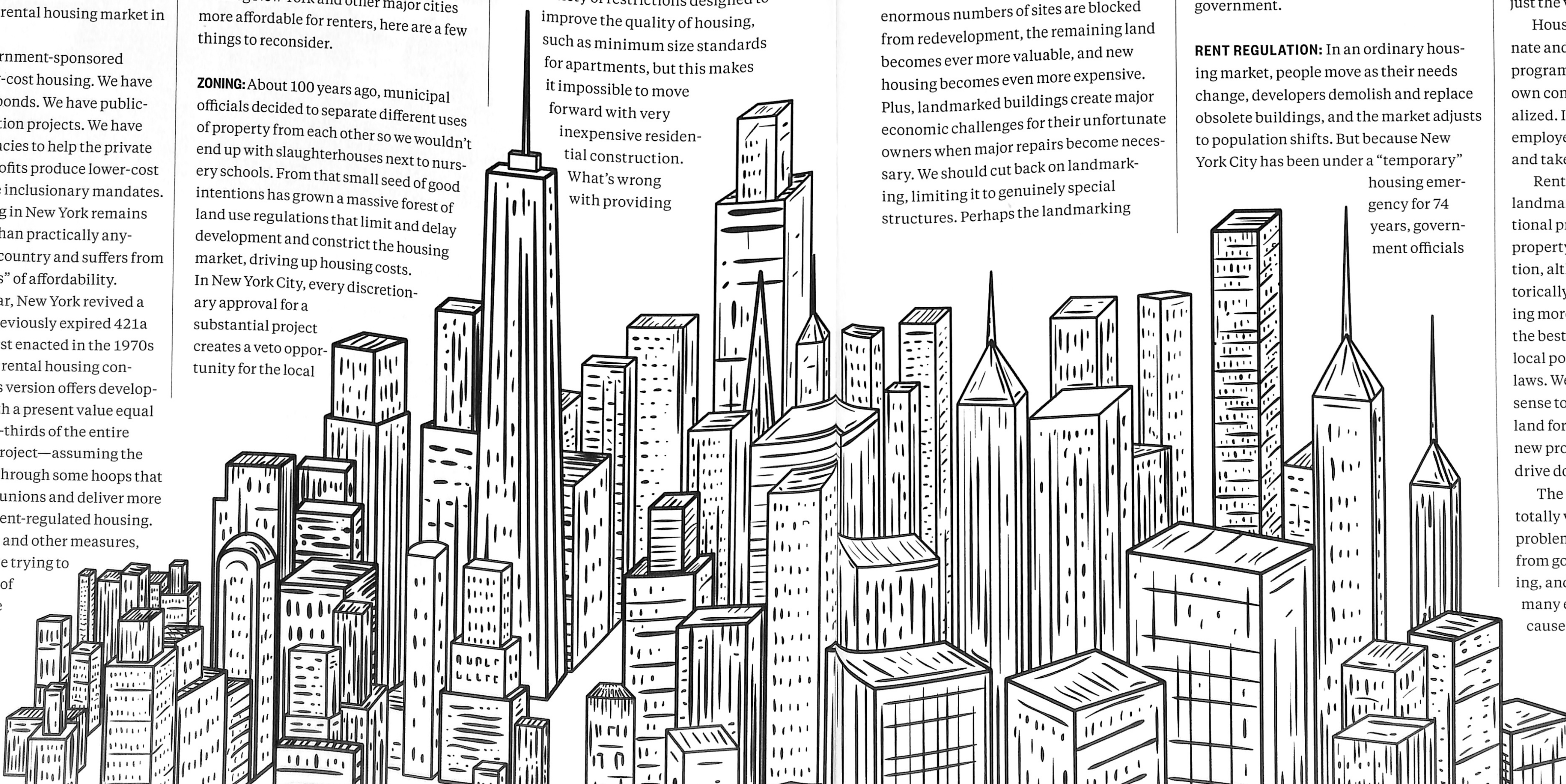
An ordinary, functioning rental housing market would free up many rent-regulated units that are underutilized or held off the market, and would make new development easier, driving down rents.

EACH OF THESE government programs exists for a putative reason. Keeping it in place helps politicians win votes from people who enjoy living in rent-regulated units and generally want to keep things just the way they are.

Housing regulations tend to germinate and take root at the local level. Each program, once established, develops its own constituency. It becomes institutionalized. It grows over time. Government employees develop special expertise in it and take it very seriously.

Rent regulation and some elements of landmarking probably violate constitutional prohibitions on the taking of private property for public use without compensation, although the Supreme Court has historically declined to rule that way. Pending more changes in the Court's makeup, the best solution might be to fight bad local policy with better state or national laws. We might also ask whether it makes sense to release more government-owned land for development, to help promote new projects or even whole new cities, and drive down housing costs.

The conventional wisdom, then, isn't totally wrong. High rents are a national problem, and solving it does require help from government—by trimming, rethinking, and in some cases phasing out the many existing government programs that caused the problems in the first place.



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