RENT CONTROL

COSTS & CONSEQUENCES

Essays on the history, and the economic and social consequences of rent control in Australia and overseas.

Edited by Robert Albon

THE CENTRE FOR INDEPENDENT STUDIES

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Rent Control
Costs & Consequences

CIS Readings 2

RENT CONTROL
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edited by

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Preface

This book is the second in a series of Readings published by the Centre for Independent Studies.* Each volume examines an important issue from a number of viewpoints, and constitutes a ready source of reference material for teachers and students.

Most of the essays in *Rent Control: Costs & Consequences* have been written especially for the book, but some have been published previously - the earliest in 1923. Most of the republished material is no longer readily available in its original form, and all is of historical and analytical interest. Australian writings and experience are emphasised in the book, but there are four contributions dealing with the consequences of rent control in other countries. The perspectives of the historian and political scientist are represented, as well as that of the economist.

Rent control is simply price control on a specific commodity. That rented housing should be singled out for special treatment is explicable mainly in terms of political expediency. Most evidence shows rent control to be a retrograde policy - yet it persists.

In modern times, and near-universally by the economics profession, rent control stands condemned. Ideological opponents agree on this matter. Friedrich von Hayek, the great liberal scholar predicted such agreement:

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* The first is *Wage-Price Control: Myth & Reality*, edited by Sudha R. Shenoy.

> If this account seems to boil down to a catalogue of iniquities to be laid at the door of rent control, that is no mere coincidence, but inevitable . . . I doubt very much whether theoretical research into the same problems carried out by someone of a different politico-economic persuasion than myself could lead to different conclusions. Therefore, if theory brings to light nothing but unfavourable conclusions, it must indicate that though the immediate benefits of rent control . . . are obvious to everyone, theory is needed to uncover the unintentional consequences which intervention brings in its wake.[1]

Gunnar Myrdal, an 'important architect of the Swedish Labour Party's Welfare State' - and sharer, with Hayek, of the 1974 Nobel Prize in Economics - confirmed the prediction:

> Rent control has in certain western countries constituted, maybe, the worst example of poor planning by governments lacking in courage and vision.[2]

Australia's experience with rent control goes back at least to the First World War. The article by H.V. Evatt deals with rent control in New South Wales in that period and is included here for historical reasons. Many readers will remember the rent controls imposed during the Second World War: one does not have to have been a landlord or tenant during the war to have been affected by these regulations for they were retained for many years afterwards - and indeed, pockets of control still linger on in some States. Australian experience exemplifies the truth that any society that implements effective rent control takes a tiger by the tail. The more controlled rents get out of line with market rents - which generally depends on how long the controls are in force - the

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[1] From F.A. Hayek, 'The Repercussions of Rent Restriction' in M. Walker (ed.) *Rent Control, A Popular Paradox*, The Fraser Institute, Vancouver, 1975. p. 80.

[2] Quoted in Sven Rydenfelt, 'The Rise and Fall of Swedish Rent Control', in Walker, op. cit. p. 182.

more difficult it is to remove the controls, for the greater is the loss suffered by the tenants as a result of decontrol - and tenants have more votes than landlords. Yet at the same time, the longer controls are in force, the more apparent become their inequities, inefficiencies, and absurdities. In favourable circumstances pressure for decontrol can avail against the interests of protected tenants.

Having - at varying paces and in varying degrees in the different States - put the era of rent control behind us, one would have thought that the lesson has been learnt: that memories of of vain searches for housing, living unwillingly with parents, of paying key money, of being locked into a controlled tenancy, of the manifest inequities among landlords, protected tenants, unprotected tenants, and would-be tenants - all of these things, and more, would ensure that rent control remained a dead letter. But memories are short. In 1973, compulsory rent control was reinstated in the Australian Capital Territory, but following a change of government, was removed in 1976. More recently, most Australian States have moved to regulate residential tenancies much more tightly than previously, and along consumer protectionist lines. Selective rent control is a standard weapon in the armoury of latter-day regulators.

This book will serve to remind older readers, and inform younger ones, of what rent control is really like, as well as to explain why it works the way it does. Mr Albon has put together a well-balanced selection of writings, wide-ranging in date and place, and varying in style from the rigorously analytical to the anecdotal. He has greatly enhanced the value of the collection by linking the selections together with his own commentaries, two of which are substantial contributions in their own right.

The Centre for Independent Studies is pleased to publish this book, which it feels makes a significant contribution to the debate on housing policy. However, the conclusions of the authors and the editor remain their's alone and cannot be considered to be those of the Centre's Directors, Trustees or officers.

Greg Lindsay

Acknowledgements

As editor of this volume, I am indebted to the assistance given to me by the Director of the Centre for Independent Studies, Greg Lindsay. His enthusiasm and attention to detail have been greatly appreciated. Much of the credit for the book must go to him.

This book has been over two years in preparation. During that time, helpful suggestions have been received from colleagues at the Australian National University - particularly Peter Swan and Ted Sieper. Ross Parish, has also provided invaluable assistance at most stages of the book's development.

I also thank the holders of original copyright in the cases where material is reprinted. Special thanks go to: The Bank of New South Wales and the Institute of Public Affairs (Vic) for allowing us to draw from their respective *Reviews*; the Real Estate and Stock Institute of Australia (now the Real Estate Institute of Australia) for allowing us to use part of its study on Canberra's rent controls; Mrs Rosalind Carrodus for giving us permission to reprint an article by her father, H.V. Evatt; and the Fraser Institute for allowing us to reprint the classic article by Milton Friedman and George Stigler and part of the article by Sven Rydenfelt.

Introduction

Robert Albon

A matter of definition

'Rent control', should more properly be called 'rent and eviction control'. The two virtually always go together, sometimes along with other legal provisions such as compulsory repair orders and controls on security bonds. Despite this, we will adhere to the traditional title, 'rent control', recognising the implicit connotations.

The term 'rent control' has recently gone out of fashion, in Australia and elsewhere. Supporters of government interference in the rental housing market do not generally wish to be associated with the rigid controls of the past. Instead, they identify with the consumer protection movement and prefer to talk of 'rental market regulation'. However,the distinction between 'control' and 'regulation' is, in general, unclear.

Private property rights

A dwelling may be viewed as a bundle of property rights held by the owner. English property law has attached a certain sanctity to these rights. In this century the law has become more ambiguous. On the one hand, the general thrust of the law remains the protection of private property, while, on the other, serious violations have occurred through the enactment of rent control and other legislation hostile to the maintenance of the private use of property.

The economist's conception of private property has

been well enunciated by Steven Cheung (a contributor to this volume).[1] The owner must have three sets of rights to an asset for it to be private property: 'exclusive right to use, or to decide how to use' the asset (Alternatively, this can be stated 'as the right to exclude other individuals from its use'.); 'exclusive right to receive income generated from the use of the good'; 'the right to transfer, or freely alienate, its ownership to any individual the owner sees fit . . . [including] the right both to enter into contracts with other individuals and to choose the form of such contracts'.

In the context of rental housing, the interpretation of these conditions is clear. The income generated by the rental dwelling belongs to the landlord (though the State may directly tax that income). Landlords and tenants will make contractual arrangements concerning the conditions of a tenancy and certain rights will be assigned to the tenant. The contract will specify the rights and obligations of both parties to the agreement.

Rent control violates the second private property condition. Control of rents below market levels entails an expropriation of income from the owner. The sum thus expropriated will usually go to the tenant, and, may, or may not, have a subjective valuation to the tenant equal to its nominal valuation. Eviction controls violate Cheung's third necessary condition. Other provisions normally found in rent control legislation also violate this condition.

'Rental market regulation' usually violates the second condition for it controls rents and hence income in some way. However, the effects may be mild because the restriction of rents is not as great as under traditional rent control. For example, rent-setting machinery may exist for use only when requested by a tenant. The temptation to call such rent regulation 'voluntary' must, however, be resisted, for if the legislation is to have any teeth any rent determinations must be binding on the parties. The 'regulators' really have an immense effect in relation to the third condition where regulatory legislation attempts to dictate many elements of the contract in meticulous detail.

Demand and supply and market 'failure'

Demand and supply remain the basic conceptual tools of economics. They have a very wide range of application, often in areas not usually considered to be the province of economics.

Demand and supply relate to markets. Economists are

usually in favour of markets as an allocative device unless the market can be shown to fail, in which case intervention designed to correct the specific failure may be advantageous. But it is hard to rationalize intervention in the rental housing market on 'market failure' grounds: rental housing is not a public good (i.e. a good the enjoyment of which by one consumer in no way diminishes its availability to other consumers); it does not give rise to significant externalities (i.e. unintended spillover effects on third parties); it is not produced subject to decreasing average costs; and the operation of this market is not seriously hampered by lack of information. Thus the economist would see no compelling **efficiency argument** for intervention such as rent control. Indeed, rent control is almost universally condemned by the economics profession.

Housing service consumption

Dwellings yield services to their occupants and it is these services that are bought and sold in the rental housing market. Ordinarily, rents are determined by the interaction of supply and demand. If demand increases as a result, say, of an increase in the incomes of tenants and potential tenants, or of an influx of migrants, rents will be bid up. If supply increases, rents will tend to fall, or not rise as much as they otherwise would have done.*

If rents are held below the market level by a system of rent control, a shortage of housing services develops. The severity of the shortage depends, in part, on whether or not eviction controls are also in force. If so, existing dwellings are 'locked into' the rental market and the shortage arises solely from the fact that more individuals and families wish to rent accommodation than there are units of accommodation available. If not, the shortage is exacerbated by some landlords, finding the controlled rent insufficient reward for the trouble and expense of letting, withdrawing their premises from the market.

The word 'shortage' has at least two meanings: an increase in the relative scarcity of a good, or the virtual inability to obtain supplies. Rent control brings about a shortage in the latter sense, and this may occur even though

---

* See the Chapters by Ross Parish, and Michael Cooper and David Stafford where this sort of simple comparative market analysis is represented in diagramatic form.

housing is no more scarce than before control was imposed. Conversely, a good many become scarce (agricultural products affected by drought or flood, for example) but still be readily available to those willing to pay its now higher price. If rents are prevented from rising, a temporary scarcity of rental housing tends to become a permanent shortage. If rents are allowed to rise, less housing will be demanded, as tenants and potential tenants economise on their use of housing space, and new supply will be forthcoming.[2]

Losers and gainers

The most obvious victims of a housing shortage induced by rent control are potential tenants. No matter how much they might be willing to pay, their chances of finding accommodation are small. Some existing tenants will also be hurt if eviction controls can be circumvented by landlords wishing to withdraw from the rental market.

Rent control deprives landlords of the difference between the market rent and the controlled rent. While landlords undoubtedly lose this amount, it is not clear that tenants make a corresponding gain: they may do so, but for a variety of reasons, tenants will usually value a tenancy at less than this rent differential.[3]

There are many other inefficiencies due to rent control. These include the administrative costs incurred in operating and enforcing the controls and compliance costs borne by landlords. Potential tenants must also face up to search costs when trying to find the 'needle in the haystack' of a vacant rental dwelling and the whole community will have to bear the costs of reduced labour mobility and deadweight efficiency costs caused by insufficient allocation of resources to housing.

Despite these costs and losses some would argue for rent control for the sake of the gainers - mainly the 'sitting tenants'. So let us suppose that society as a whole wished to redistribute income towards poor tenants. Would rent control be the best policy instrument for this task? For several reasons, the answer to this question is in the negative.

Rent control and redistribution

One reason why rent control would not be the first choice as a redistributive device is that it entails a very haphazard form of wealth transfer. It seems to be commonly believed

that poorer people are far more likely to be tenants than are the relatively better-off. This belief often forms the basis of an argument for rent control - helping tenants is synonymous with helping the poor. The Australian figures do not confirm this belief. The following table shows that there is only a slight tendency for renters to be concentrated in the lower income classes.

Percentage of Households

	Weekly Household Income						
Nature of Housing Occupancy	Under $80	$80 - $139	$140 - $199	$200 - $259	$260 - $339	Over $340	All Households
Rented	31	38	34	28	31	18	30
Owner (purchasing)	8	29	38	44	48	54	37
Owner (outright)	61	38	28	26	21	28	33
No of households ('000)	651.5	599.6	810.9	673.8	686.2	737.7	4159.5

Source: Australian Bureau of Statistics, Household Expenditure Survey 1975-76, (Canberra, 1978), Table 1.1

Tenants vary from being extremely poor to having considerable wealth and landlords range along a similar spectrum. Rent control may thus redistribute from poor to rich, as well as the other way around. An early United States study[4] was unable to establish that the average landlord was any better off than the average tenant. It is difficult to believe that any thinking person could support a policy which had such random effects as rent control. A similar result could arise by arbitrarily selecting sets of 'donors' and recipients from the telephone directory. Such a capricious policy of redistribution would be unlikely to attract many supporters.

The other major objection to this use of rent control is the fact that it is a very inefficient (as well as inequitable) redistributive device. Other policies of redistribution are superior. Milton Friedman and others have, for many years, advocated a policy of having only one tool of redistribution which would involve the abolition of all present 'welfare policies' such as pensions, unemployment benefits, government subsidised housing and family allowances. In their place would be a single scheme of general income supple-

mentation such that no-one had less than a certain level of income. This is a very radical and interesting alternative. We do not have to go this far to get an improvement on rent control. If the government must tinker with the housing market, the best option would be to remove the existing plethora of housing assistance schemes and substitute a system of housing allowances tied inversely to recipients' incomes. Even a properly administered public housing scheme would be a superior policy to rent control.

The political economy of rent control

Despite the serious deficiencies of rent control, the world has seen many instances where it has been applied. This immediately raises the question as to why legislators adopt such a policy. A justification on 'public interest' grounds seems to be impossible as there is no acceptable market failure argument for rent control and it is a very inefficient and inequitable redistributive device.

Rent control is often imposed in wartime and while the case for rent control may be at its strongest in wartime, it is by no means overwhelming. Those who argue for rent control in wartime use the usual emotive arguments (e.g. the families of servicemen must be protected from profiteering landlords) or point to special factors in wartime such as the alleged fixed supply of housing and prevalence of price controls over many other commodities. However it is far from clear that a wartime situation creates circumstances where tenants need protection. New supply of rental housing can take forms other than new building (which does stop for private purposes, during a major war). Much house-space becomes available as many leave home for various reasons. Rent control will reduce this type of response. On the demand side, it is not certain that demand will rise during a war, except in certain areas (e.g. around munition factories). In Australia, rents fell dramatically in constant price terms over the 1939-1945 period. Official estimates suggest that rents would have fallen over this period even without rent control. These circumstances are hardly those where profiteering can prevail. A further important point is that the 'protection' of servicemen's families should not be the responsibility of landlords.

However, rent control often lingers on, long after wars are over. It is sometimes imposed in peacetime, as, for example, in Canberra during the mid-seventies. Further, we have the more recent phenomenon of rental market

regulation, a policy that so far as been used exclusively in peace time.

The usual rationalisation of rent control draws on the voting strength of tenants as the political force behind the imposition or retention of controls. This story works best if there is a 'socialist' government in power, as tenants can be very loosely associated with support for the less conservative political party. Any government that contemplates the removal of rent control perceives that the loss in support from existing tenants exceeds any gain in landlord support and support from unsatisfied or potentially unsatisfied tenants. Those seeking rental housing are a diffuse and politically weak group.

Some of the papers in this volume discuss the question of the political aspects of rent control, but, except for the study by Helen Nelson, only in passing. It is, however, an extremely important feature of the rent control problem and one that needs further exploration.

NOTES

1. S.N.S. Cheung, 'A Theory of Price Control', *Journal of Law and Economics*, 17 April, 1974, pp. 53-71.
2. Rent control is not the only way that governments impede supply response. Stringent zoning and building regulations raise costs and restrict choice. See for example, the interesting study by J. Paterson, D. Yencken and G. Gunn, *A Mansion or No House*, Urban Development Institute of Australia, (Victoria), Melbourne, 1976.
3. R.P. Albon, 'The Value of Tenancies Due to Rent Control in Post-War New South Wales' *Australian Economics Papers*, 18, 33, December 1979, pp. 222-228.
4. D. Gale Johnson, 'Rent Control and Distribution of Income' *American Economic Review Papers and Proceedings*, 41, May 1951, pp.569-582.

PART I

THE OVERSEAS VERDICT

Chapter 1

Roofs or Ceilings
The Current Housing Problem

Milton Friedman &
George Stigler

Roofs or Ceilings The Current Housing Problem*

Milton Friedman & George Stigler

I. THE BACKGROUND

The San Francisco earthquake of 18 April, 1906, was followed by great fires which in three days utterly destroyed 3,400 acres of buildings in the heart of the city.

Maj. Gen. Greely, commander of the Federal troops in the area, described the situation in these terms:

> Not a hotel of note or importance was left standing. The great apartment houses had vanished . . . Two hundred and twenty-five thousand people were . . . homeless.

In addition, the earthquake damaged or destroyed many other homes.

Thus a city of about 400,000 lost more than half of its housing facilities in three days.

Various factors mitigated the acute shortage of housing. Many people temporarily left the city - one estimate is as high as 75,000. Temporary camps and shelters were established and at their peak, in the summer of 1906, cared for about 30,000 people. New construction proceeded

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* Reprinted with revisions from M. Walker (ed.), *Rent Control - A Popular Paradox*, Fraser Institute, Vancouver, 1975.

rapidly.

However, after the disaster, it was necessary for many months for perhaps one-fifth of the city's former population to be absorbed into the remaining half of the housing facilities. In other words, each remaining house on average had to shelter 40 per cent more people.

Yet when one turns to the *San Francisco Chronicle* of 24 May, 1906 - the first available issue after the earthquake - there is not a single mention of a housing shortage! The classified advertisements listed 64 offers (some for more than one dwelling) of flats and houses for rent, and 19 of houses for sale, against 5 advertisements of flats or houses wanted. Then and thereafter a considerable number of all types of accommodation except hotel rooms were offered for rent.

Rationing by rents or chance?

Forty years later another housing shortage descended on San Francisco. This time the shortage was nation-wide. The situation in San Francisco was not the worst in the nation, but because of the migration westward it was worse than average. In 1940, the population of 635,000 had no shortage of housing, in the sense that only 93 per cent of the dwelling units were occupied. By 1946 the population had increased by at most a third - about 200,000. Meanwhile the number of dwelling units had increased by at least a fifth.

Therefore, the city was being asked to shelter 10 per cent more people in each dwelling-unit than before the war. One might say that the shortage in 1946 was one-quarter as acute as in 1906, when each remaining dwelling-unit had to shelter 40 per cent more people than before the earthquake.

In 1946, however, the housing shortage did not pass unnoticed by the *Chronicle* or by others. On 8 January the California state legislature was convened and the Governor listed the housing shortage as 'the most critical problem facing California'. During the first five days of the year there were altogether only four advertisements offering houses or apartments for rent, as compared with 64 in one day in May 1906, and nine advertisements offering to exchange quarters in San Francisco for quarters elsewhere. But in 1946 there were 30 advertisements per day by persons wanting to rent houses or apartments, against only five in 1906 after the great disaster. During this same period in 1946, there were about 60 advertisements per day of houses for sale, as against 19 in 1906.

In both 1906 and 1946, San Francisco was faced with the problem that now confronts the entire nation: how can a relatively fixed amount of housing be divided (that is, rationed) among people who wish much more until new construction can fill the gap? In 1906 the rationing was done by higher rents. In 1946, the use of higher rents to ration housing has been made illegal by the imposition of rent ceilings, and the rationing is by chance and favouritism. A third possibility would be for the OPA* to undertake the rationing.

What are the comparative merits of these three methods?

II. THE 1906 METHOD; PRICE RATIONING

War experience has led many people to think of rationing as equivalent to OPA forms, coupons, and orders.

But this is a superficial view; everything that is not as abundant as air or sunlight must, in a sense, be rationed. That is, whenever people want more of something than can be had for the asking, there must be a way of determining how it shall be distributed among those who want it.

Our normal peace-time basis of rationing has been the method of the auction sale. If demand for anything increases, competition among buyers tends to raise its price. The rise in price causes buyers to use the article more sparingly, carefully, and economically, and thereby reduces consumption to the supply. At the same time, the rise in price encourages producers to expand output. Similarly, if the demand for any article decreases, the price tends to fall, expanding consumption to the supply and discouraging output.

In 1906 San Francisco used this free-market method to deal with its housing problems, with a consequent rise of rents. Yet, although rents were higher than before the earthquake, it is cruel to present-day house seekers to quote a 1906 post-disaster advertisement:

> Six-room house and bath, with 2 additional rooms in basement having fireplaces, nicely furnished; fine piano; . . . $45.

The advantages of rationing by higher rents are clear from our example:

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* Office of Price Administration.

1. In a free market, there is always some housing immediately available for rent - at all rent levels.
2. The bidding up of rents forces some people to economise on space. Until there is sufficient new construction, this doubling up is the only solution.
3. The high rents act as a strong stimulus to new construction.
4. No complex, expensive, and expansive machinery is necessary. The rationing is conducted quietly and impersonally through the price system.

The full significance of these advantages will be clearer when we have considered the alternatives.

Objections to price rationing

Against these merits, which before the war were scarcely questioned in the United States, three offsetting objections are now raised:

(a) The first objection is usually stated in this form: 'The rich will get all the housing, and the poor none'.

This objection is false: At all times during the acute shortage in 1906, inexpensive flats and houses were available. What is true is that, under free-market conditions, the better quarters will go to those who pay more, either because they have larger incomes or more wealth, or because they prefer better housing to, say, better automobiles.

But this fact has no more relation to the housing problem of today than to that of 1940. In fact, if inequality of income and wealth among individuals justifies rent controls now, it provided an even stronger reason for such controls in 1940. The danger, if any, that the rich would get all the housing was even greater then than now.

Each person or family is now using at least as much housing space, on the average, as before the war (below, p. 16). Furthermore, the total income of the nation is now distributed more equally among the nation's families than before the war. Therefore, if rents were freed from legal control and left to seek their own levels, as much housing as was occupied before the war would be distributed more equally than it was then.

That better quarters go under free-market conditions to those who have larger incomes or more wealth is, if anything, simply a reason for taking long-term measures to reduce the inequality of income and wealth. For those, like us, who would like even more equality than there is at

present, not just for housing but for all products, it is surely better to attack directly existing inequalities in income and wealth at their source than to ration each of the hundreds of commodities and services that compose our standard of living. It is the height of folly to permit individuals to receive unequal money-incomes and then to take elaborate and costly measures to prevent them from using their incomes.

(b) The second objection often raised to removing rent controls is that landlords would benefit.

Rents would certainly rise, except in the so-called black market; and so would the incomes of landlords. But is this an objection? Some groups will gain under any system of rationing, and it is certainly true that urban residential landlords have benefited less than any other large group from the war expansion.

The ultimate solution of the housing shortage must come through new construction. Much of this new construction will be for owner-occupancy. But many persons prefer to or must live in rented properties. Increase or improvement of housing for such persons depends in large part on the construction of new properties to rent. It is an odd way to encourage new rental construction (that is, becoming a landlord) by grudging enterprising builders an attractive return.

(c) The third current objection to a free market in housing is that a rise in rents means inflation, or leads to one.

But price inflation is a rise of many individual prices, and it is much simpler to attack the threat at its source, which is the increased family income and liquid resources that finance the increased spending on almost everything. Heavy taxation, governmental economies, and control of the stock of money are the fundamental weapons to fight inflation. Tinkering with millions of individual prices - the rent of house A in San Francisco, the price of steak B in Chicago, the price of suit C in New York - means dealing clumsily and ineffectively with the symptoms and results of inflation instead of the real causes.

Yet, it will be said, we are not invoking fiscal and monetary controls, and are not likely to do so, so the removal of rent ceilings will, in practice, incite wage and then price increases - the familiar inflationary spiral. We do not dispute that this position is tenable, but is it convincing? To answer, we must, on the one hand, appraise the costs of continued rent control, and, on the other, the probable

additional contribution to inflation from a removal of rent controls. We shall discuss the costs of the present system next, and in the conclusion briefly appraise the inflationary threat of higher rents.

The present rationing of houses for sale

The absence of a ceiling on the selling price of housing means that at present homes occupied by their owners are being rationed by the 1906 method - the highest bidder. The selling price of houses is rising as the large and increasing demand encounters the relatively fixed supply. Consequently, many a landlord is deciding that it is better to sell at the inflated market price than to rent at a fixed ceiling price.

The ceiling on rents, therefore, means that an increasing fraction of all housing is being put on the market for owner-occupation, and that rentals are becoming almost impossible to find, at least at the legal rents. In 1906, when both rents and selling prices were free to rise, the *San Francisco Chronicle* listed three 'houses for sale' for every 10 'houses or apartments for rent'. In 1946, under rent control, about 730 'houses for sale' were listed for every 10 'houses or apartments for rent'.

The free market in houses for sale therefore permits a man who has enough capital to make the down-payment on a house to solve his problem by purchase. Often this means that he must go heavily into debt, and that he puts into the down-payment what he would have preferred to spend in other ways.

Nevertheless, the man who has money will find plenty of houses - and attractive ones at that - to buy. The prices will be high - but that is the reason houses are available. He is likely to end up with less desirable housing, furnishing, and other things than he would like, or than his memories of pre-war prices had led him to hope he might get, but at least he will have a roof over his family.

The methods of rent control used in 1946, therefore, do not avoid one of the chief criticisms directed against rationing by higher rents - that the rich have an advantage in satisfying their housing needs. Indeed, the 1946 methods make this condition worse. By encouraging existing renters to use space freely and compelling many to borrow and buy who would prefer to rent, present methods make the price rise in houses-for-sale larger than it would be if there were no rent controls.

One way to avoid giving persons with capital first

claim to an increasing share of housing would be to impose a ceiling on the selling price of houses. This would reduce still further the area of price rationing and correspondingly extend present rent-control methods of rationing rental property. This might be a wise move if the present method of rationing rented dwellings were satisfactory.

But what is the situation of the man who wishes to rent?

III. THE 1946 METHOD; RATIONING BY CHANCE AND FAVOURITISM

The prospective renter is in a position very different from that of the man who is willing to buy. If he can find accommodation, he may pay a 'reasonable', that is, pre-war rent. But unless he is willing to pay a considerable sum on the side - for 'furniture' or in some other devious manner - he is not likely to find anything to rent.

The legal ceilings on rents are the reason why there are so few places for rent. National money-income has doubled, so that many individuals and families are receiving far higher money-incomes than before the war. They are thus able to pay substantially higher rents than before the war, yet legally they need pay no more; they are therefore trying to get more and better housing.

But not all the millions of persons and families who have thus been trying to spread out since 1940 can succeed, since the supply of housing has increased only about as fast as population. Those who do succeed force others to go without housing. The attempt by the less fortunate and the newcomers to the housing market - returning service men, newlyweds, and people changing homes - to get more housing space than is available and more than they used before the war, leads to the familiar spectacle of a horde of applicants for each vacancy.

Advertisements in the *San Francisco Chronicle* again documented the effect of rent ceilings. In 1906, after the earthquake, when rents were free to rise, there was one 'wanted to rent' for every 10 'houses or apartments for rent'; in 1946, there were 375 'wanted to rent' for every 10 'for rent'.

A 'veteran' looks for a house

The *New York Times* for 28 January, 1946, reported the experience of Charles Schwartzman, 'a brisk young man in his

early thirties', recently released from the army. Mr Schwartzman hunted strenuously for three months,

> . . . riding around in his car looking for a place to live . . . He had covered the city and its environs from Jamaica, Queens, to Larchmont and had registered with virtually every real estate agency. He had advertised in the newspapers and he had answered advertisements. He had visited the New York City Veterans Center at 500 Park Avenue and the American Veterans Committee housing sub-committee; he had spoken to friends, he had pleaded with relatives; he had written to Governor Dewey. The results?
>
> An offer of a sub-standard cold-water flat. An offer of four rooms at Central Park West and 101st Street at a rental of $300 a month provided he was prepared to pay $5,000 for the furniture in the apartment. An offer of one room in an old brownstone house, repainted but not renovated, at Eighty-eighth Street off Central Park West by a young woman (who was going to Havana) at a rental of $80 a month, provided he buy the furniture for $1,300 and reimburse her for the $100 she had to pay an agent to obtain the 'apartment'.
>
> And a sub-let offer of two commodious rooms in a West Side hotel at a rental of $75 a month only to find that the hotel owner had taken the suite off the monthly rental list and placed it on the transient list with daily (and higher) rates for each of the rooms.

Who gets the housing?

Rental property is now rationed by various forms of chance and favouritism. First priority goes to the family that rented before the housing shortage and is willing to remain in the same dwelling.

Second priority goes to two classes among recent arrivals: (i) persons willing and able to avoid or evade rent ceilings, either by some legal device or by paying a cash supplement to the OPA ceiling rent; (ii) friends or relatives of landlords or other persons in charge of renting dwellings.

Prospective tenants not in these favoured classes

scramble for any remaining places. Success goes to those who are lucky, have the smallest families, can spend the most time in hunting, are most ingenious in devising schemes to find out about possible vacancies, and are the most desirable tenants.

Last priority is likely to go to the man who must work to support his family and whose wife must care for small children. He and his wife can spend little time looking for the needle in the haystack. And if he should find a place it may well be refused him because a family with small children is a less desirable tenant than a childless family.

Socio-economic costs of present methods

Practically everyone who does not succeed in buying a house or renting a house or apartment is housed somehow. A few are housed in emergency dwellings - trailer camps, prefabricated emergency housing units, reconverted army camps. Most are housed by doubling-up with relatives or friends, a solution that has serious social disadvantages.

The location of relatives or friends willing and able to provide housing may bear little or no relation to the desired location. In order to live with his family, the husband must sacrifice mobility and take whatever position is available in the locality. If no position or only an inferior one is available there, he may have to separate himself from his family for an unpredictable period to take advantage of job opportunities elsewhere. Yet there is a great social need for mobility (especially at present). The best distribution of population after the war certainly differs from the war-time distribution, and rapid reconversion requires that men be willing and able to change their location.

The spectre of current methods of doubling-up restricts the movement not only of those who double up but also of those who do not. The man who is fortunate enough to have a house or apartment will think twice before moving to another city where he will be one of the disfavoured recent arrivals. One of the most easily predictable costs of moving is likely to be an extended separation from his family while he hunts for housing and they stay where they are or move in on relatives.

The rent ceilings also have important effects in reducing the efficiency with which housing is now being used by those who do not double up. The incentives to economise space are much weaker than before the war, because rents are now lower relatively to average money-incomes. If it did

not seem desirable to move to smaller quarters before the war, or to take in a lodger, there is no added reason to do so now, except patriotic and humanitarian impulses - or possibly the fear of relatives descending on the extra space!

Indeed, the scarcity resulting from rent ceilings imposes new impediments to the efficient use of housing: a tenant will not often abandon his overly-large apartment to begin the dreary search for more appropriate quarters. And every time a vacancy does occur the landlord is likely to give preference in renting to smaller families or the single.

The removal of rent ceilings would bring about doubling-up in an entirely different manner. In a free rental market those people would yield up space who considered the sacrifice of space repaid by the rent received. Doubling-up would be by those who had space to spare and wanted extra income, not, as now, by those who act from a sense of family duty or obligation, regardless of space available or other circumstances. Those who rented space from others would be engaging in a strictly business transaction, and would not feel that they were intruding, accumulating personal obligations, or imposing unfair or unwelcome burdens on benefactors. They would be better able to find rentals in places related to their job opportunities. Workers would regain their mobility, and owners of rental properties their incentive to take in more persons.

IV. THE METHOD OF PUBLIC RATIONING

The defects in our present method of rationing by landlords are obvious and weighty. They are to be expected under private, personal rationing, which is, of course, why OPA assumed the task of rationing meats, fats, canned goods, and sugar during the war instead of letting grocers ration them. Should OPA undertake the task of rationing housing? Those who advocate the rationing of housing by a public agency argue that this would eliminate the discrimination against new arrivals, against families with children, and in favour of families with well-placed friends.

Problems of 'political' rationing

To be fair between owners and renters, however, OPA would have to be able to tell owners that they had excessive space and must either yield up a portion or shift to smaller quarters. One's ears need not be close to the ground to know that it is utterly impracticable from a political viewpoint to

order an American family owning its home either to take in a strange family (for free choice would defeat the purpose of rationing) or to move out.

Even if this basic difficulty were surmountable, how could the amount of space that a particular family deserves be determined? At what age do children of different sex require separate rooms? Do invalids need ground-floor dwellings, and who is an invalid? Do persons who work in their own homes (physicians, writers, musicians) require more space? What occupations should be favoured by handy locations and what families by large gardens? Must a mother-in-law live with the family, or is she entitled to a separate dwelling?

How long would it take an OPA board to answer these questions and to decide what tenants or owners must 'move over' to make room for those who, in the board's opinion, should have it?

The duration of the housing shortage would also be affected. In fairness to both tenants and existing landlords, new construction would also have to be rationed and subjected to rent control. If rents on new dwellings were set considerably higher than on comparable existing dwellings, in order to stimulate new construction, one of the main objectives of rent control and rationing - equal treatment for all - would be sacrificed. On the other hand, if rents on new dwellings were kept the same as rents on existing dwellings, private construction of properties for rent would be small or non-existent.

We may conclude that rationing by a public agency is unlikely to be accepted on a thorough-going basis. Even if applied only to rented dwellings, it would raise stupendous administrative and ethical problems.

Sources and probable duration of the present shortage

The present housing shortage appears so acute, in the light of the moderate increase in population and the real increase in housing since 1940, that most people are at a loss for a general explanation. Rather they refer to the rapid growth of some cities - but all cities have serious shortages. Or they refer to the rise in marriage and birth rates - but these numbers are rarely measured, or compared with housing facilities.

Actually, the supply of housing has about kept pace with the growth of civilian non-farm population, as the estimates based on government data show (Table 1). Certain

areas will be more crowded, in a physical sense than in 1940, and others less crowded, but the broad fact stands out that the number of people to be housed and the number of families have increased by about 10 per cent, and the number of dwelling-units has also increased by about 10 per cent.

Table I

Rise in Housing and Non-Farm Population (USA 1940-1946)

	Non-farm		
	Occupied dwelling-units (millions)	Civilian population (millions)	Persons per occupied dwelling-unit (No.)
30 June, 1940	27.9	101	3.6
30 June, 1944	30.6	101	3.3
End of demobilisation (Spring 1946)	More than 31.3	About 111	Less than 3.6

Two factors explain why the housing shortage seems so much more desperate now than in 1940, even though the amount of housing per person or family is about the same.

1. The aggregate money-income of the American public has doubled since 1940, so that the average family could afford larger and better living-quarters even if rents had risen substantially.
2. Rents have risen very little. They rose by less than 4 per cent from June 1940 to September 1945, while all other items in the cost of living rose by 33 per cent.

Thus both the price structure and the increase in income encourage the average family to secure better living quarters than before the war. The very success of OPA in regulating rents has therefore contributed largely to the demand for housing and hence to the shortage, for housing is cheap relatively to other things.

Future housing problems

Rent ceilings do nothing to alleviate this shortage. Indeed, they are far more likely to perpetuate it: the implications of the rent ceilings for new construction are ominous. Rent is the only important item in the cost of living that has not risen rapidly. Unless there is a violent deflation, which no-one wants and no administration can permit, rents are out of line with all other significant prices and costs, including building costs. New construction must therefore be dis-

appointingly small in volume **unless:**

(1) an industrial revolution reduces building costs dramatically; or

(2) the government subsidises the construction industry.

The industrial revolution in building methods is devoutly to be wished. But if it comes, it will come much faster if rents are higher. If it does not come, existing construction methods will, for the most part, deliver houses only to those who can afford and wish to own their homes. Homes to rent will become harder and harder to find.

Subsidies for building, in the midst of our high money-incomes and urgent demand for housing, would be an unnecessary paradox. Now, if ever, people are able to pay for their housing. If subsidies were successful in stimulating building, rent ceilings could gradually be removed without a rise in rents. But building costs would still be high (higher than if there had been no subsidy) and so housing construction would slump to low levels and remain there for a long period. Gradually, the supply of housing would fall and the population would rise sufficiently to raise rents to remunerative levels. A subsidy thus promises a depression of unprecedented severity in residential construction; it would be irresponsible optimism to hope for a prosperous economy when this great industry was sick.

Unless, therefore, we are lucky (a revolutionary reduction in the cost of building apartments and houses), or unlucky (a violent deflation) or especially unwise (the use of subsidies), the 'housing shortage' will remain as long as rents are held down by legal controls. As long as the shortage created by rent ceilings remains, there will be a clamour for continued rent controls. This is perhaps the strongest indictment of ceilings on rents. They, and the accompanying shortage of dwellings to rent, perpetuate themselves, and the progeny are even less attractive than the parents.

An incomplete and largely subconscious realisation of this uncomfortable dilemma explains the frequent proposal that no rent ceilings or that more generous ceilings be imposed on new construction. This proposal involves a partial abandonment of rent ceilings. The retention of the rest can then be defended only on the ground that the present method of rationing existing housing by chance and favouritism is more equitable than rationing by higher rents, but that rationing the future supply of housing by higher rents is more equitable than rationing by present methods.

V. CONCLUSIONS

Rent ceilings, therefore, cause haphazard and arbitrary allocation of space, inefficient use of space, retardation of new construction and indefinite continuance of rent ceilings, or subsidisation of new construction and a future depression in residential building. Formal rationing by public authority would probably make matters worse.

Unless removal of rent ceilings would be a powerful new stimulus to inflation, therefore, there is no important defence for them. In practice, higher rents would have little **direct** inflationary pressure on other goods and services. The extra income received by landlords would be offset by the decrease in the funds available to tenants for the purchase of other goods and services.

The additional inflationary pressure from higher rents would arise **indirectly;** the higher rents would raise the cost of living and thereby provide an excuse for wage rises. In an era of direct governmental intervention in wage-fixing, the existence of this excuse might lead to some wage rises that would not otherwise occur and therefore to some further price rises.

How important would this indirect effect be? Immediately after the removal of ceilings, rents charged to new tenants and some existing tenants without leases would rise substantially. Most existing tenants would experience moderate rises, or, if protected by leases, none at all. Since dwellings enter the rental market only slowly, average rents on all dwellings would rise far less than rents charged to new tenants and the cost of living would rise even less.

As more dwellings entered the rental market, the initial rise in rents charged to new tenants would, in the absence of general inflation, be moderated, although average rents on all dwellings would continue to rise.

After a year or so, average rents might be up by as much as 30 per cent.* But even this would mean a rise of only about 5 per cent in the cost of living, since rents account for less than one-fifth of the cost of living. A rise of this magnitude - less than one-half of 1 per cent per month in the cost of living - is hardly likely to start a general inflation.

The problem of preventing general inflation should be attacked directly; it cannot be solved by special controls in

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* The actual increases that followed decontrol in 1949 averaged only about 12%.

special areas which may for a time bottle up the basic inflationary pressures but do not remove them. We do not believe, therefore that rent ceilings are a sufficient defence against inflation to merit even a fraction of the huge social costs they entail.

No solution of the housing problem can benefit everyone; some must be hurt. The essence of the problem is that some people must be compelled or induced to use less housing than they are willing to pay for at present legal rents. Existing methods of rationing housing are forcing a small minority - primarily released veterans and migrating war workers, along with their families, friends and relatives to bear the chief sacrifice.

Rationing by higher rents would aid this group by inducing many others to use less housing and would, therefore, have the merit of spreading the burden more evenly among the population as a whole. It would hurt more people immediately, **but less severely**, than the existing methods. This is, at one and the same time, the justification for using high rents to ration housing and the chief political obstacle to the removal of rent ceilings.

A final note to the reader; we should like to emphasise as strongly as possible that our objectives are the same as yours - the most equitable possible distribution of the available supply of housing and the speediest possible resumption of new construction. The rise in rents that would follow the removal of rent control is not a virtue in itself. We have no desire to pay higher rents, to see others forced to pay them, or to see landlords reap windfall profits. Yet we urge the removal of rent ceilings because, in our view, any other solution of the housing problem involves still worse evils.

Chapter 2

Rush or Delay? The Effects of Rent Control on Urban Renewal in Hong Kong

Steven N.S. Cheung

Rush or Delay? The Effects of Rent Control on Urban Renewal in Hong Kong

Steven N.S. Cheung

I. INTRODUCTION

The record of rent controls in Hong Kong presents a paradox, showing that the regulation of rents may affect urban renewal in either of two contradictory ways, causing either a premature rush or an inefficient delay in the reconstruction of buildings. Which will occur depends on a network of other factors. However, rush or delay in urban renewal is an almost unavoidable problem inherent in **any** rent control. The Hong Kong experience is chosen for discussion here only because the population pressures unique to the Colony, intensify the problem.

We deal here with three periods in which diametrically opposite developments took place. The first period began in 1921, when an influx of refugees into the Colony was putting upward pressure on rents. The rent control that followed led to surging reconstruction. The second period, following the retrocession of Hong Kong by the Japanese in 1945, introduced a new set of controls which put all-too-firm brakes on reconstruction. This lasted until increasing economic pressures led to a landmark legal decision which, together with other developments, opened a period of booming but disastrous reconstruction which extended from 1962 until 1965.

The conditions leading to the alternative and opposite results of rush or delay will be analysed in relation to each of the periods. But the basic difficulty is obvious. The goal of

any rent control is to transfer certain rights from the landlord to the tenant, yet it is difficult to specify exactly what rights are being transferred. The landlord as a rule retains the right to reconstruct. However, the tenant holds the right to possession. Since the property cannot be reconstructed without eviction of the tenant, just which one should claim the exclusive right to the rental income of the reconstructed dwelling?

The observed polarity of economic response to price controls is not surprising. Any price control operates within a framework of other economic considerations, and our study of rent control teaches that until the relevant constraints are understood, merely to say that the price of a good or the rental value of a property is by law set above or below the market price is not sufficient to produce any predictable outcome.[1] We shall try now to relate some of these constraints to the operation of rent controls in Hong Kong.

II. THE RECONSTRUCTION CRAZE, 1921-1926

On the eve of passage of the first Rents Ordinance Bill in July 1921, the Attorney General of Hong Kong announced its intention in unmistakable terms: 'The object of the Bill is to protect the tenants, not landlords.'[2] At that time, immigrants flooding into the area were bitterly competing for housing, and the bill was designed to protect current occupants of rental units from eviction or exorbitant increases in rent sparked by such pressures, while also encouraging the construction of new buildings on vacant sites.

The Rents Ordinance of 1921 and its subsequent amendments governed the relationship of tenants and landlords in four general areas. (1) Rentals were fixed, retroactively, at a 'standard' rate - that which had prevailed on December 31, 1920. (2) Landlords were prohibited from exacting side payments beyond the standard rent. (3) The lessee held the right to sublease his holding, even at a rent higher than he was paying to the landlord. (4) The right to possession of the residence was strictly stated.[3]

Fixed rentals

The rent recoverable from any tenant was clearly stated in the ordinance and was enforceable. The tenant enjoyed its full protection including the two provisions that the rent which had applied at the retroactive date of December 31, 1920, must be verifiable and that the landlord could not evict

the tenant.

When the ordinance became effective on July 18, 1921, rents had already risen considerably from the year-end level, and all expectations were that they would continue to rise. The true difference, then, between the assigned 'standard' rental and the rental prevailing on the effective date of the Ordinance was not necessarily merely the amount by which the rents had risen in that period. Rather, it was the discounted present value of the difference between the expected free-market rent and the expected controlled rent over the entire relevant period extending into the future. A landlord who could gain vacant possession of his property stood to gain by that amount; and a tenant would, if necessary, willingly have paid a comparable differential to retain possession. In that lay the seeds of under-the-table negotiation of a type which has routinely followed in the wake of rent controls. It is variously known as 'key money', construction fee, or shoe money.

Side payments

The payment of 'shoe money' had been a tradition in Hong Kong long before the ordinance was ever considered. Legend attributes the phrase to a polite euphemism for payments to middlemen who had to 'wear out their shoes' in searching out living quarters for clients. By extension, the term can to be applied to 'courtesy' payments direct to landlords by prospective tenants trying to gain tenancy. Not infrequently in crowded postwar Hong Kong such payments might amount to several hundred times the monthly rental.[5]

To discourage this type of evasion, the ordinance explicitly prohibited side payments to the landlord or demands by the landlord 'of any sum of money whatsoever, in addition to the [standard] rent.'[6] Since voluntary gifts by the lessee could not be totally forestalled, the real thrust of the regulation was against exactions by the landlord who for infractions faced a threat of court action and a fine up to one thousand dollars. To clarify the matter, the Attorney General explained that the Council considered it unnecessary to prohibit the traditional fee for 'searching' since 'while the Bill remains in operation there is no reason why anyone should be forced to pay any excessive "shoe money" . . . if [he] pays the standard rent . . . as long as the Bill remains in force, [he] cannot be turned out.'[7]

The reasoning was partially correct. The end point, however, was the question of the right of possession. If for

any cause whatever the landlord could give weight to his threat of eviction, the tenant would have incentive to offer voluntary side payment. When standard rent is lower than market rent, both the resident tenant and the prospective tenant will have reason to offer a lump sum rather than forgo a lease. Such a side payment can be effectively prohibited only if a tenant is in residence **and** the landlord has no right to evict him.

Subletting

The tenant was given a remarkably free hand to make his own arrangements in subletting his leasehold partly or entirely. While the original landlord was forbidden to raise rents, the lessee was under no such restriction. He could rent all or part of his holding at a profit. The Attorney General explained this leniency on the theory that the tenant who sublet was assuming the risks of vacancies and non-payment of rent.[7] He apparently failed to see that under a free market any landlord would be subject to the same risks and that under rent control the tenant who sublet his entire contract at a profit was, in effect, becoming an uncontrolled landlord.

Right of possession

The crux of the whole question of rent controls is reached in the consideration of who holds rights to the property, and under what terms. If rent or side payment is to be controlled effectively, the landlord must be denied the right to evict tenants. Yet unless the building is vacated, he cannot reconstruct. To establish the right of possession after its effective date, the ordinance first denied validity to 'any notice to quit, whether given before or after the commencement of this Ordinance.' It then stipulated certain conditions under which the landlord could regain possession, the principal one being Clause (a) where:

> The lessor *bona fide* requires possession of the domestic tenement in order to pull down such domestic tenement or in order to reconstruct such domestic tenement to such an extent as to make such domestic tenement a new building . . . and shall have given the tenant three months notice to quit.[8]

The landlord could also reclaim the dwelling as a residence for himself or for his family provided that he could satisfy the court that the tenant could find 'reasonably equivalent' alternative accommodation. A landlord later found to have misrepresented his own need for the property was subject to court-ordered damages to the former tenant. Although the owner was also permitted to eject a tenant who failed to pay the standard rent or who created excessive nuisance to neighbouring tenants, it was improbable that any tenant in his right mind would be obliging enough to provide such justification. Even if the owner sold the building outright, the tenants could not be evicted unless the purchaser, in turn, intended in good faith to demolish the building under the same conditions set forth in Clause (a) of the ordinance.

Great was the frustration of landlords, in a period when free-market rents were soaring and population pressures expanding. Some tried such ruses as intentionally making their properties undesirable to tenants. A bare three months after the imposition of the ordinance it was reported that 'certain landlords have gone so far as to remove windows in wet weather and even staircases to drive the tenants out.'[9] Penalties for such antics were promptly inserted in the ordinance, and by June 1922 the loopholes had been plugged up by ten new provisions.

Almost the sole remedy now remaining for the landlord who hoped to obtain free-market rents was the drastic one of demolishing and rebuilding his property. This prospect was brightened to some extent by the fact that the existing ordinance required no compensation to be paid to tenants thus evicted.

To analyse how this body of law would affect the rate of reconstruction, let us compare it with the free-market situation. The owner of a building who is free to set his own rents will reconstruct when the discounted present value of the net gain to be anticipated (the gain in site value) is positive. This gain is equal to the difference between the present value of the potential rentals of the prospective new building and the present value of the rentals of the existing building, **minus** the present value of all costs associated with demolition and rebuilding. In annuity terms, the expected market rent of the new building is calculated back to the date when the previous tenants are evicted for reconstruction.

The situation changes under rent control. Rather than market rent, the 'standard' rent represents the income from the existing old building. Instantly the brighter prospect for profit encourages premature reconstruction, to such an

extent that at first glance one might expect almost universal rebuilding if the reconstruction cost is low enough. However, side transactions will now come into play: resident tenants may have an incentive to offer substantial under-the-table payment to the landlord in return for a specific leasehold under the standard rental. The maximum key money they will be expected to offer will be the difference between the present values of the free-market rent and of the controlled rent, for the specified lease period.

Some implications are the following. If all costs of contracting for key money are zero, then under conditions where he would not have benefited from the action in a free-market situation the landlord will similarly not reconstruct his building prematurely even under controls. If all parties know that the landlord would not gain from reconstruction even under rent controls, then no threat of eviction will yield any offer of key money. Conversely, if conditions are such that the landlord would reconstruct in a free market (that is, if the aforementioned net gain is positive) then reconstruction will take place under rent control without payment of key money. Between the two polar cases, a withholding of key money payments will result in premature reconstruction.[18]

The foregoing imply that if negotiation and enforcement of a key money contract involve positive costs, then reconstruction will be premature in some cases where it would not have been undertaken under free-market conditions. Other things equal, the greater are the costs of forming key money contracts the greater is the probability that reconstruction will be too hasty.

Contributing largely to these costs of negotiation in the Hong Kong experience was the extreme difficulty of dealing with multiple-tenant households within a single residence, particularly since subletting was encouraged by the rent control itself. The typical Hong Kong building of the period had several floors, each typically occupied by several tenants and subtenants. Key money negotiations designed to curb premature reconstruction of a single building demanded consensus among that entire group, and the notorious problem of the 'free rider' further complicated matters. Moreover, since the rent control ordinance specified no termination date, the tenants held widely differing views about how long they might be protected. Another impediment was that any arrangement for key money necessarily had to be *sub rosa*; the landlord would understandably refuse to issue a receipt and the tenants had no assurance that their 'purchased' lease

rights would be honored. The stricter the legal curbs and the more costly the transactions, the greater now became the landlord's incentive to reconstruct prematurely.

Comments of legislators

Our only available evidence on the results of the Rent Ordinance of 1921 is found in the records of the legislative proceedings of the period.[11] From the reported ages of demolished buildings, it seems clear that such reconstruction was indeed well ahead of its time. However, this cannot be stated conclusively without more data. It is more helpful to judge from the comments of various legislators along the way. About eighteen months after the inception of the Rents Ordinance, the Governor informed the Legislative Council that 'the provision of houses is going on very well.'[12] Up to that time, no reconstruction had been termed 'undesirable'. Four months later, however, the Hon. Mr. H.E. Pollock sounded the earliest alarm in a lengthy report.[13] Citing a number of examples, he noted first that free-market rents for reconstructed dwellings were running about 50 to 100 per cent higher than controlled rents of comparable residences. Warning of the incentive for landlords to rush into rebuilding, Mr. Pollock continued,

> Thousands of tenants who are perfectly willing and able to pay the standard rent have been evicted or are being threatened with eviction through no fault of their own . . . Hundreds of persons at the present moment are sleeping in the streets. [One] drawback of [the] reconstruction schemes is that they have the immediate effect . . . of reducing the existing housing accommodations . . .[14]

Pinpointing one example where a two-year-old house had been demolished, Mr. Pollock continued acidly, 'I submit it is nothing short of criminal in the present state of housing accommodation to sanction any [such] scheme.'[15]

An ensuing heated debate between Mr. Pollock and the Governor resulted in no legislative action, and the reconstruction craze continued unabated. By February 1924, in another meeting of the Legislative Council, the Attorney General had come around to stating unequivocally that 'some landlords used [reconstruction] for the sake of the increased rent they can obtain from the new house.'[16] By now the

Governor himself was willing to admit his error and stated,

> I confess that where I went wrong was when I credited the landlords with having more public spirit and more refined ideas of common honesty than they appear to possess. I thought a landlord would only pull down his premises to get a substantial improvement. I did not suppose that many were prepared to go to the extreme length of destroying good buildings in order merely to evade the law.[17]

The ordinance was amended, in that meeting, to prohibit reconstruction except by approval of the Building Authority.[18]

As amended, however, the ordinance continued in force until June 1926. By that time, the pressures on housing had abruptly relaxed. The sudden and unexpected glut of housing was apparently a direct result of the earlier reconstruction craze, when the divergence between market rents and controlled rents had generated misleading market signals. Visualising vast returns to reconstruction, landlords had pushed toward more rent-productive buildings with zeal sharpened by the temporary decrease in housing while that wave of reconstruction was taking place. Once the new supply of uncontrolled housing became available, free-market forces took over and high-rent structures stood vacant.

III. THE BRAKES ARE APPLIED, 1945-1955

The second experience of rent controls in Hong Kong resulted from another, and far more severe, population surge. The Landlord and Tenant Ordinance of 1947, together with its various amendments and a dramatic reinterpretation of its meaning in 1955, constitutes an effective body of laws which is still operative today. In its present form this Ordinance is the most efficient of the many rent control systems I have investigated. Its relative success would seem to be due to its flexibility over time: in response to changing market pressures, provisions have been adopted for landlord exemptions, for tenants' surrender of lease rights, and for 'contracting out' (the latter, an option under which tenants may exchange their statutory rent protection for a privately negotiated lease not exceeding five years).[19] In combination, these provisions most nearly delineate the respective incomes (hence, the rights) of landlords and of

tenants. Even at that, we shall see that during the evolution of amendments the costs imposed upon the Hong Kong economy were high.

The forerunner of the Landlord and Tenant Ordinance was an emergency proclamation of the British Military Administration on October 22, 1945, clamping controls on the rents of all existing prewar private premises in Hong Kong and creating a Tenancy Tribunal. The regulation was considered imperative to protect the masses of Hong Kong citizens returning to the Colony after the Japanese withdrawal, against wildly inflationary rentals. For the first two years, most Tribunal cases dealt with the question of priority rights to tenancy among the thousands who had been routed from their homes by the war.

To supplement and extend this Proclamation 15, the Legislative Council on May 23, 1947, enacted the Landlord and Tenant Ordinance, setting the permissible rent of any prewar private dwelling at the amount which had been recoverable from a 'sitting tenant' on December 25, 1941. Although it was originally stated that the controls would last only one year, it shortly became apparent through routine extensions that no end was in sight. The termination clause was deleted in 1953.

The original ordinance, which left many loose ends for later tidying up, included the following terms. First, the landlord could repossess a building for reconstruction by either of two approaches: (1) eviction, or (2) exemption (also termed exclusion). Each approach presented problems. To evict a tenant, the landlord was required to prove some such infringement by the tenant as his illegal use of the premises, his refusal to pay the controlled rent, or his subletting without the owner's permission. Of these, the first would be difficult to prove, the second would be highly unlikely, and the third would in most cases be protected by the Common Law doctrine of waiver. The owner might also evict a tenant if he could prove, in terms of actual hardship, his own bona fide need to occupy the premises.

One further provision, with intereresting possibilities, was that a tenant might be evicted if he had 'given written notice to quit the premises and . . . failed to quit the same on the expiry of such notice.'[20] If a landlord foresaw adequate profit from reconstructing his building, he would be willing to bribe the resident tenants to give such notice. If his offer was tempting enough to override the obstacle of negotiations under numerous reported cases of 'hold out' by tenants and subtenants, the landlord would then be able to take over

vacant possession and rebuild. However, since the ordinance also prohibited monetary compensation, all such agreements once more had to be under the table. Observers who recall the events of that period agree that although the law was not difficult to dodge, the hold-out problem made negotiations all but impossible. There were very few cases where reconstruction followed successful negotiation with all tenants.

The second approach to reconstruction - the right of a landlord to apply for exemption from the regulations - was provided by a section of the ordinance not originally intended for that purpose. It read that on the recommendation of the already existing Tenancy Tribunal, the Governor in Council 'in his absolute discretion and without . . . hearing any interested party'[21] might exclude from the controls any premises or class of premises. Meantime the Tenancy Tribunal had been granted similar absolute discretion to make such recommendation to the Governor in response to a landlord's application.

In practice, and through the years, this double-barreled grant of 'absolute discretion' came to rest on a judgment of 'public interest', and the latitude thus given proved indispensable in the economic development of Hong Kong. However, although under these terms the tenants could be evicted without compensation, the landlord taking this approach faced the preparation of a mountain of evidence, costly and long-protracted court hearings, and a high risk of rejection. The requirements were so forbidding that fewer than one hundred such applications successfully led to reconstruction in the period from 1947 to 1954.

Need for urban renewal

Perhaps because the need for urban renewal was by then becoming so painfully obvious, the Council in 1953 relaxed the ordinance with an amendment. By that time, whether from war damage or sheer decrepitude, countless buildings in Hong Kong were all but falling down. Under rent control the landlords had little incentive to maintain their properties, yet the state of disrepair had not entitled them to take over possession for reconstruction. The Council therefore authorised the Director of Public Works to certify such buildings as dangerous and to be demolished and replaced. To avoid heightening the stresses between landlords and tenants it was stipulated that only total demolition, not even major repair, would be acceptable.

Meantime, a Building Ordinance enacted in 1935 was imposing an additional burden on owners. The ordinance had placed rigid limits on the height and general plans of prewar structures. In brief, each major residential structure was restricted to a maximum height of about four stories, based on a given angle from the centre of the frontal street. The overall structure ran the length of a block and the depth of half a block, and each consisted of a series of 'stacks' of fifteen-foot-wide apartments. Each stack was separated from an adjoining one only by shared walls and stairwells. Each of these stacks was classed as a separate building, of which a landlord might own one or more. But if he were finally granted the right to reconstruct his building, he faced the further problem of structural impact on all the adjoining properties.

Such were the obstacles which before 1955 had effectively slowed down and well-nigh halted urban renewal in Hong Kong. But in that year two crucial developments reversed the trend. First, an otherwise unexceptional court case produced a brilliant, if tortuous, legal interpretation of the Landlord and Tenant Ordinance itself. Second, the Building Ordinance was amended to permit significantly higher structures to be built.[22]

The time was overripe for change. By 1955 the population of Hong Kong had tripled over its prewar level and during that same period it had become virtually impossible to evict resident tenants. Simultaneously, reconstructed and postwar buildings were commanding rentals enormously higher than the standard rents.[23] But, as just seen, even those few landlords who finally gained the right to reconstruct were prohibited from building to greater heights and could only try to cram more stories into the permitted limit.

In this highly volatile situation, the relaxation of the Building Ordinance in 1956 lighted a fuse which had already been laid some months earlier in the landmark case of Mrs. Lee Pik-fu vs. Kwan Cheong.

IV. THE TURNING POINT OF 1955 AND THE BUILDING CRAZE OF 1962

Reconstruction and tenant compensation

In brief, the court decision in the Lee Pik-fu case established the legality of cash payments by landlords to tenants in return for the surrender of the possession of rent-controlled

property.[24] Under-the-table payments had long been practised, of course, but with indifferent success. Now it became legal for landlords to apply for exemption to the Tenancy Tribunal, which had newly been granted what amounted to the power of eminent domain* in deciding a fair recompense to evicted tenants.

Complicated as such a procedure was (and has remained) it gave some weight to a landlord's threat of eviction, rendering sitting tenants more amenable to negotiation for possession of the premises needing reconstruction. From that day to this, the Tenancy Tribunal has more or less routinely approved applications for exemption (with compensation to tenants) when they are accompanied by proper building plans and the landlord's commitment to the project. About 75 per cent of subsequent reconstruction of prewar housing in Hong Kong has taken place by way of this procedure.[25]

What would constitute fair recompense to tenants is another matter entirely. Debating the question prior to amending the Landlord and Tenant Ordinance in 1955, the Legislative Council considered a proposal that in no case should compensation exceed sixty times the monthly controlled rent. The Attorney General countered with an argument that if a ceiling were fixed, 'the maximum would become the normal.'[26] A prominent attorney put forth the economically unsound argument that the higher the compensation paid for the right to reconstruct, the higher would become the rentals of the new structure, until ultimately incoming tenants would, in effect, be paying for the new building. The amendment passed later that day specified no ceiling, leaving the determination to the discretion of the Tenancy Tribunal.

It is surprising that neither the Council nor the Tenancy Tribunal expressed any concern that too low (too high) rates of compensation imposed on landlords would predictably induce too hasty (too dilatory) reconstruction. On economic grounds it is evident that a landlord subject to controls on his rentals would have much less to lose in demolishing his existing building to escape the strait-jacket than would a free-market owner; and Hong Kong had already

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* Black's Law Dictionary defines eminent domain as; 'The right of the state . . . to reassert . . . its dominion over any portion of the soil of the state on account of public exigency and for the public good.'

seen the wastefulness of premature reconstruction under the Rents Ordinance of 1921.

Logic says that an efficient rate of compensation would be that amount which would penalise the landlord to the precise extent that he would have been willing to tax himself under free-market conditions. In the latter case he would decide to forgo the market rents of his old building after weighing them against the costs of reconstruction and the prospective rents of the new building. Exactly as in the case of key money, the efficient compensation rate under rent control for repossession of the existing structure would thus be simply the discounted present value of the difference between market rents and controlled rents over the relevant period.[27] By 1956 it was generally accepted that the rent control would continue indefinitely, therefore the compensation rate would have approximated the differential between free-market rent and controlled rent, divided by the market rate of interest. All three variables were ascertainable.

The decision in the Lee Pik-fu case had mentioned as an objective that evicted tenants should be compensated to an extent which would leave them equally well off in finding other accommodation. If effected, this solution would have been identical to the rate of compensation just outlined. But the Tenancy Tribunal chose to set its deliberations in a much wider perspective, including such side issues as legislative intent, equity, and in the typical case the mind-boggling complexity of allocating the prospective payments among the horde of tenants, subtenants, and sub-subtenants holding various areas and degrees of possession. The rates of compensation thus achieved were, of course, quite independent of true market signals. In effect, the Tribunal was now guiding the market, and the rates it set were routinely taken into consideration after 1955 in the private transaction of prewar premises and, after 1968, in private negotiations between landlord and tenants for the surrender of protection, when such a procedure was legalised by an amendment to the Landlord and Tenant Ordinance.

Rules relaxed

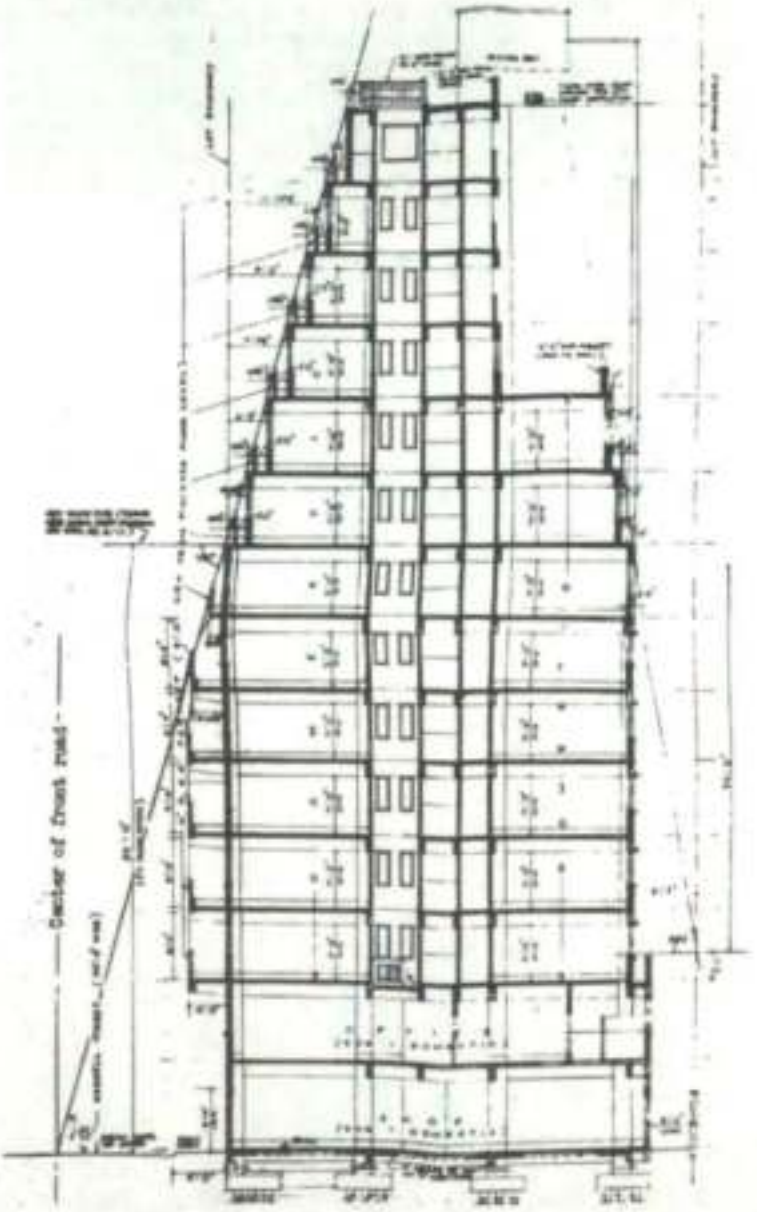
Following hard on the heels of the Lee Pik-fu case, a long-rumoured new Building Ordinance was instituted at the end of 1955 to take effect the following June 1. It notably relaxed the stricter 1935 ordinance to permit the construction of much higher and therefore more remunerative buildings.

Where the earlier ordinance had produced an average of 3.6 stories, the new regulation within five years had brought that average up to 8.85 stories, based on a random sample of 96 structures completed by 1962. Midway of that period, automatic elevators were coming into general use, greatly increasing the desirability of higher floors for living quarters. Based on 80 buildings completed in the two-year span of 1960 to 1962, the average then rose to 9.39 stories.

The new ordinance set height limits by stipulating that the main wall of a building not exceed 76° from the horizontal, as measured from the centre of the frontal street.[28] Virtually all buildings completed during 1963-1964 took full advantage of their allowance. Many owners availed themselves of a further option by setting back the upper stories; as shown in the following drawing, as many as seven stories were sometimes stepped back in this way without violating the specified angle of the hypotenuse. As we shall see, this frantic rush for the sky during 1963 and 1964 was part of what may be the most intense building craze in all history. The disastrous reconstruction was a direct result of rent control in combination with another change in the building ordinance.

The immediate result of the 1955 relaxations in both the rent-control and the building ordinances was to facilitate urban renewal. Eviction cases dropped sharply. In all the years prior to 1955 fewer than one hundred landlords had succeeded in gaining the right to reconstruct their premises by the rocky road of exemption applications. But now, in 1955 alone 104 such cases were approved, and by 1961 the annual number had risen to 270. On average, each case required the displacement of about 35 tenant households.[29]

It seems clear that the urban renewal after the Lee Pik-fu case was the immediate salvation of the Hong Kong economy. Unfortunately the period of relatively smooth readjustment was short lived. Two principal causes underlay the new outburst of construction that erupted in 1962 and was halted, perhaps providentially, only by a major depression in 1965. First, the rates of compensation determined by the Tenancy Tribunal had remained virtually unchanged through time and by 1962 had become too low and settled into a firm pattern of undercompensation which tempted landlords to demolish their buildings too early. The second and far more immediate cause was a loophole in a September 1962 amendment to the Building Ordinance which restricted the ratio of gross floor space to the site area in new buildings, thereby making new construction or reconstruction less



PROPOSED NEW BUILDINGS ON L.L. 29, SEC X
PERCIVAL ST., RUSSEL ST.

profitable. However, contained in a fine-print explanatory note to the amendment was an escape hatch through which would-be rebuilders promptly stampeded. It provided that, although the regulation would become effective in October 1962, plans to build in accordance with the 1955 standards could be approved if they were submitted before January 1, 1966, together with the landlord's agreement to carry out the project within a few months.

Applications for reconstruction boom

Aware that they could crowd significantly more floor space into the same land area if they could beat that deadline, owners snatched up hastily prepared plans and raced to the Tenancy Tribunal at such a rate that more than two thousand applications for exemption jammed the books. Soon the average applicant had to wait 306 days for a hearing. Partly as a result of the anticipated decline in future floor space in the Colony, prices for land were soaring, and the value of a given property hinged largely on how soon it was scheduled for a hearing. Not surprisingly, it was rumoured that clerks at the Tenancy Tribunal were besieged with tempting offers for advancing the papers. Meantime, the Tenancy Inquiry Bureau (in co-operation with the Department of Public Works) was under similar pressure to pronounce many buildings 'dangerous' and ready for demolition.

The records indicate that the number of buildings planned to be destroyed over a span of about three years could fairly be estimated at about one third to one half of **all** prewar premises in Hong Kong. Virtually all the plans submitted during this rush period were for the maximum height permissible. Indeed, one can walk the Hong Kong streets today and merely from the shapes of the tops of buildings bet safely on the period during which the plan for each was submitted. Had all the projected construction been rushed to premature fulfillment, what would have happened to the Colony's resources?

Construction halts

The question can never be answered, because a series of bank runs in 1964-1965 initiated a deep depression lasting from mid-1965 until late 1969. Whether the building craze was itself at least partly responsible for the depression can be judged only by monetary economists. In any case, with a deep sigh the housing boom collapsed with the rest of the

economy.

Half-built structures now stood everywhere. More than one third of the pending applications for exemption were withdrawn during 1965. By late 1965 the government was offering concessions to landlords, granting one-year extensions to those who asked for postponement of pending reconstruction or of construction under way. By January 1966, 125 cases had been postponed *sine die*, an unheard-of situation in all the years prior to 1965. Some extensions were renewed annually into the 1970s.

As to new applications for exemption, only 24 were filed in 1966; 18 in 1967; and 13 in 1968. Of 21 exemption cases handled by the Tribunal in 1967, 14 were subsequently withdrawn. In other words, both housing reconstruction and urban renewal in Hong Kong came to a dead halt until 1970.

V. CONCLUSIONS

The traditional economic analysis of price control has generated much heat but little light. The standard practice of drawing a price line above or below the equilibrium market price tells little about what the actual price or quantity will be. 'Shortage' and 'surplus', defined as the difference between the nonobservable entities of quantity-demanded and quantity-supplied, are equally unobservable concepts which confuse any empirical inquiry into the effects of price control. To say that the 'market does not clear' under such circumstances contradicts the elementary economic principle that individuals in society must resolve their conflicts one way or another through competition. Far from implying a theory, 'disequilibrium' which emerges under price controls is simply a term designed, if not to camouflage ignorance, then simply to ignore the problem.[38]

The puzzle is why economists should so long have been willing to put up with empty analysis in a subject as important as price control. The challenge of the facts has simply not been faced. My investigation leads to the conclusion that the effects of rent control (or any price control) cannot be predicted unless the relevant constraints are carefully studied and analysed.

As to the effects of rent control on housing reconstruction and urban renewal (a topic largely neglected in the literature) this paper demonstrates that totally different results may follow the imposition of such regulations. We offer here a bare outline of what has been learned in years of effort devoted to interpreting rent control laws and studying

the methods and costs of their enforcement. We have sought assistance from numerous sources and carefully verified the facts. Space limits forbid any lengthy discussion here of many other, but highly important, rights affected by rent controls: such matters, for example, as the use and maintenance of property and the transfer of lease rights. A full analysis of the many impacts of a single enactment would fill a large volume.

An economist making a snap judgment on a topic as complex as rent control would clearly be acting irresponsibly. But how much more rash is a government that imposes such controls on a nation's economy without intensive analysis to support the move. In Hong Kong, the Rents Ordinance of 1921 was fashioned in little more than two weeks. Under a justification of 'emergency', the Proclamation 15 of 1945 was deliberated for only a few days. The subsequent monumental Landlord and Tenant Ordinance of 1947 emerged from somewhat more than two months of preparation at the hands of legislators who confessed their own inexperience in that area.[31] It appears that Canada and the United States have been even more cavalier in establishing rent controls, and the various price controls enacted in the United States have been similarly unsupported by weighty analysis.

Typical of the embalmed-in-amber nature of any regulation is the fact that all rent controls in Hong Kong were initiated as 'temporary' measures. Yet the Rents Ordinance of 1921 was renewed annually, and seemed destined to eternal life, until the housing glut in 1962 rendered it obsolete. The Landlord and Tenant Ordinance of 1947, which again was intended to be temporary, survives today. All other rent-control enactments of the Colony have assumed the same durable pattern.[32] In this respect Hong Kong is certainly not unique. Professor D. Gale Johnson once observed that some of the rent controls in Europe could be traced back to Napoleon's time.

In the case of Hong Kong, the persistence of rent control cannot be blamed on any exceptional stubbornness of government. On the contrary, it has been the unusual flexibility of the ordinances in yielding to economic pressures over time which has made them tolerable. Without successive amendments, Hong Kong could never have become what it now is - one of the world's most modern cities. At great economic cost, the control laws have evolved with the city.

NOTES

1. For an elaboration of this assertion, see Steven N.S. Cheung, 'A Theory of Price Control', *Journal of Law and Economics*, 17 (April 1974): 55.
2. *Hong Kong Hansard*, 1921, p. 87.
3. These clauses as they were originally stated in *The Ordinances of Hong Kong* (1921), pp. 107-116, are quoted at fuller length in Steven N.S. Cheung, 'Roofs or Stars: The Stated Intents and Actual Effects of a Rents Ordinance', *Economic Inquiry* 13 (March 1975): 4-10.
4. Although not sanctioned, this practice was beyond the control of statutory law. It might consist of such a ridiculous, yet legal, evasion as the tenant's offer to buy from the landlord a broken chair for several thousand dollars.
5. *Ordinances* (1921), p. 116.
6. *Hansard* (1921), p. 86.
7. *Ibid.* (1922), p. 35.
8. *Ordinances* (1921), p. 111.
9. *Hansard* (1921), p. 144.
10. A more formal analysis of the various situations may be found in Cheung, 'Roofs or Stars', pp. 11-12.
11. *Hansard* of relevant years.
12. *Ibid.* (1923), p. 1.
13. *Ibid.*, pp. 40-48.
14. *Ibid.*, p. 42.
15. *Ibid.*, p. 44.
16. *Ibid.* (1924), p. 15.
17. *Ibid.*, p. 21.
18. The major clause stated that permission would not be granted 'unless the Building Authority is of the opinion that the condition of the structure . . . is such [as] to make the intended reconstruction desirable'. *Ordinances* (1924), p. 2.
19. *Ordinances* (No. 25 of 1947), currently codified in *Laws of Hong Kong*, ch. 7 (1975). The whole subject of the Landlord and Tenant Ordinance of 1947, its changing provisions over time, and its impact on the Hong Kong economy is covered in Steven N.S. Cheung, 'Rent Control and Housing Reconstruction: The Postwar Experience of Prewar Premises in Hong Kong', *Journal of Law and Economics* (April 1979).
20. *Ordinances* (No. 25 of 1947), Section 18(g).
21. *Ibid.*, Section 32.

22. The regulation of construction, as imposed in 1935 and amended in 1956, is detailed more fully in Cheung, 'Rent Control', pp. 8 and 13-16.
23. The trend continues even today. In the past decade, market rents for prewar premises in Hong Kong have soared to about eight times the controlled rents.
24. A detailed account of this remarkable case is given in Cheung, 'Rent Control', pp. 16-23.
25. The relative ease of gaining such exemptions has also lowered the bars to direct negotiation for payment between the parties, which was legalised by a further amendment in 1968.
26. *Hansard* (1955), p. 241.
27. For an analysis which yields this implication under additional constraints, see Cheung, 'Roofs or Stars', pp. 12-15.
28. Somewhat greater heights were permitted for corner or 'island' (full-block) lots, leading to competition for and merging of such sites.
29. This is calculated from data in the files of exemption cases, made available to me by the Tenancy Tribunal.
30. For a fuller discussion see Cheung, 'A Theory of Price Control'.
31. This inexperience was noted by the drafter of the bill, Mr.T.M. Hazerigg, in a covering letter to the Attorney General dated December 3, 1946.
32. The Prevention of Eviction Ordinance, enacted in 1938, was terminated by the Japanese occupation of the colony in 1941. The Rent Increases (Domestic Premises) Control Ordinance - enacted in 1963, discontinued in 1965 and reintroduced in 1970 - survives today. This ordinance controls the rents of domestic premises built in the postwar period which have estimated rental values below a certain amount. Three other less significant ordinances are related to rent control - the Tenancy (Prolonged Duration) Ordinance (1952), the Tenancy (Notice of Termination) Ordinance (1962), and the Demolished Buildings (Re-development of Sites) Ordinance (1962); they all survive today.

    It is important to note that both the dissolution of the Rents Ordinance in 1926 and the discontinuation of the Rent Increases Ordinance in 1962 occurred in periods when market rents had fallen to a point that rendered the controls largely ineffective.

Chapter 3

The Rise, Fall and Revival of Swedish Rent Control

Sven Rydenfelt

The Rise, Fall and Revival of Swedish Rent Control*

Sven Rydenfelt

I. A 'TEMPORARY' EMERGENCY REGULATION MADE PERMANENT

When rent control was introduced in Sweden in 1942 with the almost unanimous support of parliament, the decision was founded on a conviction that it was an emergency regulation that would be abolished as fast as possible after the Second World War. It was believed that wartime inflation would be followed by a deflation with a sharp decline in prices, as happened after the First World War.

However, the strong deflation which followed the First World War did not recur after the Second. For this reason rents in Sweden after 1945 remained at a level far below the prices of other commodities. And while rental costs of apartment houses remained for a long time almost unchanged, salaries and wages rose rapidly, as Table 1 demonstrates.

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* From M. Walker (ed.) *Rent Control - A Popular Paradox*, The Fraser Institute, Vancouver, 1975, with further material supplied by the author

Table 1

Rental Costs and Wages (Sweden 1939-1975)

	1939	1942	1943	1950	1960	1970	1975	Average Annual Rate of Growth
Rental Costs (1942=100)	83	100	103	104	166	253	370	4.2%
Wages (1942=100)	80	100	106	162	391	917	1600	8.7%

Sources: 'Rental costs': rents, fuel and light based on the cost-of-living index of the Board of Social Welfare. 'Wages': paid to workers in industry, communications, public services, etc., based on the statistics of the Board of Social Welfare.

In spite of all the good intentions to abolish rent control soon after the war, it succeeded in surviving until 1975, when it was finally decided to remove the last remnants (350,000 out of 2,000,000 housing units in apartment houses). Subsequently however, a new rent regulation system was introduced in 1978. The moral is that rent control is easy to introduce but hard to abolish.

A housing shortage develops

To the economist, it seems self-evident that a price control like the Swedish rent control must lead to a demand surplus, that is, a housing shortage. For a long period the general public was more inclined to believe that the shortage was a result of the abnormal situation created by the war, and this even in a non-participating country like Sweden. The defenders of rent control were quick to adopt the opinion held by the general public. All attempts by critics to point to rent control as the villain in the housing drama were firmly rejected.

The foremost defender of rent control in Sweden was for many years Alf Johansson, Director-General of the Royal Board of Housing, who has been called 'the father of the Swedish housing policy'. In an article in 1948 he described the development of the housing shortage thus:

> An acute shortage of housing units developed as early as 1941. In the following year the shortage was general and reached approximately 50,000 units in the urban communities, i.e., somewhat more than the house construction during a boom year.[1]

In a lecture he described the situation in 1948 as follows:

> We have the same shortage as at the end of the war, but the situation has not deteriorated in spite of a very great increase in demand.[2]

According to Mr. Johansson's rough sketch, the housing shortage in Sweden reached its peak as early as 1942 - 50,000 dwellings - and remained practically unchanged in the following years.

The actual development was quite different, as was revealed in the reports of the Public Dwellings Exchange offices. Only Malmo - the third largest city - had an exchange of this kind during the early war years; its reports provide a detailed account of the development (Table 2).

Table 2

Development of Housing Shortage in Malmo, 1940-1973

		APPLICANTS	
	Vacancies	Total	Without a Dwelling
1940	1,196	-	58
1941	1,047	-	129
1942	393	-	138
1943	165	-	205
1944	44	301	297
1945	41	390	288
1946	22	523	221*
1947	8	539	418
1948	-	2,459	1,498
1949	-	6,693	3,472
1950	-	9,939	4,803
1960	-	24,901	4,2595
1970	-	36,678	10,660
1973	2,086	46,526	11,593

Source: Reports of the Dwelling Exchange Office.

* In 1946 all 'old' applications were deleted from the records and a new 'purge' was undertaken in 1973.

Stockholm, the capital of Sweden, opened a Dwelling Exchange Office for the first time in 1947. Its reports give an illuminating picture of a rapidly deteriorating situation in the housing market. Families with two children, which in 1950 obtained a housing unit through the Exchange Office, experienced an average waiting time of nine months. The development during the following years is shown in Table 3.

Table 3

Average Waiting Period for Dwellings in Stockholm

	Months		Months
1950	9	1954	26
1951	15	1955	23
1952	21	1956	30
1953	24	1957	33
		1958	40

Source: Reports of the Dwelling Exchange Office. The series was not continued after 1958.

Conclusion

Thus, the 'popular opinion' encouraged by defenders of rent control, that the Swedish housing shortage was a product of the war, does not accord with the evidence demonstrated either by the Malmo data or the Stockholm data. In fact, all of the data indicate that the shortage during the war years was insignficant compared with that after the war. It was only in the post-war rent control era that the housing shortage assumed such proportions that it became Sweden's most serious social problem.

II. HOUSING AND POPULATION

The rapidly increasing housing shortage after 1945 soon ripened into a situation which could no longer be attributed to the supply dislocations that were supposedly created by the war. New explanations were needed. That most commonly adopted by the general public was the assumption that the shortage was a consequence of insufficient construction activity. If population increased at a faster rate than the number of housing units there was bound to be a shortage, people thought; and they therefore adopted the untested assumption that construction was lagging behind. Among the defenders of rent control this population growth explanation became for a long time the most fashionable.

Fallacy of the population growth explanation

The defenders of rent control were anxious to emphasise that

special consideration must be given to the rise in the marriage rate after 1940, since most housing units are occupied by married couples. The following quotation from an article by Mr. Johansson is significant:

> During 1945-46 the number of marriages in the cities was 50 per cent higher than the average for the 1930s. Under such conditions it is not difficult to explain why the addition of new housing units, even though large, has been absorbed and the shortage left unaltered.[3]

Let us confront this 'model' with statistical data on housing and population (Table 4).

Table 4

Housing and Population in Sweden, 1940-1975

	No. of Housing Units	Total Population	No. of married couples	Number of dwellings per 100 inhabitants	Number of dwellings per 100 married couples
1940	1,960,000	6,371,000	1,330,000	31	147
1945	2,102,000	6,679,000	1,463,000	32	144
1960	2,675,000	7,498,000	1,783,000	36	150
1965	2,875,000	7,773,000	1,869,000	37	154
1970	3,180,000	8,080,000	1,927,000	39	165
1975	3,430,00	8,200,000	1,833,000	41	190

Sources: Number of housing units in 1940 according to official estimates in SOU 1943: 63, p. 228; data for other years from official censuses.

During the war years the rate of housing construction was relatively low, but still high enough to increase, marginally, the number of housing units per 100 inhabitants. The number of housing units per 100 married couples, however, declined slightly (from 147 to 144) due to the exceptionally high marriage rate during the war years. During the years after 1945, when the big shortage developed, the number of dwellings in Sweden increased at a considerably faster rate than both the total population and the number of married couples.

Conclusion

In the light of the above data it seemed sensible to reject the explanation that the housing shortage was a crisis product of the war years. We have now found that the population explanation does not stand the test either.

Theory and forecasting

Human life is a walk into a future filled with uncertainty. The purpose of science is to illuminate, like a searchlight, the road in front of us. Therefore, the touchstone of all knowledge is its ability to anticipate the future - the forecast. When our astronomers can forecast hundreds of years ahead the moment for an eclipse of the sun, they prove that their conception of reality, their 'model' of the universe, is a realistic one.

The famous sociologist, Florian Znaniecki, has expressed this thesis in the following way:

> Foresight of the future is the most conclusive test of the validity of scientific theories, a test perfected in experimental science. 'Prediction' is thus the essential link between theory and practice.[4]

The need for knowledge and forecasts about society is far stronger in a centrally-directed 'planned' economy than in a liberal market economy. The British economist, Sir Roy Harrod, formulated this conclusion in the following terms:

> Lack of economic comprehension may not matter so much if the system is largely self-working. But when the working of the machine necessitates the constant vigilance of the supervisor, and the supervisor does not understand the mechanism, there is bound to be serious trouble.[5]

Judging from different forecasts, the decision-makers behind the Swedish rent controls had highly imperfect knowledge about the structure and function of the housing market. For several years they thought that the housing shortage was a product of the war and for many years afterwards they thought it to be a product of population changes. From such models of the housing market they made very optimistic forecasts, which predicted that the shortage after the war would quickly disappear.

The following 'forecast' shows how Sweden's leading official expert on housing policy 'anticipated' future developments as of 1944:

> The liquidation of the housing market shortage is a once-for-all business, which ought to be

> accomplished in a relatively short time, though not over so short a period as one year.[6]

As we have seen, subsequent developments were very much different.

A forecast of an entirely different nature was published by Professor Eli F. Heckscher, at that time the doyen of Swedish economic history and economics:

> It is probably a general opinion that the housing shortage is due to insufficient construction activity. But this is, by and large, an enormous mistake. In a free housing market no shortage would exist at the present rate of construction. On the other hand, no rate of construction activity can eliminate the shortage under the present order. It is like the tub of the Danaids, from which water was constantly flowing out at a faster rate than it could be poured in.[7]

I published a similar forecast a few months earlier:

> The cause of the housing shortage is to be found entirely on the demand side. As a consequence of rent control and the relative reduction of the rent - the manipulated low price - demand has increased to such an extent that an ever-widening gap between supply and demand has developed in spite of the high level of construction activity. Our great mistake is that we always seek the cause of a shortage on the supply side, while it is as frequently to be found on the demand side. The housing shortage will be our companion forever, unless we prevent demand from running ahead of production.[8]

It will be convenient to conclude this section with a now-classical statement by the late Professor Frank H. Knight, the 'grand old man' of the Chicago School of Economics:

> If educated people can't or won't see that fixing a price below the market level inevitably creates a 'shortage' (and one above a 'surplus'), it is hard to believe in the usefulness of telling them anything whatever in this field of discourse.[9]

III. SINGLE PEOPLE INVADE THE HOUSING MARKET

'You need not eat the whole egg to feel it is rotten'
Russian proverb

As indicated in Table 4 the number of housing units in Sweden during the period 1940 to 1975 rose by 1,520,000 (net), while the number of married couples increased by only 645,000. Even if every married couple had obtained their own home, there would still have been 875,000 dwellings available for other groups.

Which are the groups in Swedish society that have increased their occupation of dwelling space to such an extent that a serious shortage has developed? There are three groups of consumers in the housing market: married couples, previously married people, (widows, widowers and the divorced), and unmarried adults (20 years or older). Table 5 shows the size of each group at various years and the percentage living in dwellings (houses or flats) of their own.

Table 5

Number of Persons by Groups and Percentage Occupying Own Dwellings

	Married couples	%	Previously married persons	%	Unmarried adults	%
1940	1,330,000	98	933,000	65	1,655,000	23
1945	1,463,000	98	937,000	63	1,337,000	23
1960	1,783,000	96	975,000	73	1,047,000	36
1963	1,869,500	95	928,000	77	1,031,300	43
1970	1,927,000	94	717,000	80	1,073,000	30
1975	1,813,000	94	874,000	82	1,300,000	33

Sources: Official housing and population censuses.

Notes: The sum total of **occupied** dwellings, calculated from Table 5 is not equal to the sum total of housing units in Table 4. At every time, even during shortage periods, there is a reserve of unoccupied empty dwellings. According to the housing census this reserve was 93,000 in 1965 and 129,000 in 1970.

Growth of demand among unmarried adults

All housing censuses indicate that, with few exceptions, married couples have always occupied housing units of their own. However, it is also true – even in a free housing market – that there is some 'doubling up', for example, young married couples living with their parents for a while. The majority (65 per cent) of the previously married also lived in dwellings of their own in 1940. Their share had increased by 17 per cent by 1975.

The only dramatic change has been for unmarried adults of whom only one in four occupied a dwelling of his

own in 1940, while 35 years later more than one in two did. Thus the supply of dwellings available for unmarried adults must have rapidly improved during the 35-year period (Table 6, which is another way of viewing the information contained in Table 5).

Table 6

Persons without Dwellings of their Own
(In Absolute and Relative Numbers, 1940-1975)

	Married Couples	%	Previously Married	%	Unmarried Adults	%
1940	27,000	2	132,000	33	1,119,000	77
1945	29,000	2	160,000	33	1,009,000	75
1960	36,000	2	144,000	23	708,000	64
1965	37,000	2	144,000	23	611,000	57
1970	35,000	2	143,000	20	392,000	50
1975	39,000	2	157,000	18	705,000	67

Sources: Official housing and population censuses.

Table 6 shows that in both 1940 and 1945 over 1 million unmarried adults lacked housing units of their own. The reason why the housing shortage - the demand surplus - was relatively small as late as 1945 in spite of this enormous reserve of demand was that only a small proportion of these persons were actively seeking dwellings of their own. The majority either lived - and were satisfied to live - with their parents, or they rented furnished rooms.

The majority of unmarried adults from the beginning accepted a passive role. The explanation of the housing shortage must be sought in the fact that this majority was later progressively transformed into active dwelling-seekers who invaded the housing market and with energy and success hunted and occupied homes. As indicated in Table 5, the share of residents with their own dwellings in this group has increased from 23 per cent in 1940 to 55 percent in 1975. The implication of this strongly-increased demand for dwellings among unmarried adults is that they occupied 416,000 more homes than they would have done had only the same proportion (23 per cent) as in 1940 occupied their own dwellings. As the number of dwellings in Sweden increased by a net 1,520,000 from 1940 to 1975 more than 25 per cent of the increase has thus been disposed of exclusively to satisfy the extra demand of unmarried adults.

What has brought about this upsurge in the demand of single persons for private dwellings? The reason of course is that the normal relation between income and rents has been entirely distorted by rent control. In the period 1942 to 1975

industrial wages grew to 16 times what they were in 1942 while rents less than quadrupled. The distortion was particularly marked between income and rents of apartment houses built before 1942 (see Table 1).

That the share of persons with housing units of their own in the unmarried adult group increased from 23 per cent in 1940 to 55 per cent in 1975 by no means implies that the demand for dwellings by this group was satisfied. The longest queue at the housing exchange offices was, during all the shortage years, made up of unmarried adults.

Responsiveness of housing demand to changes in price

In the absence of rent control the increase in demand for rental housing would have been less accentuated and, in particular, it would have been less among unmarried adults. It all depends on the 'price elasticity' of demand. According to common experience, the price and income elasticity of demand for dwellings is low, as it is for other necessities like food and clothing.* It is on this basis that the supporters of rent control have attempted to build up a defence. If the demand for dwellings has a low elasticity, they argue, a relative reduction in rent levels could not have increased demand very much.

This general reasoning, however, is valid only for the married and previously married groups. For members of these groups private dwellings are a necessity and, as a result, price and income elasticities are relatively low. The situation is different for unmarried adults. For the majority in this group a self-contained housing unit is somewhat of a luxury, a non-necessity. Young people will often hesitate if they have the choice between going on living cheaply and comfortably with their parents or moving out and acquiring a dwelling of their own.

That unmarried adults occupy self-contained housing units of their own to a lesser extent than the married is not

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* Editor's note: Price (or income) elasticity of demand for a commodity is high if a given percentage change in price (or income) leads to a greater percentage change in the quantity demanded. Elasticity is low if the quantity demanded changes less (in percentage terms) than the change in price or income. However, the empirical evidence on the values of these elasticities does not conclusively suggest that they are low.

due to lower income. In fact, a comparison of income levels, taking account of the obligations of family men - that is, the number of persons living on one income - shows that the incomes of unmarried adults are as high as those of the married. The unmarried have demanded dwellings to a lesser extent because they assign a higher priority to other things, such as clothing, amusements, travel, education, etc.

For the majority of unmarried adults, a dwelling is a relatively dispensable commodity, and the demand for a commodity of this kind is normally highly sensitive to changes in price or income. The strong reduction in rents relative to other prices and to incomes (resulting from rent control) has, for this reason, considerably stimulated the demand for homes on the part of unmarried adults.

The data in Table 6 indicate that in 1945 more than a million unmarried adults in Sweden lacked housing units of their own. This represented a very large potential demand reserve that rent control unleashed on the housing market. The influx of this group into the housing market naturally created a demand which far exceeded supply.

IV. HOUSING PRODUCTION GROSS AND NET

> In many cases rent control appears to be the most efficient technique presently known to destroy a city - except for bombing.[18]

Deterioration of the housing stock

It is well known and documented that rent controls result in poorer maintenance, fewer renovations and modernisations and, therefore, in the long run in a serious deterioration in the quality of dwellings. Because some requests for rent increases have been granted, the defenders of control have persistently contended that deterioration and slum development have not occurred. This argument is fallacious.

Rent control breeds slums

As a result of control and lower rental income, owners' ability to maintain their apartment houses has declined. In particular, their incentive for such upkeep which is motivated by an aesthetic or comfort point of view has dwindled.

In a free market there is never a shortage of dwellings and flats to let. If the owner in such a market does not keep his property in good condition he runs the risk of losing his

tenants and being left with empty flats and losses in rental income. In a controlled market with severe shortages, the owner is under no such compulsion. No matter how badly maintained is his property, there are always long queues of homeless people willing to rent his shabby, poorly maintained flats.

Since there is no economic incentive to encourage the owners to repair, even basic upkeep - which in the long-run is necessary to prevent serious quality deterioration (i.e. slums) - is neglected. A development of this kind is difficult to describe in quantitative terms. But thanks to the detailed Swedish statistics on the number of new dwellings and the periodic housing censuses, an important aspect of the process can be documented (Table 7).

Table 7

Gross and Net Housing Production, 1941-43 to 1971-75

	Total new dwellings constructed (a)	Net increase in stock of dwellings (gain) (b)	Dwellings removed from housing stock (loss) (c)	'Loss Ratio' of (c) to (a) %
1941-45	180,000	142,000	38,000	20
1946-60	825,000	573,000	252,000	30
1961-65	413,000	200,000	213,000	52
1966-70	513,000	304,000	209,000	41
1971-75	469,000	350,000	119,000	25

Sources: Housing Construction (Swedish Official Statistics), and the housing censuses.

Rapid 'loss' of houses

What is striking about Table 7 is the rapid increase in the 'loss' (column c) up to the year 1965. During the period 1941 to 1945 the net increase in the stock of dwellings was about 80 per cent of new production and the 'loss' only 20 per cent. During the years 1961 to 1965, the net addition was barely 50 per cent and the 'loss' more than 50 per cent. The 'loss' in those years assumed such proportions that the authorities appointed a special committee with instructions to try to explain 'the mystery of the disappearing dwellings'. After 1965 the process of decontrol got into full swing, and from 1965 to 1970 the number of controlled private houses decreased from 900,000 to 600,000 and from 1970 to 1975 from 600,000 to 350,000. As a consequence, the number of 'losses' decreased.

The anticipation of profits is the incentive to private enterprise to produce housing units. If this incentive is

destroyed by regulations, and if it is made more profitable for the owner of apartment houses to rent his dwellings for commercial purposes, then it is not possible to prevent - in spite of prohibitions - a conversion of dwellings to offices, shops or storerooms.

It was of no avail to pour increasing amounts of public funds into the housing bag, as long as we did not patch up its holes. It was of no avail that since 1945 we had built more dwellings per head in Sweden than in any other country (according to the *UN Statistical Yearbook*). It was of no avail that we built more than 100,000 dwellings per year, when the 1967-1972 annual 'loss' at the same time was about 40,000. A construction of 70,000 dwellings and a loss of 10,000 would have given us the same net addition. The system of control obviously caused an enormous and shameful waste of resources.

V. THE FALL AND REVIVAL OF SWEDISH RENT CONTROL

The Swedish Government in 1965 boldly promised that one million new dwellings would be built during the decade 1965-1974. Until then the hunger for new dwellings had seemed insatiable, and the Government did not provide for the possibility of a surplus of housing. Thanks to an over-dimensioned building industry and extensive subsidies, such an ambitious programme could be fulfilled.

The gradual abolition of rent control, plus extensive new construction laid the base for a surplus that from 1970 became quite disturbing. But a political 'promise' is a 'promise' and in spite of growing surpluses the building programme had to be fulfilled. A Swedish construction record - 110,000 new dwelling units - was reached in 1970, after which construction went on at a decreasing rate.

According to the socialist Swedish Governments, housing construction must be controlled in order to prevent the ups and downs of private unregulated production. But in spite of this strict control, construction in Sweden went down from 110,000 in 1970 to 56,000 in 1976; a decrease of 50 per cent in six years.

The growing vacancies in the first years of the 1970s were one reason for the decline, but only a minor one, as rent losses were mostly paid by the government. The main reason was the new control system which prevented cost covering rents. The consequences were growing financial and maintenance troubles for the landlords - troubles so severe that

private building of rental housing practically stopped, while council building shrank drastically.

It was not only the volume which changed, but the product mix as well. The share of small family houses in new production exploded from 30 per cent in 1970 to 75 per cent in 1978. This explosion had its origins in the unsatisfied demand which had piled up during the long Social-democratic era (1932-1976). The building of family houses was, however, less imposing in numbers than in percentages: 33,000 in 1970 compared to 40,000 in 1978. The reduction of apartment house building was more conspicuous: 77,000 dwellings in 1970 compared to 14,000 in 1978.

The fall and rise of quality construction

During the years of shortage created by rent control, apartments of low quality in dismal environments were mass-produced, and having no choice, the homeless families in the queues had to accept them. Following decontrol, the growing surpluses created quite a new situation; the sellers' market was transformed into a buyers' market. The housing enterprises had to compete for tenants, and this competition forced the builders to use all their creativity to produce attractive flats. During the shortage years they could ignore the wants and wishes of the consumers but now they had to respond to them. Fewer 'skyscrapers' were built, and more construction in Sweden now consists of low houses with one or two stories and with an easy and intimate contact with the ground. Most families have out-of-door rooms or green plots of their own. In fact, the changed market situation altered the quality of new construction (houses and environment) in a miraculous way. Because of inflation and rising costs, new flats will normally be more expensive than old ones, and so in a balanced market they can find tenants only if they offer greater advantages than the older flats. The builders in Sweden, accustomed in the past to the protection that shortages provided, are today adjusting to consumer sovereignty.

Co-operative housing

In Sweden, building societies own about 500,000 housing units in apartment houses. Nominally, these houses are owned by co-operative societies founded by co-operating families, but in reality these flats, with certain restrictions, are owner-occupied.

In 1939 only 4 per cent of new construction was built by the societies, but during the war years and the following decades co-operative housing was so encouraged by the government and by the housing shortage, that the share of co-operative housing in 1959 reached a peak of 32 per cent. In subsequent years the share of co-operative housing has been declining, and from 1975 on, the share has been about 10 per cent. Because special concessions by government are not enough, there must be a shortage for a scheme of this sort to be successful. The gradual abolition of rent control from 1958 meant that the shortage reached its maximum proportions about that time. With gradually shrinking queues, the market for co-operative housing deteriorated year after year.

In order to become a member of a co-operative housing society a person must pay a rather large sum in cash, and in a period of shortage people have little choice. But as the market was permitted, by the return to a more economic pricing, to provide a supply of alternatives, a preference for rented apartments in the private sector and for single-family houses became evident. The demand for co-operative houses shrank to such an extent that it often happened that a family wanting to move could not find another family willing to take over and pay that sum in cash that they themselves had paid. As the risks of such losses became generally known, the demand for co-operative flats shrank still more.

There is a class of organisms called 'pathophiles' that detest healthy environments but thrive on sick plants and animals. So it is with council and co-operative housing enterprises. They had their golden age during the years when our housing market was fatally ill and disorganised by government regulations and shortage. But the more the shortage decreased and the more the market recovered its balance the more the status of these enterprises deteriorated.

Private housing enterprises, on the contrary, thrive only in healthy, balanced markets and react with pronounced 'pathophobia' against pathological environments. During the worst control - and shortage - years, private housing suffered seriously.

The end of co-operative rent control

Every time a member of a co-operative society wanted to move, he had to 'sell' his flat to a new member wanting to take over. But up to 1969 the society board had to calculate and approve the sum paid. No 'speculation' was allowed. In

the Swedish housing market there is intense competition between co-operative flats and family homes, and here the co-operative societies felt handicapped. Their members were not allowed to sell at free prices, which the home-owners could.

So in 1968 the big society organisations requested the Social-democratic government to abolish co-operative rent control. The government acceded and control for the co-operative sector was ended from January 1, 1969. From this time, 'speculation' with co-operative flats has flourished in a manner similar to family homes.

Council housing

From 1932 to 1976 Sweden had Social-democratic governments with an antipathy towards private housing, whether privately-owned apartment houses or owner-occupied single family houses. The construction of council houses, owned by local authorities, and co-operative houses, owned by building societies, was encouraged by special concessions and subsidies, and largely as a consequence, out of 2,000,000 rented dwellings in 1975, 600,000 were in council houses and 500,000 in co-operative houses.

The government apparently believed that apartments in local authorities' projects would be cheaper, due to the absence of profits, and better than privately-owned apartments. The managers of the local authorities' projects - often with a political career as their only merit - energetically tried to live up to that hope. But, costs could not be conjured away. In the event, rents on the council apartments stayed, for a time, at about the same level as the rents on private apartments.

Political pressures ultimately had their effect however, and for a number of years council project managers set rents lower than were to be found in private housing. This was done in spite of the fact that at the lower level, rents did not cover costs. Gradually this policy led to a depletion of council project funds and they had to fight desperately against growing liquidity problems. In the face of such difficulties there was only one expedient - rent increases. And, as council houses had been freed from rent controls in 1958, rents were increased. Having allowed considerable increases in the rents on council houses, the government had to allow private rent increases, too.

From shortage to surplus

In the 1970s a considerable surplus (mostly municipal) developed. For the local authorities, this surplus was a shocking experience. They had for several decades lived in a world without vacancies, a world they found natural. In their economic calculations there was no allowance - and no funds - for the losses associated with vacancies.

For municipal authorities this was an abnormal and undesirable phenomenon meaning economic catastrophe, and in 1972 the situation for the municipal housing enterprises was so disastrous that the government had to hasten to their rescue. Bankruptcies would have meant political scandal and 1973 was an election year.

So, loans on extremely advantageous conditions were given, and the local governments, the legal owners of the council houses, had to provide extensive subsidies as well. Up to 1975, vacancies - and vacancy losses - grew year by year, and with them the need for loans. Most of the borrowing enterprises are in such a precarious financial condition that there is little likelihood that they will be able to repay the interest on the loans, let alone the capital values. The losses, therefore, will be paid by the taxpayers.

Tenants take over power

Swedish rent control was gradually abolished from 1958 when council houses were exempted. In 1975, when only 350,000 out of 2,000,000 rented dwellings were still under control, the Government decided to remove the remaining controls over the period 1975-1978.

A puzzling element in the political fight for and against rent control was the manoeuvring of the powerful National Association of Tenants (670,000 members in 1979 - 1,300,000 including families). From the beginning it was one of the most fanatical defenders of rent control, but it eventually changed its attitude and in the last decade had become very critical. During the last years of controls, an explanation of this change of opinion emerged. The abolition of rent control was not, as could have been expected, followed by a free housing market. Instead a new regulation system was established; a negotiation system in which the Association of Tenants played a dominant role. All rents in Sweden, like wages, were now to be decided by negotiation between the bargaining blocs of tenants and landlords.

Council rents to function as guidelines

The biggest single landlord bloc was the Association of Local Authorities which in 1979 represented 650,000 out of 700,000 council dwellings. A main principle of the new system was that self-supporting, non-profit council rents were to function as guide-posts for the rents in the 800,000 private dwellings. As popular opinion held that big slices of private rents in a free market were above normal profits, then a result of this system ought to be lower rents for the tenants in private houses, though indeed they should be self-supporting. In theory this rent determination strategy seemed rational and streamlined. But alas, it did not function in practice and for different reasons. Firstly there was a strong desire in local authority managers of council houses to be able to boast of lower rents than those charged in private houses. There was however, still another reason why council rents during the new negotiation system were never self-supporting. For if you transform a market price into a political price, sooner or later the buyers will refuse to pay cost-covering prices, with disastrous effects for production, provision and distribution.

In a free market there is equality, and a power balance between individual sellers and buyers. Generally, this balance is upset as soon as government interferes in the market, supporting one party or the other by the use of its power apparatus.

In the Swedish housing market, Government supports the buyers (the tenants) not only by giving their Association official status as the legal negotiator, but also by making negotiation mandatory for the landlords. As an extra privilege, Government grants tenants legal security of tenure.

The housing crisis of 1978

Faced with such powers, not only the landlords, but Government too had to surrender. The economic crisis with rapid inflation created a need for substantial rent increases, but at the same time because of economic stagnation, a hardening resistance was met from tenants. In the autumn of 1978 the local authorities demanded and needed, 18 crowns per square metre, while the Association of Tenants refused to accept more than 7 crowns. A deadlock situation soon developed with the threat of major confrontations. A conflict with extended rent strikes would very soon have created a financial catastrophe for the landlords, not least for the local authorities. And for the Liberal minority government that

took power in October, such a conflict would have meant political disaster.

The Association of Tenants was indeed a powerful political pressure group, disposing of more than one million votes among its members. A blackmail situation developed and the new government had to pay the ransom - one billion crowns to the local authorities. This was to fill up the gap between the rents the authorities urgently needed and the rents the tenants were prepared to pay.

The surrender of the Government meant a triumph for the Association of Tenants not only at that time but also for the future, as it acted as a precedent. The new negotiation system founded on self-supporting rents was thus in ruins after only a few years.

The revival of rent control

> If you expel the devil through the front door, he will return by the back entrance.
>
> **Jewish Proverb**

The formal abolition of rent control never meant a return to free markets and free prices. In the new system substituted for rent control, rents are still manipulated by Government, directly or indirectly.

In 1975 only 350,000 out of 2,000,000 rented dwellings were under control. The new system, launched in 1975 however, meant a return from partial to almost total control (co-operative housing exempted).

Under the new system, the Government has to pay that part of rents which tenants refuse to pay. A system that means that a majority of 4,700,000 Swedes, living in farm houses, single family houses and co-operative houses, through their taxes, have to pay part of the housing costs for a minority of 3,600,000 Swedes living in rented houses.

As the members of the minority are as well-to-do as those of the majority, no social reasons can motivate the system. From this you may conclude, that the majority in the future will resist big government subsidies to the minority. Such resistance will mean inadequate funds for maintenance unless tenants pay market rents. Otherwise gradually deteriorating accommodation, growing slum areas and declining quality of life for the dwellers in rented houses would result.

In this system one of the parties of the housing market, the tenants, is exploiting not only the taxpayers in

common, but most of all, the other party, the landlords. To be sure exploitation like all immoral acts has general harmful effects. Not only do the exploited have to suffer, but the exploiters, too. The two parties in a market are like Siamese twins with a common circulation. Any party trying to exploit - blood-tap - the other one, is bound to suffer himself.

NOTES

1. *Svensk sparbankstidskrift*, No. 2, 1948.
2. From the minutes of the Congress of the Swedish Real Estate Owners' Association in Malmo.
3. *Svensk sparbankstidskrift*, op. cit.
4. 'Proximate Future of Sociology: Controversies in Doctrine and Method', *American Journal of Sociology*, May 1943, p.516.
5. 'Britain Must Put Her House in Order', *World Review*, December 1951, p.13.
6. Alf Johansson in *Ett genombrott*, 1944 (a dedication volume in honour of Gustav Moller, Minister of Social Affairs).
7. *Dagens Nyheter*, 15 May 1948.
8. *Handelstidningen*, 16 December 1947.
9. 'Truth and Relevance at Bay', *American Economic Review*, December 1949, p. 1,274.
10. *The Political Economy of the New Left*, 1970 (Harper & Row, 1972). Lindbeck, a professor of economics in Stockholm is, like Professors Oskar Lange and Abba P. Lerner, both a socialist and (partly) a supporter of a market economy.

Chapter 4

Rent Control: The United Kingdom Experience

Michael H. Cooper
& David C. Stafford

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I. INTRODUCTION

Since rent control was first introduced in the United Kingdom as an emergency measure during the First World War, it has been an important and highly controversial component of housing policy.[1] Applied initially as an *ad hoc* wartime measure, the succession of Rent Restriction Acts during the next forty years attest to the then political view that rent control was a necessary, albeit temporary, imposition which could be repealed at the appropriate moment. This moment never emerged and even as late as 1954, landlords were only able to raise rents by a limited amount provided compensating repairs to property were undertaken. It was only under the Rent Act 1957, that an element of decontrol was finally permitted. This Act provided for rent increases for some 5 million controlled tenancies and block decontrol of properties with high rateable values and those properties falling vacant and re-let. Both this Act and its intentions were short lived, for many of the original provisions were never actually implemented and no further measures of decontrol enacted.[2] The Rent Act 1965 provided both the basic and permanent framework for the present control of rents with the introduction of a formal rent regulation procedure applied to most of the properties decontrolled in 1957. The 1965 Act embodied the notion of 'fair rents', new security of tenure provisions, and a statutory control system

for future regulation of rents. Since 1965, rent control measures have been progressively extended and following the introduction of the Rent Act 1974, nearly all permanently rented private dwellings are now subject to rent regulation and security of tenure provisions.

The privately rented housing sector embraces a number of characteristics relevant to subsequent analysis.

1. Size of the market

In 1914, about 90 per cent of the total stock of 7.5 million dwellings were let by private owners. During the inter-war period, the proportion of rented housing fell at an increasing rate to about 60 per cent in 1939. This relative decline was mainly due to the rapid increase in owner-occupied and local authority housing, for the absolute net decrease in privately rented housing was only of the order of 0.5 million.[3] While 1.5 million houses were sold for owner-occupation, nearly 1.0 million new or converted houses were added to the private rented sector during that period. Since that time, both the proportion and absolute size of the stock have fallen dramatically, so that by 1977 the proportion was about 15 per cent and accounted for only just over 3 million dwellings and provided housing to some 20 per cent of all households. Sales for owner-occupation have been important but in contrast to the inter-war period, there have been only 0.4 million new or converted houses added to the private rented sector.

2. Landlords and tenants

Only very limited aggregate data exists on the types, age, and incomes of landlords and tenants. According to the 1971 Census, there was a wide diversity of households in rented housing and a marked contrast in types of tenant in furnished (resident and non-resident landlords) and unfurnished (regulated and controlled) tenancies, as defined under the 1965 Rent Act and discussed later. Tenants in the unfurnished sector were typically elderly, on low incomes, and had occupied their homes over many years. By contrast, the furnished sector comprised tenants who were typically young, single, mobile and with above average incomes for their age groups. A recent sample survey by Paley[4] in 1976 of selected local areas of England and Wales containing more privately rented households than owner-occupied households, revealed that landlords fell into several distinct groups: resident landlords 12 per cent, non-resident landlords 35 per

cent, companies 25 per cent, charities and housing associations 15 per cent, non-charitable trusts and executors 6 per cent, and public bodies 7 per cent. Compared with individual landlords, corporate and other organisational landlords each tended to own a number of premises. Different types of landlord had different motivations for letting and Paley detected three broad groups: (a) lettings made by resident landlords were regarded as part of the landlord's own home and they were not in general looking to the rent received as an economic return on the value of property occupied; (b) lettings made by housing associations (eligible for public subsidy), public bodies and charities were regarded as provision for those in need or for employees and again, no economic return on property occupied was sought; and (c) lettings made by non-resident individuals and companies (in total over 60 per cent of landlords) were in general viewed in terms of an economic investment. These landlords commonly felt that an adequate rent should cover a return on the value of the property and very few considered the 'fair' rent received as adequate.

3. Age and condition of dwellings

According to the 1971 England and Wales *House Condition Survey*, 70 per cent of privately rented dwellings were built before 1919 compared with less than 35 per cent of the owner-occupied and less than 4 per cent of the local authority housing stock. The majority of the remaining 30 per cent of privately rented houses were built in the inter-war period. Some 40 per cent of privately rented houses lacked one or more basic amenities, 30 per cent were in disrepair, and 20 per cent were statutorily unfit for habitation.

4. Geographical distribution

The geographical distribution of the privately rented sector is uneven and tends to be concentrated within the larger inner city areas. London alone accounts for over 25 per cent of privately rented dwellings and about 37 per cent of all households in furnished dwellings.[5] A number of the larger University cities contain a relatively high proportion of privately let dwellings.

II. THE PRESENT LEGISLATIVE FRAMEWORK

The Rent Act 1965, was a major influence on the form of supply of rented accommodation between 1965 and 1974 for it created two separate markets for privately let accommodation as a result of the vital legal distinction between unfurnished and furnished housings. Lettings by private landlords of unfurnished dwellings with a rateable value at the time not exceeding £400 in Greater London and £200 elsewhere were to become regulated tenancies and subject to 'fair rent' registration and security of tenure. This security of tenure provided for a regulated tenancy to be transferred **twice** to members of a tenant's family at his death. The 'fair rent' was to be determined by Rent Officers and, if subject to appeal, determined by a local Rent Assessment Committee. In fact, the 1965 Rent Act distinguished three separate categories of rented accommodation - the regulated unfurnished market, the unregulated furnished market, and the old controlled housing - which was to be gradually phased into the new regulated sector.

Criteria for 'fair rent'

The determining criteria laid down for the assessment of a 'fair rent' were of critical consequence for rental housing:

> (a) In determining for the purpose of this Act what rent is or would be a fair rent under a regulated tenancy of a dwelling house, regard shall be had, subject to the following provisions of this section, to all circumstances (other than personal circumstances) and in particular to the age, character and locality of the dwelling house and to its state of repair.
>
> (b) For the purpose of the determination it shall be assumed that the number of persons seeking to become tenants of similar dwelling houses in the locality on the terms (other than those relating to rent) of the regulated tenancy is not substantially greater than the number of such dwelling houses in the locality which are available for letting on such terms.

Under (a) a 'fair' rent is determined by reference to the attributes of the property and not the financial or personal circumstances of the tenant. Indeed, the ability of the existing tenant to pay his rent, i.e. his personal circumstances, is specifically excluded from consideration. Under (b) the scarcity value of the accommodation is to be

ignored. In other words, for the purposes of valuation, the number of dwellings in the locality is assumed to be equal to the number of tenants seeking accommodation irrespective of what they are prepared to pay. The intention would appear to be that only 'abnormal' scarcity should be ignored and the rent set at a level where all 'need' is met. In the context of a perfectly competitive market, absence of such 'scarcity' would be achieved in the long run at the equilibrium level. However, the implication of the above interpretation is that, unless long-run equilibrium assuming a perfectly competitive market is already achieved, the 'fair rent' is permanently below the market clearing rent and conditions are created whereby there is no incentive for landlords to increase the supply of accommodation. Moreover, the introduction of rent allowances in 1972 for those families on low incomes may be interpreted to mean that a 'fair rent' is a rent which families **can afford to pay.**[6]

Under the Rent Act 1974, the distinction between furnished and unfurnished tenures was abolished as the provisions of the Rent Act 1965 were applied to furnished tenancies. While the Rent Act 1974 was originally conceived as a way of controlling the relatively free market of furnished tenancies the effect of the legislation was to create new loopholes.[7] No longer was the legislative distinction between furnished and unfurnished accommodation to be the determinant for regulatory purposes, but since 1974 it has rested upon the residential status of the landlord. Specifically, that a resident landlord can, subject to certain conditions, be exempt from full control. Nearly all other accommodation which is let is now subject to both rent regulation and security of tenure provisions. The only exemptions are in cases of bed and breakfast accommodation, flats for letting to students by recognised educational institutions, and accommodation primarily used for holiday letting purposes. This legislation has recently been consolidated in the Rent Act 1977 and there is little doubt that the private rented sector in the U.K. is practically unique in having so much complex legislation formulated and implemented by successive Governments on the basis of either pure political dogma or unsubstantiated conventional wisdom. Indeed, the increase in the size and complexity of rent control has been inversely related to the absolute and relative significance of the private rented housing sector in the United Kingdom. Apart from general data derived from the quinquennial Census, there is very little accurate information on the composition of the rented sector which

could be employed to either effectively condemn or condone policy to date. The very few recent studies that have been undertaken in the U.K. have examined the ownership characteristics of the rented sector in Lancaster[8] and Edinburgh[9] and recently Maclennan[10] has examined the short-run supply effects of the Rent Act 1974 in Glasgow. There is little evidence of any monitoring by Government of the effects of the many changes in legislation and no consistent or comprehensive published Government data on rent levels (apart from aggregate data on registered rents), vacancy rates, or on the composition and income of either tenants or landlords.

III. GOVERNMENT POLICY OBJECTIVES

In 1977, the Labour Government announced its intention to review the workings of the Rent Acts and published a consultative document on *The Review of the Rents Acts*. The document included a number of objectives which the Government argued had to be met in the submission of any new proposals which sought a reversal of the decline in the number and quality of privately rented housing:

(a) to safeguard the interests of existing private tenants;

(b) to ensure that fit private rented houses are properly maintained and kept in repair;

(c) to promote the efficient use of housing and to encourage, for example, the letting of property which might be available for only short lets;

(d) to ensure that the methods and criteria for the determination of rents are tailored to meet the difficulties faced by landlord and tenant;

(e) to simplify the law on private renting and to make for a speedier and more effective resolution of landlord/tenant disputes; and

(f) to provide for a legislative framework which maintains a fair balance between the interests of tenants and landlord so that private rented accommodation can contribute effectively to meeting housing needs and choices whilst evolving into social forms involving, and acceptable to, existing landlords and their tenants.

This Review was never published before the defeat of the Labour Government in 1979. The new Conservative Govern-

ment has not, to date, either repudiated or amended these objectives but has suggested that the security of tenure provisions at least may be amended in future legislation. It is clear, however, that the new Government is at least committed to the encouragement of an increased supply of rented accommodation.

Government and housing

Government attempts to increase the supply of rented accommodation stem primarily from the considerable existing financial commitment to housing and the inability of Government to increase current levels of provision. The growth and cost of housing programmes for both local authority and housing association housing has been considerable in recent years[11] and now represents nearly ten per cent of total public expenditure. Notwithstanding this growth of expenditure, the rapid increase in homelessness and the present record levels of waiting lists for local authority housing suggests that a large group of individuals and families continue to face problems of access to housing.

Before a theoretical analysis of the notion of a 'fair' rent and the policy choices facing Government are explored, some consideration should be given to the mutual compatibility of Government objectives in the private rented housing sector and additional aspects which appear to us to seriously militate against either the stability or expansion of the sector while rent control exists. First, it is frequently argued by adherents to the maintenance of rent control that it contributes to a higher general housing standard. This appears somewhat paradoxical for housing consumption depends upon the stock of existing dwellings. If rent control is removed, the quantity of rental housing may well be reduced, but actual overall consumption of housing, at least in the short run, would not be affected since the supply is relatively inelastic. In fact, it is the imposition of rent control which results in an increase in consumption by tenants of other goods and services as a result of the income and substitution effects and the spill-over of unsatisfied demand in the rented housing sector to other markets. Moreover, rent control diminishes the incentive to 'ration' accommodation in that it encourages under-occupation by families who would, in a free market, either sub-let or move to smaller dwellings. Secondly, a rent which denies a full economic return will neither encourage new construction nor lettings from the existing stock. During periods of rapid

price inflation this situation is aggravated and will affect the repair and maintenance of the existing stock. In the U.K., rent reviews can only take place at three year intervals and there is a considerable delay before rents can rise to compensate for price increases. If the compensation is insufficient, landlords will have every incentive to reduce the housing services provided and the resultant under-maintenance and repair will be further aggravated by the present security of tenure provisions that exist. Thirdly, rent control has implications for income distribution since a tenant who pays below market rent is receiving a subsidy and hence a redistribution of income from landlord to tenant. No quantitative statement on the welfare implications of this outcome can be made in the absence of accurate data on the incomes of tenants and landlords. What can be said, however, is that the present redistribution of income is clearly random and indeed raises the issue of the justification of subsidy, per se, and whether it should be borne by the Government or by landlords. Fourthly, rent control militates against mobility of labour. Tenants will not only be reluctant to vacate a controlled tenancy but will have great difficulty in finding comparable housing elsewhere in conditions of excess demand. Similarly, control will militate against new entrants to the market, and recent evidence suggests that search costs for accommodation can be considerable.[12] Finally, given Government objectives and the market constraints and characteristics of rented housing, it can be argued that a return to an uncontrolled market, unless phased over many years, is not likely to prove at all acceptable to any Government. At the other extreme, proposals for the municipalisation of the rented sector[13] are unlikely to be politically acceptable or, indeed, financially feasible.

What is feasible, however, is the development of policies which accept, at least in the short run, the reality of rent control and attempt, through fiscal measures to at worst retain the current stock of houses intact and, at best, revitalise and increase the supply of rented housing.

IV. AN ECONOMIC INTERPRETATION OF A 'FAIR RENT'*

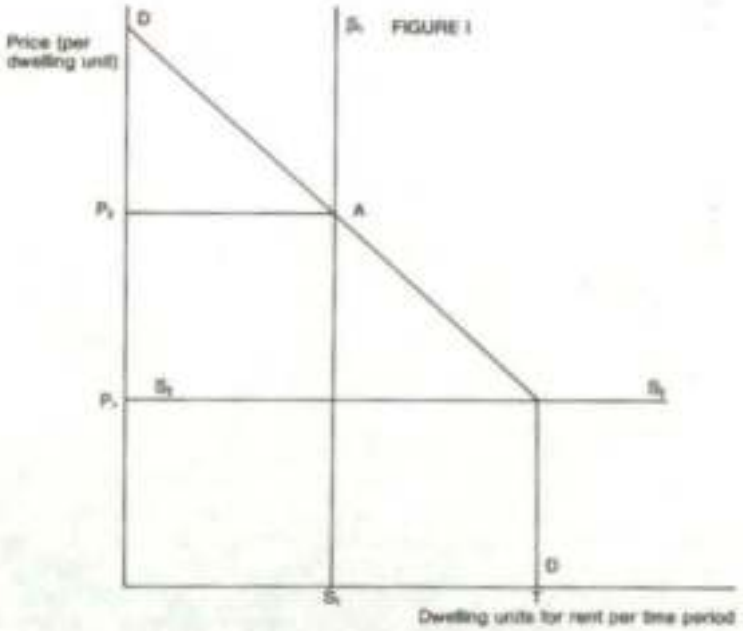
While the notion of a 'fair rent' is an evident central component of U.K. housing policy, its theoretical derivation and relationship to economic forces is obscure.

The model represented in Figure 1, embraces the following assumptions:

(a) housing units are homogeneous with the same site value and each family can only possess one dwelling unit.

(b) OS_1 is the actual stock of housing to rent and S_1S_1 is a perfectly inelastic short-run supply curve.

(c) S_2S_2 is the long-run supply curve assuming a perfectly competitive market with all firms having the same long-run average cost curves and no technological or pecuniary externalities.



* Editor's note: This section is of a fairly theoretical nature and may be omitted by the lay reader.

In a perfectly competitive market, P_1 is the 'fair rent' because it would be the rent in the absence of scarcity under constant cost conditions, i.e. the long run perfectly competitive equilibrium rent level. Thus P_1, the 'fair rent', is defined as the level where, in the absence of abnormal circumstances, need would be equated to supply with neither the landlord nor tenant penalised. Under this determination of the 'fair rent', the Government assumes that OT families are both ready and able (at least with assistance through rent allowances) to pay a rent of P_1 for some standard of accommodation of given quality and location. In this context, the rent of P_1 is fair to both landlords and tenants and the demand curve DD will, under these assumptions, have a kink which will coincide with the 'fair rent' P_1. Demand is therefore perfectly inelastic up to and including the fair rent level on the earlier assumption that people are only able to possess one dwelling unit and are not able to respond to low prices by demanding to rent more than one unit.

An initial situation of disequilibrium is assumed in the model with P_1 rent prevailing as the 'fair rent'. While OT families are ready and willing to pay P_1, supply in the short run is only OS_1. Therefore, in the short run at least, equilibrium can only be achieved at a rent of P_2. In the long run, assuming a perfectly competitive market, new entrants would ensure that a rent of P_1 would ultimately be attained and OT families housed.

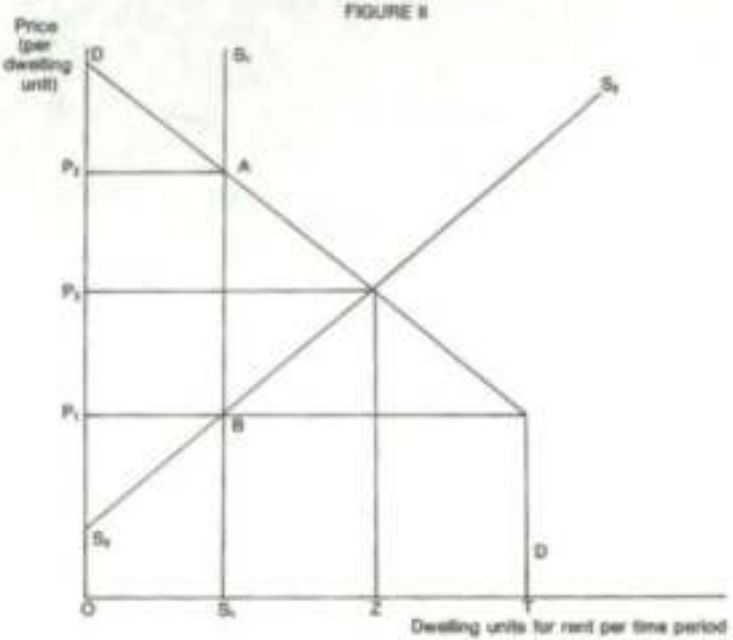
In figure 2, the more realistic assumption that long-run supply is subject to increasing costs is made and the supply curve S_2S_2 slopes upwards from left to right. Since no obvious long-run solution presents itself, given the control of rent of P_1, the State is faced with a number of possibilities but they all pose difficulties.

A. Control rents at P_1

Rent control at P_1 would represent a perpetuation of the present policy of 'fair rents' and theoretically implies the transference of P_1BAP_2 suppliers' surplus to consumers and prevents them 'exploiting' the short-run shortage. While the rent is 'fair' in that it fully meets the long-run supply price of OS_1 units, it in no way provides an incentive to suppliers to increase supply, even in the long run. Moreover, it is potentially unstable, for landlords are well aware that there are OS_1 people willing to pay a rent of P_2 or more and will accordingly attempt to circumvent rent legislation. Moreover, once the rent is controlled at P_1 it will be politic-

ally difficult to remove the control for there will be an excess demand of S_1T (OT families are willing and able to pay the 'fair rent') and a queue will emerge.

FIGURE 8



In the case of those landlords who attempt to evade the law, some of the enhanced consumer surplus will find its way back to them. A black market will emerge with such practices as key-money and payment for fixtures and fittings. Some families are even willing to pay in excess of a rent of P_2. Landlords will also attempt to increase utility from rationing by prejudice (colour, creed, a ban on children and pets, etc.) in order to reduce the potential risks of being suddenly subject to rent regulation. Nevertheless, without Government provision of housing, S_1T families will still go homeless or be forced to share housing in extended family groups.

B. Control rents at P_3

A 'fair rent' set at P_3 would represent market equilibrium in the absence of the 'temporary' supply constraint. Moreover, it has the advantage that it offers landlords some inducement

to expand supplies in the long run under increasing cost conditions and consumers are not being asked to pay more than the 'normal' long-run cost. On the other hand, a shortage of S_1Z units would still remain with S_1T homeless in the short run and ZT in the long run.

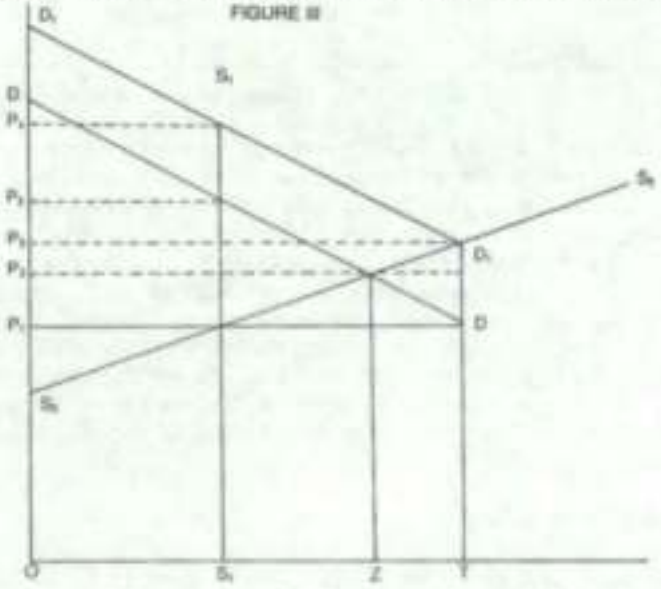
C. Permit rents to rise to P_2

This would mean effective abandonment of 'fair rents' in the short run, given the expectation that in the long run equilibrium would be achieved at P_3. In the short run, landlords would gain considerable surplus but, given the freedom of entry, there would apparently be a strong incentive to supply OZ units. No rationing other than the ability and willingness to pay is necessary or probable but, even in the long run, there would remain unmet need of ZT.

D. Subsidise demand

Under this strategy, the State could abolish rent controls but accept that 'needs' outstrip ability to pay and so subsidise demand either at a flat rate per unit of housing or ad valorem subsidy. In Figure 3, the removal of controls at P_1 and the

FIGURE III



subsidising of demand by P_2P_4 per unit would, in the short run, increase rents to P_4. In the long run the shift of the

demand curve to the right would yield a new equilibrium level which coincided with need of OT units at the rent of P_3. Both DD and D_1D_1 demand curves will 'kink' at OT units for the same reasons as given under Figure 1, except that in the case of D_1D_1 it is assumed that every family with assistance can pay a rent of P_3. Demand, therefore, is perfectly inelastic up to and including the 'fair rent' level of P_3.

The State would pay the difference between the tenant's payment of rent of P_1 and the landlord's receipt of P_3. The relative gains to the tenant and the landlord will depend upon the elasticities of supply and demand. In figure 3, the tenant is now paying P_1P_3 less than he would have in the former equilibrium position and the landlord is receiving P_3P_3 more. The greater the elasticity of supply and the lower the elasticity of demand, the greater will be the relative gain to the tenant from any given subsidy and vice-versa. In the case of an ad valorem subsidy, the gap between the two demand curves would widen or narrow depending upon whether the subsidy was progressive or regressive.

V. CONCLUSIONS

Clearly data on the actual position and shape of the demand and supply curves for housing to let is critical, but there has been little rigorous analysis of elasticities of demand and supply undertaken in the U.K. U.S. studies[14] calculate elasticities of demand of the order of 0.9 and price elasticities of supply in the range of 0.3 and 0.7 in free market conditions. Of particular relevance in the U.K. will be the future status of the landlord, government controls, and returns on alternative investments. Although this paper has concerned itself with analysis of the effects of rent control, it cannot be deduced that it has been the principal or even a major factor in explaining the contraction of the privately rented housing sector. Many tenants have undoubtedly been attracted out of the private rented sector into owner-occupation through aspiration and rising real incomes. Moreover, there has been 'unfair' competition from the heavily subsidised local authority housing sector. Other factors affecting the decline of the privately rented sector might include taxation policy in respect of both landlord and tenant, urban clearance and redevelopment programmes, and the general political uncertainty surrounding the rented sector during the post war period.

Future projection of households seeking privately rented accommodation will be influenced by the tastes and

willingness of people to live in extended family groups, future marriage and divorce rates, and the availability, conditions and price of housing in alternative sectors, especially the Government subsidised local authority and housing association markets. There is little doubt, however, that many families will continue to be unable to secure owner-occupied housing and remain ineligible for local authority housing.

The recent consolidation of existing rent legislation in the Rent Act 1977 may nevertheless be predicted to strengthen the uncertainty relating to a landlord's ability to repossess or dispose of property when desired, and have an important impact on investment, maintenance and letting decisions. Paley's survey[15] revealed that of those landlords interviewed, 61 per cent said they would re-let a vacancy occurring at the address and 49 per cent said they were prepared to re-let if the whole building became vacant. Only 18 per cent of landlords interviewed in 1976, expected their holdings to increase during the next three years and these landlords were mostly charities or subsidised housing associations. Where a decrease in the landlord's lettings was expected, the most common reason, given in 44 per cent of cases, was that it was no longer economic to let accommodation. The next most common reason, given in 15 per cent of cases, was that landlords felt there was too much restriction in the form of legislation or officialdom generally. Landlords, when asked to select the one most helpful change to existing legislation, seemed most concerned about rent levels - 58 per cent chose higher rents, rents linked to costs, less tax on rent income or a more frequent review of rent levels.

The risks associated with the present legislation can therefore induce some landlords to cease letting at the earliest opportunity while continuing landlords may attempt to contain risks by letting to more transient groups and adjust the level of housing services provided. Either one of these effects is sufficient to militate against the Government's major objectives - the provision of a stable supply of furnished accommodation at a decent standard with full security of tenure for 'poor families' within that sector.

All these demand and supply influences which have been studied serve to emphasise that the models examined in this paper make simplistic assumptions regarding the shape of both the demand and supply curves, and the homogeneity of the units traded. Moreover, it assumes that the State is in a position to identify the demand and supply relationships at different rent levels. This paper has, therefore, explored

just one interpretation of a 'fair rent' and it is clear that any economic interpretation is fraught with difficulties for the legal definition provides considerable scope for highly subjective interpretations.

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PART II

RENT CONTROL IN AUSTRALIA

Chapter 5

Australia: History and Overview

Robert Albon

Australia: History and Overview

Robert Albon

I. THE PRE-1939 SITUATION

New South Wales

Australia's first experience with rent control was almost certainly the New South Wales *Fair Rents Act*, 1915.[1] The history and operation of this Act are discussed in the paper by H.V. Evatt included in this volume. Evatt expressed qualified support for the New South Wales legislation on the basis that the adverse effect of the Act ('adding its quota to the causes of the housing shortage'), was possibly outweighed by its effect of keeping 'rents at a reasonable rate during an exceptionally difficult period, and acted as a valuable deterrent to the building "profiteer".'[2]

The New South Wales Act was only partial in its coverage, excluding leases of three years or more or where the rent was more than three pounds per week. The Act set out a rigid formulation for the determination of rents. An 'opportunity cost' was calculated by applying an interest rate to the building's capital value and adding the costs entailed by a list of specified outgoings such as rates, land tax, repairs and maintenance, insurance, depreciation and a vacancy allowance. Any 'fair rent' so determined (indeed, any rent falling within the ambit of the Act) was not to exceed the actual rent prevailing as of the first day of 1914, except in special circumstances. The landlord had to show reasonable cause for ejecting a tenant.

The Act attracted considerable attention, both in Australia and abroad. An American, M. Whitman writing in 1925 was quite impressed with the legislation, suggesting that it 'went further than that in this country [the United States] during the war [because] fair rent courts were established and definitely instructed with reference to the net returns which might be allowed to landlords'.[3] Evatt reports on some of the Australian commentaries on the Act including criticism by the long-since defunct Inter-State Commission, and an ex-Premier of New South Wales who suggested that any person building rental housing in future 'deserved to be sent to Callan Park, a well-known Sydney lunatic asylum.'

The *Fair Rents (Amendment) Act*, 1920, made some minor amendments to the New South Wales legislation, and outlawed side payments such as 'key money' and discrimination against tenants with children.

A 1926 amending Act explicitly set out a series of grounds on which an eviction could be made. These included failure to pay rent, being a nuisance to neighbours, using the premises for immoral or illegal purposes, and reasonable requirement by the owner for personal occupancy of the premises.

A non-Labour Government was elected in 1927, and rent control was an election issue. The leader of the new Government, Mr Bavin, pledged substantial decontrol in his policy speech. The 1928 *Fair Rents (Amendment) Act* provided that the legislation should cease to have any effect after July 1, 1933. Dwellings built during or after 1928 were exempted and the 1915 standard rent was dropped. The duration of rent determinations was reduced to one year. The *Fair Rents (Amendment) Act*, 1915-1928 was completely removed from the statute books in 1937.

In the meantime, the depression had intervened leading to two early Acts - the *Reduction of Rent Act*, 1931 which reduced rents by 22.5 per cent though it had allowed for voluntary reductions since June 30, 1930; and the *Ejectments Postponement Act*, 1931 which among other things outlawed 'squatting'. The *Landlord and Tenant (Amendment) Act*, 1932 also dealt with the postponement of ejectments and the reduction of rents.

There was not, for any practical purposes, any form of rent control in New South Wales on September 3, 1939, but the War was soon to change that.

Victoria

Victoria's first brush with rent control was its 1938 *Fair Rents Act*. The Housing Investigation and Slum Abolition Board in it *First (Progress) Report* (1938) had expressed some dismay that the June, 1937 basic wage increase had led to rent increases. According to the Victorian 1956 Board of Inquiry, referring back to this 1937 experience, 'some machinery is . . . necessary to ensure that landlords do not, without justification, use their dominant position to deprive tenants of the benefits of increased income'[5]. The *Report* of the Housing Investigation and Slum Abolition Board led to the 1938 Act.

The 1938 Act was limited to houses with capital value of £800 or less in Melbourne, Ballarat, Hamilton and Shepparton. Either a landlord or tenant could apply for a determination, but rents could not be determined at more than 10 per cent of current capital value and a determination could remain in force from six months to two years. Those who drafted the 1938 *Fair Rents Act* of Victoria realised that it was useless to control rents without also controlling evictions, and so the 1938 Act allowed evictions on such grounds as: failure to pay rent; failure to take reasonable care of premises; using premises for illegal purposes; and reasonable requirement by the lessor of the premises for occupation by himself or for a close relative. At least 28 days' notice had to be given to secure an eviction.

Queensland

According to Butlin in his book *War Economy* the 'Queensland Government had had (in 1939) a system of rent control since 1920, and this had been tightened up in 1938.'[6]

II. RENT CONTROL DURING THE SECOND WORLD WAR

After the outbreak of war, the question of rent control was discussed at the September 1939 Premiers' Conference. The outcome of the Conference was the introduction of *National Security (Fair Rents) Regulations* by the Federal Government which gave the States executive power to freeze rents at the August 31, 1939 level. States could set up Fair Rents Boards to make determinations at the request of either landlords or tenants.

Prescribed grounds for eviction were failure to pay rent, failure to take reasonable care of the premises, use of

the premises for immoral purposes, being a nuisance to neighbours, sub-letting at a profit, or sale of the premises with vacant possession. According to Butlin, these Regulations 'gave landlords considerable advantage as compared with tenants'.[6] At the end of 1939, the rent freeze ceased, and only those who had sought a determination had 'protection' under the Regulations. Butlin also reports, however, that 'many tenants would prefer to pay higher rent than risk eviction and bad relations with their landlords'.[7]

Three States, Tasmania, Queensland and Victoria (which suspended its 1938 *Fair Rents Act*) adopted the 1939 Regulations, but New South Wales decided to introduce its own legislation, the 1939 *Fair Rents Act*, which applied only to dwellings with rents of less than £3.10.0 per week.

'Fair rents' can be set in one of three ways - a mechanistic basis, a flexible system or a mixture of the two. The New South Wales *Fair Rents Act* of 1939 employed a mechanistic basis of rent-setting where the legislation provided the 'ingredients' (the factors to be taken into account) and the 'recipe' (how the factors were to be combined, as in a formula). The tribunal was to use a prescribed interest rate and an ascertained capital value to calculate a money return and was to add to this, specified outgoings, depreciation and an allowance for vacancy. This mechanistic formulation contrasts with the 1948 New South Wales' *Landlord and Tenant (Amendment) Act*, which provided only a set of ingredients to which the controller was to have 'regard to'. The way the factors were to be combined was not specified.

South Australia froze rents as at September 1, 1939 and allowed rent increases only where there were improvements or structural alterations. Western Australia pegged rents at the August 31, 1939 level and allowed increases only by appeal to the Supreme Court for premises with values in excess of £2,000. Eviction controls similar to those in the Commonwealth Regulations were imposed in both states.

New Federal Regulations were introduced in March, 1940. As before, there was no compulsion for the states to adopt them. Rents were frozen at the December 31, 1940 level and a determination from a Fair Rents Board was required to vary a rent. Eviction provisions remained substantially as they had earlier. Queensland, Victoria and Tasmania continued with the Federal Regulations and South Australia and Western Australia had their own rigid rent and eviction control laws. New South Wales' *Fair Rents Act* was a matter of some concern to some commentators as its legislation was relatively weak.

Labor Party in power

After the Australian Labor Party came to power in 1941, new *National Security (Landlord and Tenant) Regulations* were introduced and could be imposed compulsorily on any State and in the Territories. The eviction provisions were considerably tightened up and applied universally. The rent control provisions froze rents at the August 31, 1939 level unless altered by a determination (to be based on such things as capital value, the Commonwealth Bank overdraft rate, rates, taxes, insurance, repairs and maintenance spending, rents on comparable premises, any services provided, justices and merits of the case, and hardship). These regulations applied immediately (November 1941) in New South Wales, replacing the existing weak controls, and subsequently were adopted in the Australian Capital Territory (December 1941), Tasmania (February 1942), Victoria (March 1942), Queensland (April 1942) and the Northern Territory (January 1943). Western Australia and South Australia continued their own legislation without interference from the Commonwealth as it considered the state legislation to be adequate.

A new set of Commonwealth Regulations was introduced in June 1945, and one of its main features was the extension of controls to 'shared accommodation'. Small changes were also made to the eviction provisions including the requirement for a Magistrate to have regard to alternative accommodation in considering whether to issue an order to quit. In 1946 and 1948 other minor amendments occurred, but the situation remained substantially unchanged. The Regulations ceased to exist entirely in 1948.

The effect of the Regulations had been to keep rents virtually static over the period from the beginning of the War until 1948. During the war itself, rents (on 4 and 5 room houses) rose only by 1.0 per cent while the 'C' Series Index* as a whole rose 22.3 per cent over the same period. It was known, however, that illegal payments such as 'key money' and above-rent sums were quite common.

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* The 'C' Series Retail Price Index was the forerunner of the current 'Consumer Price Index' (CPI). The C Series index had base 1923-1927 = 1,000. The rent component encompassed rents of 4 and 5 room houses.

Verdict of economists

The economists' verdict on the controls was generally favourable. E. Ronald Walker, a former Professor of Economics at the University of Tasmania, expressed strong support for wartime rent controls. He saw the object of such controls as being to 'avoid a rise in general living costs and to prevent profiteering'.[8] In his study of the wartime rental market in Melbourne, Wilfred Prest contrasted the situation in 1939 with that at his time of writing (1945). In 1939 'there was no scarcity of houses . . . in the sense that we know it today'.[9] This was despite a high level of post-depression demand. 'The rise in rents must . . . have served as a brake upon demand, compelling some of these seeking better homes to revise their ideas, restraining some who contemplated housekeeping for themselves, and sometimes, perhaps, inducing the postponement of marriages'.[10] Prest then refers to the 'pegging' of rents in 1939 which 'prevented any further application of the brake which higher rents had previously imposed on the expansion of demand . . . Thus demand and supply have ceased to be adjusted to one another by the operation of the market. Demand exceeds supply and even the normal interchange of houses has come to depend on personal contacts . . .'[11] Surprisingly, Prest then states that 'this does not constitute a criticism of the war-time control of rents and property values'.[12] The pressures of wartime demand (argued by Prest to be mainly due to rising incomes) were:

> too powerful to be held in check by any normal increase in rents and property values. A rise in rents of the required magnitude would have borne particularly heavily on all those whose incomes did not rise proportionately and particularly on the families of service men. This in itself is sufficient justification of the control of rents and property values.[13]

Another commentator on the wartime regulations was Ronald Mendelsohn who gives two completely different views In one study he argued that measures to regulate rents 'can have no effect on the basic level of rents, which is determined by the demand for houses and the cost of producing them. In the long run . . . rent restriction has a bad effect, because it discourages new building and creates a housing shortage'[14]. However, in another study in the same year he argued that

the 'regulation can . . . be justified on the ground that they have prevented a probable future price rise' and that 'rent control must be considered as an integral part of general housing policy . . .'[15]

III. THE END OF COMMONWEALTH REGULATIONS

As of early 1948, the Commonwealth Landlord and Tenant Regulations applied in all States and Territories except the two most westerly States which had their own legislation. This soon changed with the removal of Commonwealth power to regulate rents and prices.

The *National Security Act* lapsed at the end of 1946 and rent/eviction controls were included under the *Defence (Transitional Provisions) Act*. A successful challenge to this legislation in the High Court led the Federal Government to seek a change in the Constitution through a Referendum to retain permanent power over rents and prices. This Referendum, held in May 1948, was lost by the Federal Government and the power to legislate in this area was consequently restored to the States in August 1948. The Commonwealth retained the power to control rents and prices in the Territories.

South Australia and Western Australia continued their own legislation after 1948 while the other States all adopted legislation containing eviction provisions virtually identical to those in the wartime Commonwealth Regulations. The rent control provisions were also very similar, except in Queensland where the *Landlord and Tenant Act* (1948) controlled only rents of houses, whereas the other State Acts also encompassed flats.

The Australian Capital Territory's *Landlord and Tenant Ordinance* was introduced in 1949. It carried on the provisions of the Commonwealth Regulations except for one important difference; all premises built or leased after March 1, 1945 were exempted from rent controls save for a 'voluntary' fair rent determination which could be sought by either landlord or tenant from the rent controller, but was binding once made. Eviction controls were continued.

It is important to note that all States, being completely free to legislate in the area of landlord and tenant, decided to continue with systems of rigid rent and eviction controls.

Verdict of economists

Commentators on the rent control issue at the time of the transition from Commonwealth to State legislation were conspicuous by their absence. In 1948 R. I. Downing published an *Economic Record* article on housing policy in which he completely ignored rent control, while in his book of the same year, *Housing and Employment* it was only mentioned incidentally.[16] This is a little difficult to understand in the context of blanket rent control of privately rented dwellings constituting some 40 per cent of the total dwelling stock. In his review of the book, H.W. Arndt took Downing to task for his neglect of rent control. Arndt outlined some of the problems associated with rent control and suggested that:

> a choice will have to be made between further injury to landlords, subsidisation of abnormally low housing expenditure out of the public purse, or a gradual stepping up of controlled rents. The first two courses seem hardly justifiable; the third will require unusual political courage.[17]

IV. DECONTROL IN THE 1950s

Except for Western Australia, there were five years of State legislation before the first chinks in the armour of rigid rent control appeared. Western Australia was the first State to decontrol, beginning the process in 1951 and completing it in 1954. All States made some moves towards relaxing controls during the fifties, for instance in relation to decontrolling new lettings (Victoria in 1953 and New South Wales in 1954), allowing proportional rent rises (Victoria, Queensland and South Australia) or slowly freeing up evictions (New South Wales). By the end of the decade, three States (Western Australia, Tasmania and Victoria) had all but decontrolled completely while South Australia and Queensland had gone a long way towards decontrol. New South Wales still had a considerable way to go in 1960.

Western Australia's *Increase of Rent (War Restrictions) Act*, 1939-50 was continued after the War by continuance Bills which in some cases incorporated slight amendments. The *Rents and Tenancies Emergency Provisions Act* No 47 of 1951 continued the effects of the former Act, but in a considerably restricted form. This Act decontrolled all new leases, allowed controlled rents to be raised by

up to 20 per cent and put rent determinations on the basis of current capital value less depreciation. The Act was amended in 1953 to the effect that from May 1, 1954, landlords and tenants could negotiate on a rent. Both parties still had recourse to a rent determination based on current values if agreement could not be reached.

Tasmania allowed a 20 per cent rise in dwelling rents in 1950 and additional increases in 1952. At the end of 1955, Tasmania's *Landlord and Tenant Act* lapsed and was not renewed. However, in 1956, new provisions in the *Fair Rents Act* re-introduced elements of control. Even so, Tasmania can be counted amongst those States which had largely decontrolled by the end of the 1950s.

In 1953, Victoria decontrolled all new lettings and all leases on dwellings not let between 1940 and 1954. From the beginning of 1955, all dwellings let in 1940 at £2.10s or more, became subject to an agreed rent and, if no voluntary agreement could be reached, a determination based on current capital value could be sought. Several amendments were made in the 1955 *Landlord and Tenant (Amendment) Act*, which was to operate from mid-1956. Written leases of three years or more could be subject to an agreed rent and dwellings that became vacant could be re-let without an externally determined rent. The base rent (that is, the rent prevailing in 1940) could be increased by up to 25 per cent. The most crucial step came in 1959 when an amendment allowed rents on most dwellings to be fixed by agreement. Failing an agreement, a determination based on current values could be sought. Certain leases of a residual group of 'prescribed premises' still came under legislative protection and rent control provisions. These included, for example, all premises leased between 31st December 1940 and 1st February 1954 which had not been re-let for any time to another tenant, or had become vacant or had been excluded from the protection by an Order of the Governor in Council published in the *Government Gazette*.

In South Australia, an independent committee of inquiry reported in 1951 and as a result, 1939 values were abandoned as the basis for 'fair rent' determinations. The rent-setting body, the Housing Trust, was instructed to use 'current replacement cost, less depreciation' in setting rents. A 22.5 per cent addition to the base rent was allowed in 1951 and this was extended to 27.5 per cent in 1954 and to a full third in 1955. Written leases for two years or more were exempted from control in 1954 and all fixed term leases were exempted the following year. These latter amendments

effectively decontrolled all new leases, whether on new or previously unlet premises or where vacant possession had been attained on previously let dwellings. South Australia entered the 1960s with a fairly mild form of control, similar to that existing in Tasmania and Western Australia.

In Queensland, as in New South Wales, rent control remained more rigid than in the other States. An amending Act of 1957 allowed an increase of 20 per cent in the controlled rent of dwellings which were under lease in 1942, the basis of determination being the 1948 value, which replaced the previously used 1942 capital value. Dwellings first leased after 1957, and premises which were leased after that date, but which had not been leased during the previous three years, were exempted from control. Any other leases made after 1957 were to be free of control if the parties agreed in writing.

New South Wales was the laggard in decontrol. That State spurned the option used in the other States of allowing a percentage increase in all rents. The other five States all moved either to current values or to later year values, at some time during the fifties, but New South Wales persisted doggedly with 1939 capital values as the basis of rent determinations. Nevertheless, it did make three significant changes to its *Landlord and Tenant (Amendment) Act* in the fifties. The first major reform was the exemption in 1954 of all new lettings and of leases which had not been previously let. Secondly, a 1956 amendment allowed decontrol on dwellings where vacant possession had been attained by the voluntary quitting of the tenant or if eviction had occurred on certain grounds. Both of these changes were made by amendments under Section 5A* of the Act. Finally, in 1958, new grounds for eviction were also added.

In the Australian Capital Territory, very little happened in the 1950s or indeed, the sixties. The one minor change was a 1952 alteration which served to include as 'protected persons', those involved in the Korean conflict.

Interest in rent control by Australian economists during the 1950s was minimal. One item by three economists (D. Cochrane, D.M. Hocking and J.E. Isaac) from the University of Melbourne appeared in the Melbourne *Age* of April 15, 1953 and argued for the abolition of rent controls in Victoria. They argued that the shortage of housing was an artificial creation which would be largely solved by the

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* See Chapter 8 by Helen Nelson for further details.

removal of rent control.[18]

V. THE SIXTIES

New South Wales

The big event of the 1960s was the slow decline of rent control in New South Wales. By the end of the decade, rent control was virtually a dead issue throughout Australia. Even where facilities existed, these were very little used. In some States, there were vestiges of the 'old control' manifested by pockets of dwellings still under some form of restriction. Despite this, a reviewer writing from the vantage point of 1970 would have (erroneously, as it transpired) dismissed rent control as a thing of the past.

In New South Wales, there were still 207,000 controlled dwellings in 1960, representing about two-thirds of all private rentals still extant.[19] The State was governed by the Australian Labor Party from 1948 to 1965 and, in 1960, this Government directed a Royal Commission to inquire into the *Landlord and Tenant (Amendment) Act*, 1948-1958. The Commission reported in 1961 and recommended: (i) that rent control be abolished for luxury premises, (ii) a milder form of control for premises remaining under control, and (iii) a 60 per cent rise in the rent of controlled premises. The Commission's recommendations were not accepted.

Rent control nearly lost its teeth in 1964. This was not due to Government action, but rather to legal challenge. In 1963 the Supreme Court of New South Wales confirmed that the Fair Rents Courts should not consider current capital value when making determinations. The 1939 value (or value at construction if built after 1939) was to remain the appropriate value. However in 1964, the High Court of Australia reversed this decision and determinations began to be based on current values. Following an extremely complex series of events this again changed and there was a reversion to the use of 1939 values. This often-cited affair is usually remembered by the 1963 Supreme Court case, *Rathborne* v *Abel*, which began it. Meanwhile, some amendments to the Act had taken place.[20] In 1964, Section 17A was added which allowed landlords and tenants to agree on a rent, if they wished. Soon after came the 'wealthy tenant' provision which meant that if a tenant's income exceeded a given amount (initially $6000 per annum) he could be asked to agree on a rent based on current values, or be decontrolled. Before 1964 it had been possible to get an eviction if it could

be shown that a tenant was better able to provide himself with accommodation than could the landlord. Major amendments were made to the Act in 1968 when inheritance of tenancies was limited to a spouse, sub-letting was made illegal, and other anomalies cleared up.

Queensland

Queensland was the other State which had not substantially decontrolled in the 1950s. Decontrol occurred in 1957 such that only those houses which were let or leased during the three year period ending on December 1, 1957 remained under old control. Until the end of 1970, either the landlord or tenant could apply to a Fair Rents Court for a determination. A Stipendary Magistrate assessed the rent so as to allow a return of six per cent of the capital value after allowing for outgoings, services provided by the lessor, and a vacancy allowance. At the end of 1970 all rent control in Queensland ceased after the amendment of the *Landlord and Tenant Acts*,1948 to 1961 and the enactment of the *Termination of Tenancy Act*, 1970.

The other States

In Victoria, there were still vestiges of control. In addition to a diminishing number of tenancies under 'old control', there remained a facility for setting 'fair rents'. The Rental Investigation Bureau (RIB) could recommend a fair rent determination after a complaint from a tenant. The RIB still operates today, negotiating settlements and recommending some cases to a Fair Rents Board. Fair rent determinations allowed an 8 per cent return on capital value plus an allowance for legitimate expenses by the landlord including rates, land tax, 20 per cent depreciation on furniture and an allowance for agent's fees. Capital value was estimated from a number of sources, including sales of comparable premises.

South Australia retained some 'old control', but with rents based on current values (unlike New South Wales). At the end of 1962 the *Landlord and Tenant (Control of Rents) Act* was replaced by the *Excessive Rents Act* under which a tenant may apply to a Local Court to determine whether the rent is excessive. South Australia has also had, throughout, a *Housing Improvement Act* which allows the control of sub-standard houses. This latter Act is administered by the Housing Trust.

The Australian Capital Territory made no changes to its *Ordinance* in the 1960s. Rent control had however, become a dead issue as the small base of controlled dwellings dwindled and very few new determinations were made under the 'voluntary' system.

VI. THE 1970s

The seventies witnessed something of a revival of controls on the rental housing market. Traditional rent control came and went in the Australian Capital Territory. Some form of controls were also imposed in Darwin after Cyclone Tracy devastated the city on Christmas Day 1974. John Singleton and Bob Howard in *Rip Van Australia* discuss the possibility of a 'natural economic recovery' in Darwin brought about by market forces. They observe however, that the authorities 'imposed rent control, . . . forbade people to repair their own houses, and dithered about letting contracts for the building of new houses'. As a result it 'was over a year before a single new house was built'.[21] In many ways, post-cyclone Darwin can be compared to San Francisco after the 1906 earthquake as discussed by Friedman and Stigler. The contrast with the bureaucratic bungling in Darwin is striking.

Most important however, has been the introduction of a milder form of control in several States. This form of intervention is sometimes given the soft-sell label of 'rental market regulation'. The issues raised by these regulatory activities are considered in Part III of this book.

The Australian Capital Territory

In August 1973, compulsory rent control was re-introduced in the Australian Capital Territory. In many ways, the system was similar to that which prevailed during the war years. Premises that were leased on January 1, 1973 were able to have their rents pegged at the level prevailing at that date, unless or until fixed by a determination. Lessors of premises leased between January 1, 1973 and August 9, 1973 had three months from that date to apply for a determination. Lessors of premises leased after August 9, 1973 had 28 days from the date of the letting to apply for a determination.

The Rent Controller was to 'have regard to' a number of factors in making a determination. The capital value of the premises at the beginning of 1973 was one of these factors. The list of factors is a familiar one except that the Controller was not instructed to take into account the 'justice

and merits' of the case: rent setting was supposed to be more objective. Eviction provisions of the 1948 *Ordinance* were incorporated.[23]

Following a change of government, the *Ordinance* was amended in 1976 and compulsion was removed from the legislation. In addition to making applications non-compulsory and removing rent-pegging until there had been a determination, the 1976 amendments made other changes. A 'voluntary' system of fair renting was restored where determinations, based on *current* values (not at a prescribed date) could be sought by landlords or tenants and were to hold for one year only. Where there was no determination in force, the landlord was required to give notice 90 days in advance of a proposed rent increase. The amended *Ordinance* placed a limit on the amount of a security bond at 4 weeks rent. These changes took the Australian Capital Territory some considerable distance in the direction of the reforms suggested by the Henderson Poverty Inquiry.[23]

The imposition of rent control in Canberra attracted considerable attention from many quarters. The then Real Estate and Stock Institute of Australia published a study of these controls which was thorough and objective and stimulated considerable debate on the issue of rent control.[24] The Priorities Review Staff in its *Report on Housing* condemns Canberra's rent control as it expected controls to 'depress rental investment below what it would otherwise have been'. . . 'benefit a few affluent tenants' . . . 'discriminate against potential low-income or high-risk tenants' and encourage evasion or contempt of the law'.[25]

One of the major effects of controlling rents in Canberra was an adverse effect on renters in the adjacent and uncontrolled town of Queanbeyan in New South Wales. Queanbeyan provided about one-quarter of the rental accommodation in the Canberra-Queanbeyan area, even though it had only about 10 per cent of the combined population. Queanbeyan attracts many of the poorer tenants in the area and rent control in the A.C.T. had the effect of transferring much of Canberra's unsatisfied demand to Queanbeyan and raising rents there in an extraordinary fashion. The relative rent movements are shown in the following Table.

In a very real sense, it can be said that part of the costs of rent control in Canberra were borne by those least able to cope - the poor tenants of Queanbeyan.[26]

Table 1

Quarterly Canberra and Queanbeyan Private Rent Indexes
(December 1973 = 100)

		Canberra	Queanbeyan
1973	June		97.12
	September		98.90
	December	100.00	100.00
1974	March	100.80	100.00
	June	101.40	110.05
	September	101.60	114.29
	December	102.00	118.33
1975	March	102.90	121.17
	June	105.10	123.96
	September	106.20	125.70
	December	107.90	
1976	March	110.90	
	June	115.80	

Sources: The Canberra Index is the 'Rent, Privately Owned Houses and Flats' Sub-Group from 'Consumer Price Index, Index Numbers for Groups, Sub-Groups and Special Groupings, Canberra' (ABS, Canberra, various issues). The Queanbeyan Index is from a sample of rents on 161 Queanbeyan flats taken from the files of Allen Curtis & Partners, Queanbeyan.

Rent control - 1980 on

In 1980 there are still pockets of 'old control' in Australia, particularly in Sydney and Melbourne. While traditional rent control, with its long and involved history seems to be all but gone, new control or 'rental market regulation' - is beginning to pervade the country. Certain aspects of the history and effects of old control are the subject of this section of the volume.

NOTES

1. The Act is discussed at length in the *Report of the Royal Commission of Inquiry on the Landlord and Tenant (Amendment) Act, 1948 as amended* (1961), New South Wales Government Printer, Sydney, 1962, which looked at the New South Wales legislation and provides a detailed history of that legislation.
2. See Chapter 6 this volume.
3. M. Whitman, 'The Public Control of House Rents', *Land Economics*, 1, July 1925, p. 345.
4. *Report of the Board of Inquiry to Inquire into the Operation of the Landlord and Tenants Acts*, (R.M. Eggleston), Victorian Legislative Assembly, Melbourne, 1956, p. 22.
5. S.J. Butlin, *War Economy*, Australian War Memorial, Canberra, 1954, p. 48.
6. *ibid.*
7. *ibid.*, p. 49.
8. E.R. Walker, *War-time Economics with Special Reference to Australia*, Melbourne University Press, Melbourne, 1939, p. 101.
9. W.R. Prest, 'Rents in Melbourne', *Economic Record*, 21, June 1945, p. 53.
10. *ibid.*, pp. 53-54.
11. *ibid.*, p. 54.
12. *ibid.*
13. *ibid.*
14. R. Mendelsohn, 'Australian Housing Policy: War and Post-War', *Economic Record*, 17, June 1941, p. 58.
15. R. Mendelsohn, 'Rent Control', Economic Monograph No. 23, NSW Branch of the Economic Society of Australia and New Zealand, December 1941, p. 2.
16. R.I. Downing, 'Housing and Public Policy', *Economic Record*, 24, June 1948, pp. 72-86; and *Housing and Employment*, International Labour Office, Geneva, 1948.
17. H.W. Arndt, 'Review of R.I. Downing's *Housing and Employment*', *Economic Record*, 25, June 1949, pp. 98-100.
18. D. Cochrane, D.M. Hocking and J.E. Isaac, 'The High Cost of Rent Control', *The Age*, April 15, 1953.
19. Figures from Helen Nelson, 'The Politics of Rent Control in New South Wales', Ph.D. Thesis, Department

of Government, University of Sydney, March 1977.
20. P. Clyne, 'The Landlord's Lament', *The Bulletin*, July 16, 1966, pp. 28-29.
21. John Singleton and Bob Howard, *Rip Van Australia*, Cassell, Sydney, 1977. p. 207.
22. For a good account of the changes in the A.C.T. Ordinance see A. Robertson, Untitled Paper on A.C.T. Landlord and Tenant Ordinance, mimeo, Canberra, 1978.
23. A.J. Bradbrook, *Poverty and the Residential Landlord-Tenant Relationship*, Commission of Enquiry into Poverty, Law and Poverty Series, Australian Government Publishing Service, Canberra, 1975.
24. Real Estate and Stock Institute of Australia, *Rent Controls: A Study of the Effects of Rent Controls in Canberra*, Canberra, 1975. Part of this study is reproduced as Ch. 9 of this volume.
25. Priorities Review Staff, *Report on Housing*, Australian Government Publishing Service, Canberra, 1975.
26. See R.P. Albon, 'Rent Control, A Costly Redistributive Device? - The Case of Canberra', *Economic Record*, 147, December 1978, pp. 303-313.

Chapter 6

A 'Fair Rent' Experiment in New South Wales

H.V. Evatt

A 'Fair Rent' Experiment in New South Wales*

H.V. Evatt

I. INTRODUCTION

The land history of Australia in general, and of the State of New South Wales in particular, bears little resemblance to that of Ireland. Yet the same idea of a Fair Rent to be determined irrespective of contract which was advocated by Parnell in 1878, and was adopted by Gladstone in the Irish Land Act of 1881, was canvassed about ten years ago in the various Australian Labour Parties as a possible solution of the problem of housing the people. Partly owing to their natural position, but chiefly to intentional forcing of the lines of trade communication towards them, the cities of Sydney and Melbourne were by 1910 growing to extremely large proportions relative to the States of New South Wales and Victoria, of which they were the respective capitals. This growth was becoming more pronounced in the case of Sydney, which in pre-Federation days could not rival Melbourne in the possession of local industries, and was in fact primarily the clearing-house and importing centre of its State. The development of manufacturing under the uniform Australian Customs Law increased the industrial life of Sydney to a great extent, and created the housing problem of yesterday and today. The Labour Party was returned to power in New South Wales in 1910, and in response to repeated demands

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* From the *Journal of Comparative Legislation and International Law*, Third Series, Volume II, Part 1, 1920.

from the Trade Unions the Government introduced a Fair Rents Bill in 1913, which passed through the Legislative Assembly, but was rejected by the Upper House. In the general elections held in December 1913, one of the issues of the appeal to the people was that rejection, and the Labour Party was returned with an increased majority. The Upper House recognised the constitutional position and a new Fair Rents Bill became law in 1915.

Rack-renting

Prior to the passing of the Act the Government had attempted to assist the Sydney City Council, which had demolished certain slum areas, but lacked the necessary authority to construct new buildings in place of the old. The assistance took the form of certain garden-suburb experiments, designed to relieve the congestion. This congestion was becoming serious, and was keenly felt early in 1914. Along with it came a good deal of 'rack-renting', a phrase used in Australia with a particular mediaeval connotation of the term 'rack'. In many cases it was proved that special bonuses were being given to agents by hungry home-seekers in order to secure dwellings, and private builders, afraid both of further Government housing experiments and of threatened increases in the cost of materials and labour, were not eager to relieve the situation.

At this period came the war, and by the middle of 1915 rents had eased somewhat when the effect of the absence of Australian troops began to be felt. It was at this juncture that the Fair Rents Bill was reintroduced.

The chief object of the Government in introducing the Bill was to put an end to existing 'rack-renting'. As mentioned above, the rents towards the end of 1915 were lower than those at the beginning of that year. This was admitted by the Government, which pointed out that the second object of the Bill was to prevent the possibility of 'rent profiteering' during the war by enabling a tenant to have a fair rent of his dwelling determined by a summary tribunal 'of equity and good conscience', providing a 'rough-and-ready method of arbitration' between the conflicting parties. The Government admitted further that the Act would not solve the housing problem or prevent its recurrence when the reaction from war conditions should set in. But they argued that at least the Act would deter unscrupulous landlords from acting unfairly, and that therefore it would provide a valuable protection to the tenant.

Opposition to the Bill of 1915

The Bill was strongly opposed on the grounds that it interfered with the 'economic law of supply and demand', that it attempted the impossible in endeavouring to fix a rental, and that it would prevent building operations from being started, owing to the subjection of the landlord to the control of the Court. One critic, Sir Joseph Carruthers, M.L.C., an ex-Premier of New South Wales, even suggested that after its sure and certain failure the Act should be burned by the common hangman, and declared that a person building in future deserved to be sent to Callan Park, a well-known Sydney lunatic asylum. The arguments against the Bill did not prevail, although certain important amendments were suggested in the Upper House, and accepted by the Government. Australian public opinion is seldom disturbed by the fear that a definite practical proposal may offend against 'fundamental economic laws', if it is seen that the scheme so criticised seems to be fair in its projected operation and worthy of a trial. The Labour Party in power at the time was still 'socialistic' in the way suggested by Metin in his phrase 'Socialisme sans doctrines'. Their theoretical objective, providing for the socialisation of all the means of production, distribution, and exchange, was still kept in the background, and prominence was given to the immediate fighting platform consisting of definite practical schemes, *quorum magna pars* the *Fair Rents Act*, 1915. By that Act, reports the Inter-State Commission of Australia,[1] 'the right of the landowner, recognised as a cardinal one for many centuries, to get what rental he can for his property, is displaced by a Statute of 25 sections'. Let us glance for a moment at the provisions of the Act.

II. THE ACT OF 1915

The Act is intituled *inter alia* 'To provide for the determination of fair rents for certain dwelling-houses, and to enforce such determination'. It applies to all premises leased wholly or partially for residence by a lessee, and includes any part of such premises separately leased. It applies therefore to flats, although very few applications have been made in those cases, and also to shops attached to a dwelling. Leases exceeding three years, or leases at a rent of more than three pounds a week, are excluded from the operations of the Act.

The Act binds the Crown, and its aid has been sought

by tenants holding from the Government authority in the Rocks area of Sydney, where after resumption and demolition of a large slum area new dwellings were erected.

Dwellings ordinarily leased for summer residences are not subject to the Act, which has not yet been extended outside the metropolis of Sydney. The various Sydney seaside residences which bring an increased rental in the summer months are also occupied as a rule throughout the winter. No case, however, has yet arisen in which an exemption from the Act has been granted on the ground mentioned.

The Act is to apply as proclaimed throughout New South Wales, but as already pointed out, has been restricted in its operation to Sydney.

Fair Rents Courts are established, each to consist of a Stipendiary or Police Magistrate, as recommended and appointed. So far only one Court has been constituted for the Sydney area, and it has been able to cope with all the applications under the Act.

A Registrar is in charge of the business side of the Court, and he has carried out the whole of the administrative work without other assistance than that of a part-time assistant.

Applications to the Court may be made in the form prescribed, either by a tenant who has paid his rent to date, or by a landlord. Particulars must be given in the application of any existing mortgage, and the mortgagee is entitled to notice of the application, and to be a party to the proceeding.

The Court is empowered to receive as evidence statutory declarations as prescribed, and oral evidence either in the ordinary way or for the purpose of cross-examination on the contents of a declaration. The procedure as to examination of witnesses, addresses, etc., is to be the same as that of the Supreme Court of New South Wales in its common-law jurisdiction, but in practice little oral evidence is adduced, and the Magistrate is guided by the four main statutory declarations - those of the landlord, the tenant, and the two experts mentioned below.

The calculation of the Fair Rent

The Act provides a definite scheme for the determination of the fair rent of a dwelling.

(a) The unimproved value of the land is first ascertained. This value is defined to be the capital sum which the fee simple of the land might be expected to realise if offered for

sale on such reasonable terms and conditions as a *bona fide* seller would require, assuming that the improvements, if any, thereon or appertaining thereto had not been made. The Court in the ascertainment of this value is assisted by an expert Government land valuer, who makes a declaration, and if required attends for cross-examination.

(b) The Court next estimates the cost of erecting a similar dwelling-house on the land at the time of the application, and deducts such fair and reasonable sum as may be allowed for depreciation of the actual dwelling the fair rental of which is being determined. In this assessment the Court is assisted by its second expert, a Government architect, who makes a declaration, and gives an estimate of depreciation allowing for the age, condition, construction, and lettable value of the dwelling.

(c) The capital value of the dwelling-house is then obtained by adding the value of the land obtained in (a) to that of the dwelling obtained in (b).

The next calculation is that of interest on the capital value to be allowed to the landlord. The Act provides that this interest is to be not less than the current rate charged upon overdrafts by the Commonwealth Bank of Australia, and not more than 2.5 per cent above such rate. The Court's interpretation of this provision is that the reference to the Commonwealth Bank shows the intention of the Legislature to adopt that rate as the standard, and that the 2.5 per cent margin is to be considered only in extraordinary circumstances. The current bank rate laid down as a basis is 6.5 per cent, and that is taken as the rate to be struck, plus .5 percent for collection of the rent. It has been contended that this interpretation is too narrow a one, and that the Court is entitled to allow the whole of or part of the marginal rate on any ground it may choose, e.g. the state of the market in other investments. The Court's interpretation is made final by another provision of the Act, and so the superior Courts have been prevented from criticising such interpretation. In support of the Court's view as to the intention of the Legislature, it is said that the Act is simply a determination between landlord and tenant, and that all it has to deal with is the single issue between the parties at the time of the hearing. If that is so, outside circumstances, such as the encouragement of building, and the state of the market, are not relevant, and the Commonwealth Bank's rate is fairly indicative of what the Legislature considered to be a fair thing as between the rival parties.

To the 7 per cent of the capital value, as ascertained

above, the following items are added by the Court in order to fix the fair annual rental:
(a) The annual rates as levied by Local Government, Water, and Sewerage authorities.
(b) The annual taxes imposed by State and Commonwealth on the land or the income derived therefrom.
(c) The amount estimated to be required annually for repairs, including painting, maintenance, and renewal.
(d) The annual insurance on the buildings.
(e) The amount estimated as annual depreciation in the value of the buildings where such depreciation is shown to have diminished their letting value. This allowance enables the landlord to establish something analogous to a sinking fund based on the lettable life of the dwelling.
(f) The amount (if any) the Court may allow for the estimated time per year when the dwelling-house is untenanted. To ascertain this item the Court takes a period of two years immediately preceding the date of the application as a guide.

The Act goes on to make the very important provision, which seriously qualifies the above method of calculating the annual fair rent, that, excepting where circumstances which render an increase equitable are proved to the satisfaction of the Court, the fair rent shall not exceed the rent at which the dwelling was let on the first day of January 1915.

The date mentioned is precisely one year before the commencement of the Act, so that where the Court is dealing with applications in the present month (July 1919), it generally has to refer to the rent existing four and one-half years ago. Considerable objection was raised to this in Parliament, but it was pointed out, and indeed it was a fact, that rents in Sydney were at an extraordinarily high level towards the end of 1914 and the beginning of the following year. War had broken out in August of 1914, but the departure of Australian soldiers had little appreciable effect in lowering rentals, until some time near the middle of 1915. On January 1, 1915, rents were higher than in August of 1914 or in August 1915. Consequently although the provision set out has had the effect of stabilising rents, stability has been maintained at a high and not at a low level. The same policy had been adopted in a British Statute - the Increases of Rent and Mortgage Interest Act, 1915 - which was passed for the period of the war and six months thereafter. In his interpretation of the provision, the Magistrate of the Fair Rents Court has apparently dealt with 'the circumstances which render an increase equitable' under three main classes, viz:

(a) Cases in which the rental as at January 1, 1915, was based on charitable or family as distinct from business reasons.
(b) Cases in which improvements in the dwelling effected since that date have resulted in a substantial increase of comfort to the tenant. It has been held that the addition of a bathroom to the dwelling is such a substantial increase.
(c) Cases in which the burden on the landlord has been considerably increased since January 1, 1915, owing to the heavier incidence of taxation or to other reasons.

The following case dealt with by the Court illustrates how the provision is applied:

	£	s	d
The total capital value of the dwelling was estimated at:	604	0	0
6.5 per cent. on this value had to be calculated in accordance with the method already explained and came to:	39	5	2
Annual rates and taxes	6	2	11
Estimated annual repairs	8	0	0
Insurance	0	14	11
Depreciation affecting the letting value, estimated at 1s. a week	2	12	0
Total as arrived at under the Act	56	15	0

The Court estimated this total (£56 15s.) as being equivalent to a rental of 22s. per week. It then had to apply the provision at present under consideration, viz. the rental as at January 1, 1915. This rental was 17s.6d. per week, and the Magistrate had then to consider whether there were circumstances rendering an increase equitable. It was proved that in 1915 the annual rates and taxes and the cost of repairs came to £7 12s. 11d., and it is seen from the above figures that the present burden to the landlord in rates, taxes, and repairs is £14 2s.11d. The Court therefore estimated the additional burden to the landlord as the difference between these two amounts, which came to £6 10s. per annum, which is equivalent to 2s. 6d. per week. It was therefore held that the present fair rental should be the 17s. 6d. rental of January 1, 1915, plus the 2s. 6d. per week thus calculated, and the rental was accordingly fixed at 20s. per week.

The provision moreover has apparently tended to

induce persons desirous of investing in property to build new dwellings rather than to deal in houses constructed before 1915. The Court has very seldom refused to increase the rent of dwellings constructed since that year and to which, of course, the provision cannot be applied.

In the case of a dweling occupied by two or more lessees, the Court determines the fair rent of the whole dwelling, and then apportions the fair rental for the particular tenant before it. This provision is used in the case of flats, and also in the cases where two families share a home in a crowded area.

A tenant not in default who is applying to have his rental determined is protected from being given notice and from having the rent increased while the application is pending, and for three months thereafter, unless the landlord can show reasonable cause for such action.

In the case of a furnished dwelling-house where the furniture is also leased, the Court determines the fair rent of the dwelling, and then adds an estimated furniture rental.

The determination of the fair rent of the dwelling has force for a period between six months and three years as the Court directs, and if no such direction is made, for three years. In practice the Court always fixed the period at twelve months.

While the determination is in force, the rent must remain as fixed notwithstanding any change of ownership or tenancy, unless the landlord satisfies the Court that since the award substantial alterations or additions have been made to the dwelling, or else that his outgoings in respect of the dwelling have been increased.

Terms or covenants in existing or subsequent leases of the dwelling are subject to the decision of the Court as to the fair rent, and rent paid in excess may be recovered. Penalties are provided to meet the cases of landlords ignoring the Court's determination by asking for or receiving additional rent, and also of persons threatening tenants against applying to the Court or acting detrimentally after application is made.

No costs are allowed in any proceeding under the Act. It was at first intended to prevent the parties from obtaining any legal assistance at all, but that provision in the Bill was not adopted. In practice the Court acts on the four declarations already mentioned, and the procedure is more ministerial than judicial. In the early cases before the Court counsel were briefed in order to secure interpretations favourable to the landlord, but now legal assistance is seldom

invoked by the parties. As there is no appeal from the Court's determination, the fixing of the rent has been arrived at in the way intended by the authors of the Act - a summary method of arbitration between landlord and tenant.

Covenants or agreements limiting the right of a person to take the benefit of the Act are made null and void.

Proceedings of the Court

On an average the Court sits once a week, and deals with about seven applications in about two hours. From the commencement of the Act in 1916 to June 30, 1919, there have been 1,301 applications to the Court. Apart from pending applications the figures as to the operation of the Act are as follows:

Number of cases	- Rent reduced	487
" " "	- Rent increased	182
" " "	- No jurisdiction	60
" " "	- Withdrawn	241
" " "	- Rent not altered	229
Total, apart from pending applications		1,199

In the majority of cases in which the Court had no jurisdiction the objection was on the ground that the tenant was in arrears. The smallest increase in rent granted was 6d. per week, the largest 10s., and the average increase 1s. 8d. The smallest reduction was 6d. per week, the largest 6s., and the average deduction 1s. 11d. The figures given show 182 cases in which the rent was increased, but it must be remembered that the application usually comes before the Court after the landlord has notified his intention to increase the rent, and that probably the usual increase so notified is for more than 1s. 8d. per week, the average increase granted by the Court. The figures for the first six months of the present year taken alone show that there were 104 cases of increase as against 58 cases where the rent was reduced; this illustrates what is undoubtedly a fact - that within the provisions of the Act the landlord is treated fairly by the Court.

III. THE EFFECT OF THE OPERATION OF THE ACT

In considering the effect of the Fair Rents Act after a working of something over three years, it is instructive to point out the present position of housing in Sydney. The

Inter-State Commission dealing with the question unanimously report[3] the existence of a . . .

> mischief which overwhelming testimony shows to be acute, arising from the actual deficiency in the number of houses necessary for the community, and which has caused a notable increase in overcrowding, coupled with the existence and enforced occupation of a mass of dwellings in our cities which fall short of the meanest standards of health and comfort, and which constitute a serious social menace.

In Sydney the resumptions for the purpose of street widening, apart altogether from the Rocks resumptions, dispossessed the inhabitants of 1,760 dwellings, and in addition factories and business houses have had a similar effect. At the end of 1917 it was estimated that there was a shortage of about 9,000 houses, and the shortage at the time of writing (July 1919) cannot be less than 13,000. To what extent has the Fair Rents Act been responsible for this serious and dangerous position?

An outstanding feature of the evidence given before the Inter-State Commission in Sydney was the dissatisfaction expressed by agents and investors with the Act and the Court. It was claimed by them that the 6.5 or 7 per cent of the capital value on which the Court commenced its determination was entirely insufficient, and that at least 8 per cent should be taken as a nett rental rate. Although, as we have already seen, the official valuer to the Court estimated that the landlord was getting a gross return of 10 per cent under the Act, this figure was keenly disputed. In view of the weight and body of this evidence there can be no doubt but that 'the Act has increased the disinclination to invest particularly on the part of the "speculative builder" who before the war provided a large proportion of the new dwelling-houses at rents within the reach of the industrial classes'. This conclusion of the Inter-State Commission seems quite justified, and indeed it is clear that the object of the Act was to deal only with the rival claims of landlord and tenant, and that the Court seeks only a present remedy to the dispute between those parties, and has little regard for the future investor in household property.

But, as was also pointed out by the Commission, the same disinclination to invest exists both in Brisbane and in Melbourne, where there are no Fair Rents Acts, and so 'the

effect of the new law cannot, therefore, be regarded as more than supplementary to the general causes tending to check building for investment'. This conclusion is reinforced by three considerations. In the first place, it must not be forgotten that the period of the Court's working has been an abnormal one in the highest degree. In most belligerent countries there was a practical end to building activity during the currency of the war, and Australia in general and New South Wales in particular have provided no exception to this rule. In the second place, the acute shortage of houses has been felt even more keenly in Melbourne than in Sydney, and Melbourne in its own relative situation to Victoria and in its own industrial life bears a very close analogy to Sydney. In Melbourne building for investment has been checked to at least as great an extent as in Sydney. In the third place the general causes of the decline in building have operated throughout Australia more or less uniformly. Those causes have been the difficulty of obtaining money for the purpose owing to the general financial position, the greatly increased costs of materials and labour, and possibly a certain amount of discouragement caused by the working of certain sections of the Federal Land and Income taxes which apply of course throughout the Commonwealth.

Sydney has been subject to all these general influences, and no doubt the Fair Rents Act has added a little to their cumulative effect. But the Act is certainly not the *causa causans* of the present housing crisis, which extends throughout all the eastern and southern cities of Australia.

On the other hand, the Act has worked both smoothly and inexpensively. The number of cases given above in which the rent was reduced does not fully illustrate the very considerable part played by the Fair Rents Court in keeping down rents during the difficult war period. Further, the provision fixing the general standard as at January 1915 has brought about the stability which was desired, and generally, the Inter-State Commission is fully justified in its conclusion that 'the Act has been a formidable bulwark against raising rents where no additional service is given by way of accommodation or equipment, and this deterrent operation of the Act represents its most valuable achievement'.

It is not possible, therefore, to pronounce final judgment as to the effect of the New South Wales experiment. The expected fall in the price of building requisites, which has not yet eventuated, will make the way clear to a more

definite conclusion. But if an interim opinion must be given, it does seem that the Act, although acting as a restraint both to the 'speculative builder' and to the cautious and timid investor, and thereby adding its quota to the causes of the housing shortage, has certainly kept rents at a reasonable rate during an exceptionally difficult period, and acted as a valuable deterrent to the building 'profiteer'.

NOTES

1. *Report of the Inter-State Commission of Australia dealing with Prices*, sub-nom, Rent, July 1919.
2. *ibid.* p. 10.

Chapter 7

Post War Confusion

(i) The Institute of Public Affairs (Vic)
(ii) & (iii) The Bank of New South Wales

Post War Confusion

(i) Rent Control*

Rent control is a classic example of where government interference with the free price mechanism can do almost irreparable damage. Maintained long after the disappearance of the emergency conditions which justified its introduction, it has inflicted grave social injustice on a small minority, and has delayed the provision of adequate housing facilities for the great majority. Some protection against unfair rents was provided under Victorian Law well before the Commonwealth began to enforce nation-wide rent-pegging under its war-time powers. As part of a comprehensive system of controls aimed at stabilising incomes and diverting resources to war purposes, rent control for a time worked tolerably well. In broad, rents in Victoria were pegged at 1940 levels, or, subject to appeal to rent tribunals, adjusted upwards to a maximum of 5% net of 1940 capital value of properties (i.e., after allowing for rates, insurance, maintenance, depreciation and other costs).

So long as prices ruling in the community and hence property values remained fairly steady, a ceiling on rents imposed little hardship on landlords. But the devastating effects of war-time finance on the price level could not be permanently deferred. With the return of peace, wage-pegging became politically untenable, subsidies were tapered

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* From the *IPA Review* published by the Institute of Public Affairs (Vic.) Vol. 8, No. 3, July-September 1954 pp. 73-79.

off and a number of other checks on inflation were relaxed or removed. Although money national income started to rise rapidly, rigid rent control was retained and consequently landlords were prevented from sharing in the higher incomes being received by the rest of the community. Rents were kept at 5% net on a capital figure already 50% undervalued by the end of 1946. Between September, 1939, and September, 1946, building costs of three-bedroom dwellings doubled; they are now about five times pre-war levels. The capital valuation of dwellings and business premises let after 1945 was related to actual construction cost, but practically nothing could be built by private investors because of building controls and other restrictions.

After the defeat of the Prices Referendum in 1948 the Commonwealth retired from the field of rent control and the problem of rents became one for the States. But the emotions aroused by rent control were too deep and too widespread to permit any possibility of an equitable solution. State politicians took the easy and popular course of disregarding the problem. The early war-time Commonwealth regulations were thus taken over almost in toto by the States despite the fact that they were utterly irrelevant to 1948 conditions.

The easing of control

In 1950 the Government of Western Australia removed controls on all houses rented after December, 1950, altered the basis of capital valuation to current replacement cost less depreciation, and granted an all-round increase in controlled rents of 20% on housing and 30% on business premises. This ceiling was raised a further 10% in 1951. Rent control legislation in Western Australia lapsed on April 30th, 1954, but has since been restored, retrospective to May 1st.

Following the recommendations of a special public committee, Tasmania granted a 20% rise in dwelling rents and a 35% rise in business rents in 1950. Additional increases were permitted in 1952 and restrictions over the renting of business premises have been virtually removed.

South Australia set up an independent committee of enquiry in 1951, and, as a result of its report, abandoned the principle of pre-war capital valuations and authorised its rent-fixing authority, the Housing Trust, to grant increases in rents of up to 22.5 per cent. The controls were further eased in 1953 and all restrictions over the renting of business premises were removed. Queensland and New South Wales have

taken minor steps towards the revision of their rent-fixing laws. However, probably as a result of a liberal interpretation of the existing provisions, there has been a gradual increase in the average rents paid in these States.

Victoria has been the laggard. Table 1 shows increases in average rents of four and five roomed houses in the various States since 1939.

Whereas, since 1939, rents of pre-1945 houses have increased by 40 per cent in Perth, and even by as much as 28 per cent in Sydney, they have risen by only 4 per cent in Melbourne. Apart from tightening up on sub-letting abuses, making it easier for home-owners to repossess, and freeing from control certain new tenancies and, in the case of business premises, all tenancies taken on leases of three years or longer, Victoria has made no attempt to remedy the glaring injustice to lessors who have to pay 1954 wages for maintenance and repairs, but barely recoup 1939 rents. Since pre-war the general price level in Victoria has increased by 151 per cent, average weekly wages by 216 per cent and building costs by 400 per cent.

Table 1.

Weekly Rents of Four and Five Roomed Houses

	1939	June 1954	Incr. %
Sydney	23/3	29/8	28
Melbourne	21/5	22/4	4
Brisbane	19/2	22/7	18
Adelaide	19/11	26/4	32
Perth	19/9	27/8*	40
Hobart	20/9	28/7	38

* March, 1954.

Note: Rentals of new houses completed since the end of the war - mainly Housing Commission homes - are not included.

Source: Commonwealth Statistician

The effects of rent control

Little statistical data is available on income from rents. However, an analysis of information published in the National Income Estimates, suggests that the share of the national income attributable to private landlords for dwelling rents had fallen from about 4 per cent in 1938-39 to less than 1 per

cent today. Rents have lagged so many laps behind costs that few landlords are able to make repairs or improvements to their properties. The cost of this type of work has risen much more than other costs because of the dearth of skilled tradesmen and materials. Many tenanted houses and business premises are falling into disrepair for lack of proper maintenance. Whether driving down the main shopping block or side residential streets, in most of the older suburbs of Melbourne one is met with a picture of almost unrelieved dinginess and dilapidation. Government attention is concentrated on the erection of new housing, oblivious to the fact that the stock of old houses is being hastened to premature decay through rent control. Landlords are not by any means always well-to-do. An analysis of taxation statistics shows a far greater concentration of incomes from rent in the low income brackets than for any other type of property income. The truth of the matter is that many elderly people and others of small means have in the past invested their life's savings in house property to provide for their declining years. They now find that, because of rent control, they are obliged to live on a mere pittance and are also unable to 'cash in' on high post-war property values because they have practically no rights of repossession. Owners, especially deceased estates, have in many instances been forced to sell at whatever price the tenant was prepared to pay since under the Act he has first option to purchase. Because of the high premium for vacant possession, tenants are often able to make a substantial gain through resale.

The continuance of rent control has a bad psychological effect on investment in house property for rental purposes. Although technically free from control, most investors do not relish building at the present high level of costs coupled with uncertainty about the future of rent control legislation. The provision of new houses for letting has virtually become a State monopoly, and under present conditions it is likely to remain so. Apart from the burden on the State budget and the inability of Government housing to keep up with demand, there is a strong case on broad social grounds for the retention of some degree of private letting of houses. Rent control is bringing about a revolution in home ownership. The supply of privately rented houses is falling rapidly each year through sales to tenants and other owner-occupiers. Thus many people seeking to rent a home are being forced against their wishes and, ultimately possibly against their interests, to purchase on heavy mortgages. These people are often obliged to erect cheap weather-board

homes on the outskirts on the metropolitan area, greatly adding to the community cost of providing sewerage, electricity and transport.

At the same time as the outer areas are being uneconomically extended, rented housing in the inner suburbs is being under-utilised. The number of persons per dwelling is now substantially lower than before the war, and this is largely attributable to rent control. Protected tenants have a strong interest in remaining in their existing dwellings, even though their families may have grown up. Moreover, since rents are so low there is no great incentive to take a lodger to help out. Removal of rent control over private dwellings would pave the way to the equalisation of dwelling rents for houses of similar type, whether privately or government owned. Rents now depend not such much on the size or location of dwellings but the date of their first construction or letting. This has created the greatest inequity between Housing Commission tenants whose rentals range all the way from 15/6 per week for dwellings let in 1939 to nearly £4 per week today.

Business premises

Owners of property let for business purposes suffer equally with other landlords from inadequate rentals and inability to maintain and renovate their premises. Since the majority of business tenancies are on short term leases, rents cannot be adjusted without approval from the Fair Rents Court; nor can tenants be evicted to modernise premises or to demolish old structures and erect new buildings without its consent. Ramshackle establishments are thus permitted to remain on sites ideally suited to new office blocks, hotels and shops. The services which the city urgently needs are not likely to be provided under existing conditions. To date not one single new building has been finished in Melbourne since the war. With the removal of restrictions and the introduction of American cost-saving methods of construction, investors might again be prepared to turn their attention to city real estate. The longer this is delayed, the further will Australian cities drop behind the developments occurring in the main cities in overseas countries.

Rents and the cost of living

The main argument advanced against any relaxation of rent control is that it would mean a sharp rise in the cost of living

and, unless this was passed on through basic wage adjustments, the living standard of wage-earners would be reduced. If it were passed on, the price spiral would be generated afresh. For the purpose of compiling the 'C' Series Index, the Statistician takes into account only four and five roomed private houses completed prior to 1945. These houses whose rents have been subject to rigid control comprise probably no more than 10 per cent of accommodation occupied by wage and salary earners in Melbourne. This explains why the Index shows an increase in rents of a mere 4 per cent since 1939, whereas the rise in costs of housing accommodation for the majority of people would be substantially greater.

At present less than half of the accommodation of wage and salary earners in Greater Melbourne is being rented. Over half is owned or being purchased on terms. Possibly one-quarter comprises tenanted one-family private houses and flats whose rentals can be effectively policed under the *Landlord and Tenant Act*. The remainder consists of Housing Commission homes (possibly 5 per cent of all employee homes) exempt from the Act and a great variety of shared and miscellaneous accommodation, most of which, though within the scope of the *Landlord and Tenant Act*, is in actual practice more likely to be the subject of private arrangements. Both the South Australian and Tasmanian committees of enquiry draw attention to the high rents being paid for shared accommodation due to the ineffectiveness of the controls. The Tasmanian committee points out that tenants sharing accommodation do not avail themselves of their legal rights through ignorance, insecurity of tenure or just plain desire to live in peace and harmony with the co-sharing landlord or head tenant.

This means that the cost-of-living of the great majority - about two in every three - of those wage and salary earners who have to pay for housing accommodation, would in actual fact not be increased by relaxation of rent control, even though the 'C' Series Index - because of the peculiar nature of its compilation - showed a rise in living costs. If women, juniors and others bearing little or no direct responsibility for housing costs are taken into account, the proportion of wage and salary earners whose living expenses would be unaffected by relaxation of control would be about four in every five. This majority would therefore have no moral or economic claim for an adjustment in their incomes should rent control be eased. At the moment the average controlled rent on four and five roomed houses is

22/4. A increase of 50 per cent in rents would mean that the minority enjoying the benefits of these rents would still be paying only 33/6 a week compared with the £3 or £4 by Housing Commission tenants and others.

If the cost-of-living index were allowed to affect wages, a 50 per cent rise in controlled rents would increase wages all-round by 12/- a week in spite of the fact that the living costs of the majority would remain unaffected. It would surely be the height of folley to disturb general price and cost stability on the flimsy ground that a favoured minority - already paying far less for their housing than everyone else - would be adversely affected.

A new policy for rents in Victoria

The complete removal of rent control would overcome the principal economic difficulties - the shortage and waste of rented housing facilities, the inequitable diversity of rents, unsightly business premises, retarded city development and the premature decay of valuable national assets through inadequate maintenance - and in the long run would be highly beneficial. However, with housing rentals it is not suggested that this should be done at one fell swoop. But an immediate rise in Victorian rents of something like 40 to 50 per cent would be justified as a first instalment towards the eventual elimination of control.

(ii) Implications of Rent Control*

Government control of house rentals has aroused controversy over the rights of landlords and tenants which have been distorted by continued inflation. Of equal importance with the question of equity are the effects of rent control on the full use of existing housing and on the building of new houses

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* Bank of New South Wales *Review*, No. 12, February 1953, pp. 10-13.

for a rapidly expanding population. Under current conditions many people find it beyond their means, or inclinations, to buy their own houses, yet the same high costs and the prospect of official control make the construction of homes for rental unattractive for the private investor. Would more homes be built if economic factors of supply and demand for housing were allowed to determine the level of all rents?

Imposed at the outbreak of war in 1939, Commonwealth-wide rent control pegged house rentals at current levels as part of a plan to avoid any profiteering from war circumstances and to help keep down prices. As long as other controls kept the general level of prices and incomes fairly steady, no serious injustice was done to landlords. Yet, as with all controls in conditions of scarcity, serious abuses developed, particularly with new lettings, to the detriment of would-be tenants.

In recent years, however, average wages and other incomes have risen sharply, most controls have been relaxed or removed, but owners of rental properties have received little comparable benefit. Indeed, they have been faced with higher rates and also higher payments for repairs, not only because the scarcity of materials entailed the long deferment of maintenance, but also by reason of extremely high costs and wages for that type of work. Recent amendments to rent control provisions have taken some account of these increased costs, but they stopped short of awarding substantial increases in net earnings to owners of house properties, in line with other increases in incomes and living costs throughout the community.

Fixing rents

Rent control is now administered by the various States, for the Commonwealth abandoned its wartime defence powers over prices and rents after the adverse result of the 1948 referendum. By that time awkward pressures were beginning to appear, and the emphasis of rent control turned gradually from universal pegging at pre-war levels towards the determination of 'fair rents' for individual properties of which certain States had some pre-war experience. The general basis of computation of a 'fair rent' was to allow a net return to the owner of about 5 per cent on the value of the property, with additional amounts to cover actual rates and insurance charges and estimated allowances for maintenance depreciation, and rent collection. For pre-war dwellings the value on which net return was calculated was, and still is in

some States, the value ruling in 1939 or 1940. For new houses actual cost was generally adopted. Only in Western Australia, South Australia, and Tasmania has there been any substantial change in administration of rent control. In those States a general increase in rentals of 20 to 30 per cent on dwellings and over 30 per cent on business premises was allowed. In addition, in assessing 'fair rents', both Western Australia and South Australia use 'current replacement cost, less depreciation' as the value of a property rather than the arbitrary pre-war market value.

Rigidities and injustices

Despite these steps towards more liberal administration the continued existence of rent control has created extremely rigid conditions in the letting of houses. Persons who have a house rented continuously since before the war may still be paying the same rental, though they go in fear of being 'fair rented', but they would be unwilling to move to another area because of the extreme difficulty of securing tenancy of another house. For this reason older people whose children have left the family home may be occupying a house substantially larger than their present needs or desires, and may in fact pay a lower rental than they would for a new but much smaller house. In these circumstances, too, they have a positive financial discouragement from building a new house for themselves at current high costs while they are enjoying a relatively low rental. Few newcomers to the housing market, ex-servicemen, newly married persons, or growing families, have been able to obtain a pre-war rent-controlled dwelling; others have the difficult choice of living with parents, buying a high-cost post-war home, if they can finance it, paying high rentals for inadequate temporary accommodation or waiting indefinitely for a State-built house, the rental of which, incidentally, would be based on contemporary building costs.

Parallel with rent controls go various restrictions on an owner's rights to gain possession of his property and to let it to whom he will. Generally he is faced with the difficult requirement of finding alternative accommodation for his tenant and persevering through lengthy legal proceedings. In turn, these provisions react on tenants, for some landlords endeavour to avoid these restrictions by leasing for short terms not subject to control.

These examples illustrate the stultifying injustices of a control which was introduced to meet circumstances far

different from those of today. In some States it is continued largely out of political prejudice against property owners, and only two States have endeavoured to have the subject properly analysed by independent commissions. Undoubtedly there are landlords who own large blocks of rented property, but political animus against them also affects large number of small property owners. The industrious and provident retired person relying on his modest block of flats or pair of cottages to keep him independent of the old age pension has been penalised by a relatively fixed income from rents which has fallen steadily behind the rise in living costs.

Economics of housing

Apart from questions of equity as between owners and tenants and between property investors and other sections of the community, rent control has important effects on the state and quantity of housing available to accommodate the rapidly increasing population. A direct consequence of the restriction of rental income is that landlords are forced in effect to live on their capital, and houses deteriorate for want of adequate maintenance. It has already been remarked how rent control has encouraged an uneconomical occupation of housing and has been a factor increasing the immobility of labour.

Yet these considerations are perhaps secondary to the more fundamental one of whether in the absence of rent control more housing would be available. Probably more people could be comfortably and effectively housed in existing dwellings, but the question of additional new housing is determined more by costs of building than by rent control. In point of fact, rent control has rested more lightly on newly built houses, but of all the houses privately constructed since the war an insignificant number were available for rental, and even then in most cases the letting has been due to a change in circumstances of the owner. In New South Wales in 1951/52, of 24,000 houses and flat units completed, about 20,000 were immediately occupied by the persons building them and about 4,000 were built for renting; virtually all of the 4,000 for renting were constructed by the State Housing Commission.

It is true that direct government restrictions on buildings for investment may have been responsible for stopping some private building of rental flats and houses after the war, but in the main it would seem that possible investors in the new rental properties have not considered the 5 per

cent return allowed under rent control sufficient to balance the risks involved - in particular the risk of being treated unfairly by some future government freeze on rents. In addition, in the last year or so mounting building costs would cause many would-be investors to doubt whether the tenants they might obtain could continue to meet a rent yielding an adequate return on the capital invested.

Thus private investment in housing has been limited to those who bought their own houses, accepting a lower return on their equity in the house than could be obtained in other investment, perhaps ignoring the fact of depreciation and in many cases reducing the cost of maintenance with their own labour.

Building costs

In the post-war period the benefits to house builders of general low rates of interest were swallowed up by the sharp rise in all building costs. The latter were a direct reflection of shortage of skilled labour and building materials in the face of demand banked up since the early war years and reinforced by relatively easy money conditions. It might be argued that in the circumstances further demand from would-be landlords would have merely forced up costs further without adding to the total number of houses built. Yet if an adequate supply of homes for rental had been assured fewer individuals would have attempted to build for themselves, overloading themselves with debt and pushing up building prices in their desperate attempts to build.

As it happened, the great bulk of rental housing has been provided by State housing schemes, whose concern about building costs was less pressing than that of the individual. These projects have enjoyed cheap loan finance and have adopted periods of amortization much longer than those reasonable for a private individual. Although the Commonwealth housing agreement offers rental rebates to prevent rents absorbing an unduly large proportion of a tenant's income in the lower wage-earning groups, rents on State projects generally have been higher than controlled rentals for comparable pre-war houses.

Whatever may have been the circumstances in past years, relatively slack conditions in the building industry reopen the prospect of private building for rental. For this to be feasible on any scale, building costs, particularly on large projects, whether of flats or groups of cottages, must be reduced substantially, but that type of steady construction

offers obvious opportunites for greater building efficiency. The shortage of public loan funds also helps to tip the scale in favour of private building, but here, as in other forms of investment, the return must be appropriate to the outlay, risk, and supervision involved. In currently restored competitive conditions, rent control is an anachronism; its abolition would help stimulate investors' confidence and general housing activity.

(iii) Rent Control and Property Investment*

Of the 2.5m dwelling units which house the Australian population of nearly 10m, about 600,000 units are occupied under tenancy contracts arranged to a large extent between individual property owners and individual tenants. The terms of occupancy and the amount of rent are subject to various limitations under State laws which survive from emergency wartime legislation of the Commonwealth Government.

In some States, however, elements of these laws have links with social legislation of the depression years in the early 'thirties. In all States the laws, usually under the old-cliched and emotional title of Landlord and Tenant Acts, have been steadily amended in recent years in a way which has, in general, allowed varying increases in the rentals of old properties, eliminated rent control for newly-built houses, and reduced the types of tenancy subject to the laws. The amendments have also given property owners greater opportunities to terminate tenancies to obtain possession of their properties either to live in or to sell with vacant possession.

No uniformity, however, exists between the States in the range of tenancies still covered, in the way fair rents are determined, or in the rules governing termination of tenancies. The complexities of some of the laws are

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* Bank of New South Wales *Review*, No. 35, November 1958, pp. 11-13.

notorious, but it is possible to outline some of the salient features

State variations

In New South Wales, Victoria and Queensland, where control is more detailed and rigorous than elsewhere, the most important class of property affected is that tenanted continuously since 1939. In each of these States the property owner is generally allowed to raise rentals only to cover increases in regular outgoings on the property, such as rates, and to permit a larger allowance for repairs, which may or may not cover actual expenditure. In a large proportion of cases, however, the owner is prevented from gaining anything like the full benefit of the capital appreciation of his asset. He is not allowed in most instances to terminate the tenancy in order to sell the property at its current market value, but is compelled to leave the tenant in possession and to accept a return of 4 to 6 per cent on a fictitious valuation of the property. In New South Wales this is the 1939 valuation, in Victoria the 1940 valuation plus 25 or 30 per cent, in Queensland the 1948 valuation. As current market value of the property with vacant possession is often three times as high as the figure used by rent control, the real effect is to allow property owners only a very low net return on the real value of their property.

In each of these States the rigidity of the control has been eased off in the last few years. For example, in New South Wales the controls do not apply to houses constructed since 1954, and business premises erected since 1957 and new tenancies may now be excluded. In Victoria all business premises not previously let have recently been freed and owners may raise existing rents 20 per cent and place the onus of approaching the Court for a rent determination on the tenant. In each of these States, too, the rights of certain classes of property owners to gain possession of their property, and therefore realise on the capital appreciation of their investment, have been restored, and it is now permissible in some cases for an owner to pay a tenant a fee to vacate premises.

In South Australia, Western Australia, and Tasmania the control does not insist on a rigid basing of rental on a fictitious capital valuation, but allows the controlling authorities to consider many factors, including the level of other rents. This approach, together with the effects of an easier housing situation and rules which allow owners to

regain possession, has altered the emphasis of rent control from a discriminating and uneven price control to a means of preventing gross abuse of a tenant's need.

Fair rents

In its more rigorous forms, however, rent control has allowed only a reluctant increase in returns, while prices, wages, and returns on many other forms of investments have trebled. The rent element of the 'C' Series retail price index rose only 57 per cent since before the war, while the total index virtually trebled and nominal weekly wages rose by 264 per cent. Because of inability to gain vacant possession many owners have not been able to take advantage of the high property market arising from the fourfold increase in the cost of building homes and the large increase in money incomes. Prices of tenanted houses are depressed because, generally speaking, the purchaser of a house still subject to rent control seeks a net return from the fixed rental of over 8 per cent on his outlay. Only if the purchaser sees opportunity to gain possession of the property from the tenant would he be prepared to pay a price more in line with the values of other property.

In such a situation injustices and anomolies invariably occur. But the major injustice of rent control is that it forces a limited section of the community - those property owners whose properties are still within the scope of control - in effect to subsidise the incomes of another limited section of the community, those who happen to be renting older houses. In the emergency of wartime such arbitrariness might be justified. But more than a decade later it should be possible to devise a more equitable form of subsidising cheap housing if it is thought desirable. This principle is recognised by provision in the Commonwealth-State housing scheme for subsidising from public revenue those whose family income is judged inadequate to pay an economic rent.

Effects of rent control

Two very noticeable effects of rent control have been, first, the virtual elimination of new investment in rental housing, and, secondly, falling standards of maintenance together with minimum modernisation in tenanted houses. In the absence of new private building for rental purposes, a large expansion of individual home building was necessary to cope with the rapid growth of family formation. State housing authorities

were responsible for almost all building for rental. Thus, between the two post-war census dates the number of dwellings owned or being purchased rose by about 50 per cent, but the number of tenancies fell slightly, despite the scale of government housing activities.

Table 2

Census of Dwellings

Nature of Occupancy	1933	1947	1954
Owner	604,413	838,025	1,121,814
Purchaser by Instalments	189,627	147,677	353,093
Tenant	615,412	812,750	799,230*
Other	100,219	75,171	69,284
Total	1,509,671	1,873,623	2,343,421

* Including 99,376 government housing units.

While socially desirable for many reasons, an expansion of private home building has some economic drawbacks. It has led young people into burdens of debt which they might well have preferred to avoid if rental homes had been available. The trend towards private home ownership has made demands on the banking system for a heavy proportion of longer-term housing finance, and so limited the loans available for other purposes. Investors who might have invested in rental housing but for rent control presumably directed their funds towards other avenues via the stock exchange, while those who owned rent-controlled property, found their asset virtually frozen. It might be said, therefore, that the forced movement towards more extensive home ownership has introduced greater rigidity into the financial structure. Possibly it has also brought about less mobility of labour, for people are less willing to move to new locations when, because of the absence of suitable rental accommodation, they are obliged to sell their own house and buy another.

The outlook

Although investment in new rental housing has been thoroughly discouraged by the nature of rent control for nearly 20 years, it is interesting to note that substantial sums have been invested in factory and business premises where rent control has been lifted and where, apparently, investors have little fear that it will be reimposed.

If decontrol of rents and tenancies proceeds along the lines established in recent years, and if private tenancies continue to decrease as a result of sales of tenanted properties to home owners, then, even in the States where the more rigorous forms persist, the number of electors directly affected will become less significant politically. In this event, the form of control might well change from what is really an anomolous form of price control and private subsidy to a simpler preventative against gross abuse of an owner-tenant relationship, such as even now applies in some States.

Whether such a trend would bring forth a flow of private investment into new rental flats and houses is difficult to assess, since so much depends on the relative attractiveness of other forms of investment available. One factor of some importance is that the growth of home ownership has made an increasing number of people aware of the costs and tribulations of property maintenance and of the burden of a long-term debt commitment. These circumstances may make more people face with greater equanimity a level of rents based on current costs and consequently offering a fairer return to the investment of private capital in housing.

Chapter 8

The Politics of Decontrol in New South Wales

Helen Nelson

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I. INTRODUCTION

The 'temporary' rent control measures introduced in New South Wales (NSW) during World War II in order to meet an emergency situation have long outlived the emergency. Today, more than thirty years after the cessation of hostilities, the legislation continues to operate. Its application has been narrowed from virtually the entire private and business and commercial rental market to, in 1975, an estimated 35,870 dwellings, or approximately two per cent of the total number of dwellings.[1] Rent control has survived although neither the Labor Government (1941-65) nor the Liberal Government (1965-76) nor the current Labor Government (1976-) has ever advocated a policy of permanency.

Rent control has a political significance that gives it a momentum of its own and an unintended longevity. It is an issue that deals with an area of basic human necessity - shelter. In addition, it is an issue that carries a heavy historical burden. The debate surrounding the conflict between landlord and tenant is one that traditionally evokes passionate debate. As Brown reports '. . . even a group composed mainly of lawyers can become excited and overheated when rent control or its abolition is discussed. The political animal breaks loose from the detached professional mind'.[2]

The release of political passions is not uncommon in debate surrounding issues that seek redistribution. Rent

control is redistributive in the sense that it represents legislative interference in the 'normal' law regulating the landlord and tenant relationship so as to effect a reallocation of the rights and obligations of the respective parties. Rent control restricts the amount of rent that a landlord can demand and it imposes limitations upon the landlord's ability to repossess his property. It thus impinges on the landlord's exercise of the 'normal' privileges of property ownership and in exchange offers the tenant increased security of tenure. By presenting a bias in favour of the tenant and negating ownership rights, rent control poses a threat to the established order. It challenges the basic assumptions of property law and thus, of the capitalist system. It is the 'threat' it presents that gives rent control its special political flavour.

This chapter examines the politics of rent control with reference to the case of the NSW legislation.

II. BACKGROUND

The NSW *Landlord and Tenant (Amendment) Act, 1948*, had its origins in the Second World War. On 9 September 1939, shortly after the outbreak of war, Australian Commonwealth leaders and the Premiers of all States met to discuss wartime controls. It was resolved that in order to avoid rent inflation and exploitation of the shortage of housing accommodation in areas surrounding military camps and wartime industries, the States would co-operate with the Commonwealth in setting up the machinery necessary for rent control. On 29 September 1939, the Commonwealth, acting under its emergency powers, issued the *National Security (Fair Rent) Regulations*. The regulations were introduced in the Australian Capital Territory and the Northern Territory and adopted in Victoria, Queensland and Tasmania. Separate State legislation was introduced in NSW, South Australia and Western Australia.[3]

In May 1941, a Labor Government was returned in NSW. R.R. Downing, Minister of Justice, drafted new rent control legislation to replace the 'meagre' provisions of the previous Government's 1939 Act. In October, before the new bill was ready, a Labor Government under the Prime Ministership of J. Curtin was returned at the national level. At Curtin's instigation, Downing conferred with Commonwealth officials and the proposed NSW legislation was used as the basis for revision of the Commonwealth regulations. The new *National Security (Landlord and Tenant) Regulations* were introduced on 28 November 1941 and were put into

operation in NSW immediately. They remained in force until 1948 when the Commonwealth withdrew from the field following the defeat of the prices and rents referendum of that year.

Controls by the States

Following the enforced withdrawal of the Commonwealth rent control regulations, all States enacted legislation to ensure some form of continued State control. It was feared that unless subjected to regulation, rent levels would rise steeply, affecting not only individuals but having also a damaging effect upon the price structure generally. It was agreed further that tenants were entitled to some protection against eviction. The priority given to the war effort had resulted in a severe post-war accommodation shortage in all States and especially in the most populous, NSW. In 1947, evictions in the Sydney, Newcastle and Wollongong areas had totalled 3,082, an average of almost sixty per week, and the number was expected to increase in 1948. The NSW Housing Commission had before it 4,900 applications for emergency accommodation. Emergency facilities were stretched to the limit and the Commission claimed that it could not make any impact upon the problem unless there was a decrease in the number of evictions.

The NSW Act passed in 1948 was similar in content to the Commonwealth regulations. It operated in respect of 'prescribed premises', which were defined in terms wide enough to include all urban property with the specific exclusion of the Crown, the Housing Commission, licensed premises and holiday premises. Rent determinations were made by Fair Rents Boards constituted by a stipendiary magistrate, except in the case of shared accommodation, where the Rent Controller acted. The Act did not stipulate any set formula for the determination of rents. Section 21 merely set out the matters to be considered by the Board. In practice, the formula used was the same as that evolved under the regulations, whereby controlled rents were calculated from a basic rent, based on rates payable as at 31 August 1939, plus outgoings.

Eviction controls

The most radical departure from the regulations, and the most controversial section of the legislation, was in the provisions dealing with eviction controls. That there should

be some restraint upon evictions was not contested. The dispute concerned the extent of the protection to be afforded tenants. Under the NSW *Landlord and Tenant Act, 1899*, if a notice to quit is properly given and the landlord can prove his case, the court has no alternative but to grant an eviction order. The Commonwealth regulations had defined the grounds for eviction and extended greater security to tenants by directing the court to 'take into consideration' hardship factors. The decision to grant or refuse an order was thus left to the discretion of the court. In practice, the court had held that in cases where the hardships of landlord and tenant were equal, the normal rule should apply and the landlord was entitled to obtain an eviction order. Section 70 (2) of the NSW Act went further. It stipulated that no eviction order could be granted on any ground other than negligence on the part of the tenant unless the landlord provided the tenant with reasonably suitable alternative accommodation. Whereas under the regulations the provision of alternative accommodation had been a factor to be considered, under the NSW Act it was now a prerequisite to the granting of the order. Given the prevailing conditions of a severe accommodation shortage, it effectively vetoed the landlord's right to reclaim his own property and stemmed the tide of evictions.

III. AUSTRALIAN LABOR PARTY IN GOVERNMENT, 1941-1965

The NSW ALP Government, 1941-1965, was a government of moderates. It never advocated rent control as a permanent policy. There was no ideological commitment to such a policy. The right wing of the party dominated the machine and there appears to have been no great interest in reform policies. Labor spokesmen generally acknowledged that rent control was no more than a necessary response to extraordinary economic circumstances. It was seen as an interference in the 'normal' law of landlord and tenant and in the 'normal' economic life of the community. It was regarded as a temporary policy, necessary only in order to meet the demands of an emergency housing situation. A small minority group in the Upper House regularly opposed any move that hinted of decontrol, but their opposition never manifested itself in advocacy of rent control as a social policy.

'Anti-landlordism'

If there was no coherent ideological commitment to rent control, there was, nevertheless, a set of ill-defined 'partial ideologies' or political ideas that permeated the party's response to rent control. Firstly, the policy of tenant protection had great symbolic value for the ALP. It represented the fulfillment of many old ideas and slogans. Secondly, there was a legacy of 'anti-landlordism'. This was muted by the number of 'small' landlords (that is, those who owned only one or perhaps two tenancies), who were known to suffer adversely under the legislation. But though there was sympathy for the 'small' landlord, the historical baggage made it difficult for a party such as the ALP to agree to any decision that represented a gain for the landlord - and thus, a loss for the existing tenant.

Fear of eviction

An additional theme that came across constantly in the parliamentary debates was the fear of evictions. It was particularly real for those who had witnessed the mass evictions of the depression of the 1930s and was the rationale behind section 70(2) (the alternative accommodation provision) and other stringent eviction controls, particularly those placed on new owners. 'New owners', 'people with ready cash', were clearly identified in the minds of some parliamentary speakers with the new settlers arriving in the post-war wave of immigration - there are several references in the debates to cases where, for instance, 'Good Australians were cast into the street to make way for foreign immigrants.'[9]

Considering the electorate

Finally - and perhaps, most importantly - any amendment to the *Landlord and Tenant (Amendment) Act* had to be viewed in the light of pragmatic considerations about the likely impact on the electorate. Any amendment that allowed an increase in rents or opened the way for easier eviction of tenants from controlled premises would be most keenly felt in Labor-held electorates. There are no statistics revealing the location of controlled premises, but the suburbs most frequently mentioned as having a large proportion of protected tenants were mainly Labor-held old residential

areas such as Paddington, Darlinghurst, Randwick, Bondi, Coogee, Leichhardt, Balmain, Drummoyne and Newtown. With time, as protected tenants came increasingly to accept controlled rents as the norm, the political consequences of raising rents became more potent.

Fear of the electoral consequences, fear of mass evictions and an element of anti-landlordism were to be constants in Labor's response to the issue. However, the Government could not ignore the pressures for decontrol that began to emerge in the early 1950s.

Investment in rental accomodation

All wartime controls on building operations were lifted in October 1952. When a boom in the building industry failed to materialise, rent control began to be a scapegoat for the continuing accommodation shortage.[5] It was claimed that rent control compounded the shortage by repelling private investment in rental accommodation and by discouraging landlords from re-letting when tenancies became vacant.

Private investment was traditionally the main supplier of rental accommodation. While it was conceded that the removal of rent control would lead to some increase in private rental investment, there were doubts as to the extent of that response. There were other factors which mitigated against a large investment response. These included changed consumer attitudes towards rental housing and the availability of other fields of investment which offered better returns and fewer management problems. Even if the lifting of controls provided the necessary stimulus for investors to respond to the housing demand, there was no guarantee that the building industry had the capacity to meet the demand quickly.[6] Against this uncertain gain in rental investment, the political costs of decontrol were daunting - decontrol contained the threat of protected tenants evicted, on the street and unable to find alternative housing accommodation. There would have been also a backlash against greatly increased rentals.

Public housing resources were stretched to the limit and could not be relied upon to fill the gap. Housing Commission priorities were, anyway, directed towards home-ownership. The first Commonwealth-State Housing Agreement, introduced by the Commonwealth Labor Government in 1945, had the provision of low rental housing as its prime objective. But high maintenance costs and electoral pressures meant that there was little opposition when the Menzies Liberal Government changed the terms of the

Agreement in 1956. (They switched the emphasis to one of home-ownership by providing easy terms for the sale of Commission houses and by directing a portion of the funds away from the State Commissions to co-operative housing societies. The move was endorsed by the NSW Labor Government, which, in 1956, agreed to the proposal that the Housing Commission should build 80 per cent of homes for sale and 20 per cent for rent.)[7]

Towards decontrol

So long as the opponents of rent control could link controls to the housing shortage, the issue of decontrol could not be ignored. Also, the rent control policy sat uneasily beside the policy to promote home-ownership. There was, therefore, for the Labor Government, a fine balance between the pressures for decontrol and those favouring retention of controls.

The first option, total lifting of controls, was not feasible. There was no certainty that it would resolve the accommodation shortage. The political consequences of a decision that left tenants vulnerable to eviction at a time when the supply of accommodation was critical were too risky to test. Nor could tenants be expected to tolerate a sudden move by landlords for increased rents, which would be the inevitable result if restrictions were lifted while the housing shortage persisted. Tenants represented a substantial, albeit declining proportion of the electorate: the 1947 census revealed that 48.2 per cent of private dwellings in NSW were occupied by tenants; in 1954, the figure was 37.9 per cent.

Decontrol was to remain linked to the supply of accommodation. The Royal Commission appointed to enquire into the rent control legislation in 1960 reported that, in the situation then current, ample accommodation was available for those in the middle and upper-income groups but that there remained a shortage of accommodation at rents that were within the economic capacity of the lower-income group.[8] By the late 1960s, the lack of alternative housing for protected tenants unable to meet market rents was to present, even for a Liberal Party government, an insurmountable barrier to the total withdrawal of controls.

Administrative problems appear to account for the closing off of a second option, namely, that the formula used in rent determinations be updated. The basic rent for a dwelling, calculated on 1939 values, was used as the basis for

all rent determinations for the dwelling; any change to the basic rent would involve considerable recalculation in each individual case. Rent control had created already a large enough administrative load. In 1952, there were 85,000 applications for rent adjustments; in 1954, the number was expected to reach 30,000 and there was a considerable waiting time before cases could be heard.[9]

A third option, and that taken by most other State Governments, was to decontrol gradually by granting a general percentage increase on all controlled rents and to continue doing so until they reached market levels. Press reports suggest that Cabinet proposals to grant increases in 1951 and 1952 were blocked in caucus.[10] As stated above, the longer controls remained in force, the less attractive this - and the previous - option became. After a long period of rent control, families paying low rents begin to treat a fixed rent as the norm. Their housing expenses remain a steady factor in the household budget and any increase in income is allocated to other areas of consumer spending.

Labor's solution was to instigate a pattern of decontrol that continued full protection for sitting tenants (and their heirs)[11] but released from control properties where no tenant interest was threatened. The first move towards decontrol was made in 1954 with the introduction of section 5A. This section excluded from the operation of the Act any dwelling house the construction of which began after the date of the amendment; dwelling houses that were in the course of construction at that date; and those that had not been let during the period between the introduction of the Commonwealth regulations (7 December 1941) and 16 December 1954.

Prior to 1954, rent control had been universal in its application. Henceforth, the wartime landlord and tenant controls applied to one section of the rental market only, namely, existing rental stock. Section 5A protected the tenant interest but it also changed the nature of the issue. The policy now affected one group of landlords and not another, one group of tenants and not others. It prepared the ground for a system marked by disparities in rents and in landlords' returns. The politics of the issue became more fragmented.

Action by landlords

Following the 1954 amendment, landlords began to form themselves into pressure groups in order to campaign for increased decontrol. In 1954, the Home Owners' League was

formed. It was followed by the Landlords' Justice Association (formed in 1957) and the Flat and Property Owners' Association of NSW. Initially their demands were modest - an increase in the rate of controlled rent, special concessions for landlords in special circumstances and so on. The *Sydney Morning Herald* drew attention to the moderate nature of the proposals and noted the assumption underlying them, namely, that the State Government had no intention of abolishing rent control. Neither, according to the *Herald* did the Liberal Party: each party now had too many supporters who were 'doing very well' out of the landlord and tenant legislation and the voting power of landlords was relatively unimportant.[12]

At the same time, arguments that rent control was having a detrimental affect on the supply of accommodation were gathering momentum. In particular, there were claims that a number of dwellings were being left vacant because owners were unwilling to take in new tenants under rent control conditions. Potential landlords were reluctant to enter a market in which they ran the risk of losing control over the use of their property. Real estate agents were said to be advising their clients against letting flats that became vacant. Also, the requirement that leases of premises decontrolled under section 5A be registered with the Rent Controller, allegedly made investors remain wary of entering into housing commitments as there was no guarantee that restrictions would not be reintroduced.

The Labor Government reacted in 1958 with a long and complicated measure that in effect decontrolled houses and flats of which owners regained possession on court orders obtained without the necessity of the tenant being offered alternative accommodation. That is, dwellings where tenants vacated voluntarily or were evicted on grounds of their own default could now be re-let at market rents. Again, the pattern was to protect the existing tenant interest.

The response highlighted the political saliency of the issue within the ALP. Anti-ministerial forces within caucus and from the industrial wing of the labour movement condemned the move. Efforts to force the withdrawal of the bill included deputations to the Premier, unfavourable motions passed at ALP zone conferences and the formation of an Anti-Eviction and Tenants' Protection Committee under the leadership of Eddie Ward. The dispute threatened to split the State party and to spill over into the Federal arena. A settlement was reached only after the intervention

of the Federal leader, H.V. Evatt, and the introduction of a number of 'safeguards' in the legislation.

'Creeping decontrol'

The 1958 amendments introduced 'creeping decontrol' whereby tenancies were released as they became vacant. It was a form of decontrol that, as stressed already, had the political advantage of not disturbing sitting tenants. It also limited the application of rent control further by restricting its operation to an existing clientele; as that clientele diminished, either through vacation of premises or through natural causes, the premises they occupied became eligible for re-letting as part of the normal private rental market. But it was also indiscriminate in its application. It created different classes of tenants and of landlords. The outcome was that flat buildings, for instance, were occupied by tenants paying different rents for similar accommodation. Whereas some tenants, including wealthy tenants, were paying rents based on pre-war values, others, including young married couples, migrants and other newcomers to the rental market, were paying market rents. Similarly, landlords of controlled premises continued to receive rents based on pre-war values and, if selling their premises, could not sell for the same capital value they would have received had they had vacant possession. Landlords of similar but decontrolled premises suffered none of these limitations. As H.V. Budd put it: 'It would be just as logical to make some law to provide that plumbers whose names began with A should do jobs at half-price for people whose names began with H'.[13]

The irony of Labor's policy of decontrol was that while it weighed heavily on the small landlord, it favoured the rich landlord. With his property and assets, he could take advantage of rent control by buying up controlled premises at prices below the market value, pay the tenant to vacate (or gain possession by less reputable means), and then resell with vacant possession at a profit. As a big landlord was the only one likely to have available alternative accommodation, he was also more likely to be able to gain possession through eviction than the small one-house owner.

Creeping decontrol gave landlords an incentive to get rid of protected tenants. After the 1958 amendment, allegations of harassment of tenants became increasingly common in the parliamentary debates. Those named were certain large property owners and developers, but there is no reason to doubt that 'small' owners also indulged in similar

tactics. It was said that the victims were usually widows living alone. Tactics included telephone calls throughout the night and constant threats.[14]

Abuse of the Act, by both landlords and tenants, became widespread. Malpractices included owners' attempts to gain payment for consent to the assignment of a lease; demands for key money; illegal methods to obtain possession; tenants' use of provisions of the Act to cause delays and complications in eviction cases; and the payment by landlords of amounts varying from $4,000 to $20,000 in order to gain vacant possession.[15] Although many of the alleged malpractices were contrary to public mores, they were not necessarily, in strictly legal terms, illegal. The small number of prosecutions carried through indicates the difficulties of policing the Act.[16]

Wealthy tenants

Because protection of sitting tenants was based on occupancy rather than tenants' means or need for housing protection, no account was taken of tenants' increasing income. By the late 1950s, the legislation had created a new class of racketeer, the wealthy tenant. The Royal Commission *Report* cited the case of a building of thirteen flats where certain of the flats consisted of three bedrooms, a large living room, hall, dining room and closed verandah, kitchen, a separate bathroom, a separate shower room, and two toilet rooms. Those flats in the building that were subject to rent control were let at rents between $19.20 and $24.60 per week while decontrolled rents were approximately $56 per week. Among the tenants benefiting from the controlled rents were one who had occupied 'a very senior position with a large industrial concern of world-wide importance', a 'chairman of directors of a substantial public company' and 'a widow of substantial means or income derived from a well-known company trading in Sydney in popular brands of motor vehicles'.[17]

Complex legislation

These developments caused the legislation to fall into increasing disrepute. The complexity of the legislation was a further cause for criticism and derision. Thirteen amending bills were introduced during the period 1948 to 1965. Most were measures designed to block loopholes revealed through litigation, but inevitably in an area renowned for the amount of litigation it attracts, the band-aid approach to legislative

amendment tended merely to reveal new loopholes and anomalies to be tested in the court, which, in turn, invariably brought forth decisions demanding further legislative attention. The Act acquired a reputation as one of the most complex on the statute book. It was described variously as 'the State's most confused law', 'jungle legislation', 'a legislative monster' and a 'maze in which even lawyers hesitate'. An example of the convoluted language of the legislation - its use of 'foo-language', according to one critic[18] - is section 113 (4), which was inserted in order to clarify the wording of section 113 (3):

> s.113 (4): For the purpose of subsection three of this section, where the doing of any act is dependent on the completion of any preliminary act, the commencement of the doing, or the continuance or completion of the doing, of the preliminary act shall be deemed to be the commencement of the doing of the first-mentioned act.

The Royal Commission *Report* drew attention to the complexity of the legislation and gave several examples of the sort of complicated provisions that, it claimed, made the Act almost unworkable and furthermore, discouraged potential landlords from making accommodation available.[19]

Rehousing low-income tenants

By the 1960s, the main barrier to decontrol was the rehousing of protected tenants whose incomes were insufficient to meet market rents. Rent control had served to provide this group with low-cost housing at no cost to the government. The rehousing of such tenants would become a government responsibility if controls were lifted. The actual number of tenants likely to be so affected was not known. The Royal Commission had estimated that there were approximately 34,000 protected pensioner tenants, of whom 34,500 lived alone and were dependent on the pension as their sole source of income.[20] The Housing Commission resisted all pressure to take responsibility for rehousing any new group of pensioner tenants. The Commission had already a long waiting list of applicants for aged persons' units. Nor was a rent subsidy scheme feasible: the number of likely applicants and the cost were unknown and also, any such scheme ran the risk of stimulating demands from other groups for similar assistance.

The Government could, however, take steps to deal with wealthy tenants. N.J. Mannix, who had replaced R.R. Downing as Minister of Justice, rejected the notion of introducing a new rents formula: 'we do not want these people to have their rents fixed in accordance with an arbitrary formula, which then becomes a formula that lives down through the ages, as in France and other countries that now find they have the tiger by the tail and cannot let it go'.[21] But Labor already had the tiger by the tail. Its 1964 amending legislation resisted the introduction of a new rents formula for the wealthy tenant and, under the new section 17A, set up the machinery by which tenants could voluntarily negotiate a new rental agreement with the landlord.

It was a token gesture. It was already common practice for owners and tenants of business and commercial premises to by-pass the legislation by entering into agreements fixing new rents through a system of payment based on controlled rent plus a premium. Tenants of an estimated 90 per cent of controlled business and commercial premises had entered into such agreements.[22] The impact of the new legislation on tenants of private dwellings is difficult to assess. The bill was introduced in December 1964; at the general election in May 1965, a Liberal Government was returned to office and prepared the way for more drastic decontrol measures.

IV. LIBERAL PARTY IN GOVERNMENT, 1965–1976

A Liberal Government was elected to office at the State general election held on 1 May 1965. Although in the period immediately following the war the Liberals accepted the need for temporary rent control, they had opposed from the beginning the severest of those provisions in Labor's legislation that restricted a landlord's access to repossession of his property. They opposed in particular the introduction of section 70 (2) (the alternative accommodation provision), the restrictions on a new owner's right to issue a notice to quit, the provisions regarding inherited tenancies, and those enabling tenants to profit from subletting.

It was quite contrary to Liberal political beliefs to advocate permanent increased tenant protection. On the other hand, the Liberals could not afford to associate themselves too closely with the landlord's cause. Electorally, the Liberal Party was highly vulnerable on the issue. The Labor Party made full use of election advertisements with headings such as 'Home-hungry citizens are going to be exposed to the

cupidity of Liberal Party landlords' and 'The Liberals want to increase rents!'[23]

Wary of the electoral support for rent control, the Liberal Party throughout the 1950s was forced into the position of promising to maintain rent control if returned to office.[24] It was not until the election of 1962 that the Party was confident enough to advocate decontrol. At that election it adopted the recommendations of the Royal Commission and proposed the complete removal of rent control from business and commercial premises and from residential dwellings let at $10 per week or more. Controlled rents would be increased by 40 per cent. After the election, they claimed that the proposals were partly responsible for their defeat at the polls. A Liberal Party post-election study reported that the rent proposals had been a vital issue and influential in Liberal defeats in four seats and in worsening the Liberal position in three others.[25]

Henceforth, Liberal Party policy adopted Labor's stance that rent control was providing a service to a particular group in the community and that decontrol could not be undertaken unless an alternative form of housing assistance was made available.[26] When a Liberal Government was elected to office in 1965, it was with the promise that there would be no general increase in controlled rents during their first term of government.

Administrative action

The election commitments restricted the Liberal Government's ability to introduce complete decontrol. Also, whilst Labor retained control of the Upper House any legislation seeking to remove section 70 (2) and the other more stringent aspects of the legislation was doomed to failure. Initially, the main thrust was to apply new administrative procedures to the existing legislation. The first target was the wealthy tenant. The Liberals continued the voluntary aspect of section 17A but applied more pressure. Wealthy tenants (defined as those whose gross income was $6,000 or more) were warned that if they did not voluntarily negotiate new rents, they might be decontrolled completely. The procedures adopted instructed the Rent Controller, on an application from the landlord, to send the tenant a questionnaire seeking information as to the tenant's gross income, and the incomes of all other residents over 21 years of age. Tenants who qualified as 'wealthy tenants' were then required to enter into an agreement to pay a new rent, based on

current value.[27] Peter Clyne, a longstanding protagonist of the legislation, described the procedures, aptly, as 'not dissimilar to the ones used by fatherly sergeants of police when they are seeking a voluntary confession'.[28]

The Liberal Party gained control of the Upper House in 1968. The amending bill introduced that year effectively removed protection from all but the hardcore, namely, the low-income and pensioner protected tenants unable to find alternative accommodation for themselves. The legislation incorporated the wealthy tenant procedure into the Act through the introduction of Division 4AA. In future, current market rents could be demanded from tenants whose income reached a prescribed level. In 1965, the wealthy tenant level was $6,000; in 1968 this was reduced to $4,000. It was increased again to $6,000 in July, 1975 and currently (1980) stands at $10,000. Section 5A was revised to extend the categories of decontrolled premises; all business and commercial premises were decontrolled; section 70 (2), the alternative accommodation provision, was repealed; the provisions regarding grounds for issuing a notice to quit were revised and extended; and the right to carry on a tenancy after the death of the lessee was limited to members of the immediate family.

The 1968 legislation shifted the direction of the rent control provisions away from protection of sitting tenants to a policy that placed the onus on the tenant to prove that he or she was incapable of meeting market rents and therefore warranted continued protection. After 1968, occupancy was no longer sufficient guarantee of continued protection. The stringency of the provisions introduced to deal with wealthy tenants[29] and their subsequent impact on protected tenants met little resistance. By 1968, the legislation had become a mockery and rent control had lost its potency as an electoral issue.

The Act continues to be a source of litigation, although not on the same scale as prior to 1968. There are occasional newspaper articles on the plight of aged protected tenants, living mostly in dwellings decaying through lack of repairs and maintenance and waiting to be accepted for Housing Commission aged persons' units. A Labor administration replaced the Liberal Government in 1976. Reform of the 'normal' landlord and tenant legislation is on the new government's agenda but, to date, the NSW *Landlord and Tenant (Amendment) Act, 1948, as amended*, stands as the Liberals left it, to wither away with the passing of the last protected tenant. Long term, the main beneficiaries of rent

control in NSW appear to have been those who bought controlled premises and had the means and the know-how, or the luck, to gain vacant possession.

V. CONCLUSION

The long term impact of rent control in NSW - and in every other known instance - has been exacerbation of a critical shortage of rental accommodation, extensive litigation and embitterment of landlord-tenant relationships.

True to its history as a party less interested in principle and more interested in gaining practical concessions, the NSW ALP Government chose to use rent control as a means of providing low-income housing for a select clientele. The failure to provide for a parallel program of development of some form of State-sponsored low-income housing (either by rent subsidy or provision of accommodation) resulted in an inability to withdraw from a policy that engendered its own, inevitable, perpetuation.

Rent control is most effective as an instrument of redistribution of the rights and obligations pertaining to the relationship between landlord and tenant. Its purpose is to change the balance in favour of the tenant. Used as a housing subsidy to a particular group of tenants it creates the disparities, injustices and anomolies that have characterised its operation.

NOTES

1. There are no reliable data on the number of controlled premises in NSW. The Royal Commission appointed in 1960 to enquire into the impact of the rent control legislation carried out a survey of controlled premises in selected suburbs. The first official survey was authorised by the Liberal Government in 1966. It was conducted by the Rent Control Office and was based on its records of applications for fair rent determinations. Since then, figures have been kept up-to-date as new controlled premises come to light and others are decontrolled. There is no doubt, however, that an unknown number of controlled premises has never been the subject of an application to the Rent Control Office and, furthermore, that an unknown number has never been properly decontrolled via registration of a section 5A lease.

2. L. Neville Brown, 'Comparative Rent Control', *International and Comparative Law Quarterly*, vol.19, April 1970, p. 209.
3. see *Official Year Book of the Commonwealth of Australia*, no.37, 1946-47,pp. 1197-2000.
4. see for example, NSW *Parliamentary Debates*, vol. 187, 28 July 1948, pp. 3377, 3394; 4 August 1948, pp. 3576, 3583.
5. On the seriousness of the housing shortage, especially in NSW, see, Department of National Development, 'The Housing Situation', Commonwealth of Australia, Canberra, 1956.
6. see Marian Bowley, *Housing and the State 1919-1944*, Allen and Unwin, London, 1945.
7. M.A. Jones, *Housing and Poverty in Australia*, Melbourne University Press, Melbourne, 1972, pp. 118-122, and *Sydney Morning Herald*, 29 June 1956, p. 5.
8. *Report of the Royal Commission of Inquiry into the Operation and Effect of the Landlord and Tenant (Amendment) Act, 1948, as amended*, Government Printer, Sydney, 1962, p. 19.
9. *Sydney Morning Herald*, 12 January 1953, p.2, and *Sun*, 4 May 1954, p. 9.
10. *Sunday Herald*, 11 November 1951, p. 4; *Daily Telegraph*, 28 December 1951, p. 8; *Sydney Morning Herald*, 19 March 1952, p. 5.
11. The Act provided that, following the death of a lessee, a controlled tenancy could be passed on to spouse, children, parents or any person who had resided in the dwelling for the previous two years (sections 83 and 83A). The provision was designed to provide protection for the tenant's dependants. However, according to the *Report* of the Royal Commission, such was the complexity of the provision that it worked so that a tenant could by will bequeath the tenancy of the premises to a person who was neither a relative nor a resident at the time of death. *Report*, op. cit., p. 60.
12. *Sydney Morning Herald*, 25 October 1957, p. 2.
13. NSW *Parliamentary Debates*, vol. 55, 9 December 1964, p. 2824.
14. For an account of various harassment activities on the part of landlords, see 'ACOSS Study on Landlord/Tenant Relations' (prepared by Kate Holland), Submission to the Commonwealth Commission of Inquiry into Poverty, Australian Council of Social Services, Sydney, 1974 (mimeo).

15. *Report*, pp. 31-32
16. *Ibid.*, p. 31.
17. *Ibid.*, pp.45-46.
18. Peter Clyne, *Practical Guide to Tenancy Law*, Rydge Publications, Sydney, 1970, p. 99.
19. *Report*, p. 31.
20. *Ibid.*, p. 45.
21. NSW *Parliamentary Debates*, vol. 55, 8 December 1964, p. 2763.
22. *Report*, p. 53; and NSW *Parliamentary Debates*, vol. 55, 8 December 1964, pp. 2772-2773.
23. *Sydney Morning Herald*, 1 February 1953, p. 6 and 10 February 1953, p. 6.
24. see for example, *Sydney Morning Herald*, 18 March 1959, p. 11 and 21 March 1959, p. 4.
25. Legislative Council Office, New South Wales, *Record of the 40th Parliament*, (6 April 1961 to 21 March 1965), revised, NSW Government Printer, Sydney, 1965, p. 26.
26. see for example, NSW *Parliamentary Debates*, vol. 55, 8 December 1964, p. 2788.
27. NSW *Parliamentary Debates*, vol.57, 26 August 1965, p. 156.
28. *Sydney Morning Herald*, 3 December 1969, p. 13.
29. see W.J. Geraghty, 'Tenancy Law Without Justice', Sydney 12 April 1973 (mimeo); Australian Government Commission of Inquiry into Poverty, Law and Poverty Series, *Poverty and the Residential Landlord-Tenant Relationship* (research report by Adrian J. Bradbrook), Australian Government Publishing Service, Canberra, 1975.

Chapter 9

Rent Control in Microcosm
The Case of Canberra

The Real Estate and
Stock Institute of Australia

Rent Control in Microcosm

The Case of Canberra*

I. AIM OF RENT CONTROLS IN THE A.C.T.

The responsible Minister at the time of the introduction of rent controls in the Australian Capital Territory was the Hon. K.E. Enderby, M.P., Q.C. In assessing the effects of these rent controls it was considered most relevant to know the aim in introducing them. Consequently Mr Enderby was asked if he would give the reasons for the introduction of these controls and the essential paragraphs of his reply are reproduced here with his permission:

> I caused the system of rent control to be re-activated in the A.C.T. at a time in 1973 when there was a great shortage of rental accommodation and when the rentals being charged were unreasonably high.
>
> In doing this I sought to maximise the opportunities of low and middle income earners in need of rental accommodation to have access to that accommodation at a reasonable rent. The market in rental accommodation in Canberra in 1973 was not working in that direction.

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* Adapted from *Rent Controls: A Study of the Effects of Rent Controls in Canberra* published in 1975 by the then Real Estate and Stock Institute of Australia. The selection is basically Chapter 7 (Conclusions) of the study.

> The thinking behind my action was to limit the opportunities for exploitation which existed at that time, while providing substantial increased funds for the construction of substantially increased quantities of rental accommodation. Unfortunately the land boom and the inflationary situation that hit Australia during late '72 and throughout 1973 meant that the pressure on our resources was such that the increased funds did not produce the increase in the number of houses built. That pressure on resources has only recently diminished and it is confidently hoped that the increases in numbers of houses and flats will shortly be seen.

Restraint of rent increases

Certainly rents in the private sector in Canberra have not risen significantly since rent controls were introduced, while there have been noticeable rises throughout the rest of Australia. Even if to the average rent is added the administrative costs in the public and private sector arising from the implementation of the Ordinance, the effective increases in rents are still being restrained much more than is evident elsewhere in Australia.

The low and middle income earners

Governments have accepted as a social responsibility the provision of housing for low income earners. Most low income earners find their rental accommodation through State Housing Commission or their equivalent at the Federal Government level in the Australian Capital Territory and the Northern Territory.

Considering that in the Australian Capital Territory more than half the rental accommodation is provided by the Government, it is difficult to follow the reasoning behind introducing rent controls which affect only the private sector, and so prevent the rents from rising when this class of rental accommodation has been and remains beyond the low income earner.

Restraining rents below the free market equilibrium level may offer some relief to the middle income earner, but it becomes a matter of definition. If the middle income earner is considered to be a male on average weekly earnings, which at the time rent controls were introduced was $143.50

in Canberra, then even the middle income earner could barely afford to seek accommodation in the private sector, unless he was receiving a subsidy from his employer or there was a second income earner in the family (both not uncommon in Canberra). At the date of this report, to become eligible for rental accommodation in the public sector, the weekly earnings must be well under the average which puts the middle income earner into the private sector for rental accommodation. The government is simply not coping with this problem and rent controls do not relieve it, except that with rapidly rising wages and fixed rents the middle income earner and for that matter, the low income earner, will eventually be able to afford to rent in the private sector - the only problem being that there will be little private rental accommodation available.

Since rents in the private sector are beyond the low income earner and some in the 'middle income' bracket, then it certainly behoves the public sector to construct more rental accommodation. Mr Enderby had recognised the need for this as he mentioned the provision of increased funds for the construction of greater quantities of rental accommodation. For various reasons, some of which are mentioned by Mr Enderby, the construction in the public sector has not met the need nor has it been keeping pace with the increase in population in Canberra.

Rent controls do not really affect the Canberra low income earner whose needs are met by the public sector. The middle income earner may get some relief but he is not catered for by the public sector and must still struggle if he is to rent in the private sector.

It is the high income earner that has been helped as the rent controls have restrained the housing component of his living cost. It does seem odd that the controls best help those who can best afford to pay.

II. INVESTMENT

Loss of private investors

It would seem however, that a fundamental point has been missed in the introduction of these rent controls.

It is well known from overseas experience and from experience in Australia, when rent controls existed during and after the Second World War, that these controls will drive out the private investor. Insufficient recognition appears to have been given to this matter and the result is undoubtedly

that private investors are abandoning Canberra.

Even if the government had managed to increase its supply of rental accommodation, the fall-off in the private sector was not being overcome. There would be a need for a very marked increase in government rental accommodation to offset this loss in the private sector. This loss in the private sector would be absolutely disastrous in areas outside of Federal Government control where 75 per cent of rental accommodation is provided by private investors.

But even in Canberra, where some 58 per cent of the rental accommodation is provided by the Government, it still needs a very large increase in the public sector expenditure on rental accommodation to overcome the loss which arises in the private sector because investors no longer find it profitable. As it is, total housing construction is falling whilst the population is growing.

So although part of one aim has been achieved in introducing rent controls (some benefit to some middle income earners), there has been a very marked increase in the shortage of rental accommodation in Canberra - a shortage which is greater than anywhere else in Australia and this can be attributed only to the introduction of rent controls.

Supply and demand

It is widely accepted by economists that the introduction of controls merely treats the symptoms and not the causes of the problem.

The two symptoms which were identified to the Minister were the high rentals and the shortage of rental accommodation. It cannot be disputed that the rentals at the time were somewhat higher than average for Australian capital cities, some of which might be explained by the higher cost of construction in the A.C.T. However other reasons could exist: Lindbeck comments that short run equilibrium rents tend to be rather high during periods of rapid economic growth and substantial shifts in inter-regional distribution of population[1] - economic growth was high and Canberra's population was increasing rapdily; also Gelting points out that "in periods of rapidly rising aggregate real income a housing shortage . . . is apt to rise"[2] - this rise was taking place and the average male weekly earnings are higher in Canberra than in any other capital city in Australia.

However, discussions with many property managers and the survey of classified advertisements did not indicate that there was any grave shortage of rental accommodation

at the time the Minister made his decision. For example, an advertisement for vacant premises during the first half of 1973 might have resulted in a few responses, often groups. This is in very marked contrast to the situation today where owners and property managers have relatively little need to advertise and indeed are sometimes reluctant to do so because of the vast numbers that will respond.

It is a basic economic fact that excess demand can be relieved by increasing the supply. Even if rental accommodation was short in Canberra, something which does not seem to be proven in 1973, then the way in which to have prevented rents from rising unduly was to have had a marked increase in the provision of rental accommodation. While the public sector made some attempt in this regard, there would be a need for substantial increase from this sector, as well as the private sector. In addition to a large injection of public funds for housing, the increase could have been achieved by making it attractive for private investment to have undertaken construction of rental accommodation. In fact, the exact opposite has happened - there has been every disincentive for the construction of rental accommodation by the private sector.

It would seem that there was insufficient appreciation of the relatively small contribution made to the total housing stock by one year's production. In June 1973 there were about 47,000 dwellings in Canberra so the 773 dwellings completed by the public sector between 1 October 1973 and 30 September 1974 added only a little over 1.6% to the total stock.

There would be a need for a massive increase in public expenditure to overcome the reduction in private expenditure on rental accommodation. As it is, at this stage the total construction of rental accommodation is just not keeping pace with the growth of Canberra. With the downturn which is taking place in building in the private sector, which is unrelated to specific Canberra problems, and the projections of population growth, it seems that the accommodation shortage can only get worse in Canberra.

Additional disincentive

It would seem also that one new tax by the Australian Government will exacerbate the situation in Canberra. This tax will affect investment throughout Australia but the critical situation in Canberra is certainly going to be that much worse. The tax is a surtax on income that is derived

from rents.* With this new tax introduced it would seem that the public sector's problems in meeting the private sector fall-off in Canberra are going to increase even further and rental accommodation will become even shorter.

III. RENT SETTING

Fair rent

There have been a number of methods applied in attempting to determine a fair rent.

The mechanistic formula which was used by the Rent Controller can give a figure unacceptable to a tenant or to a landlord. It was only one guide used by the Rent Controller in making his determination but it included arbitrary figures for return on valuation, maintenance, etc. and can easily be unrelated to reality.

The Rent Controller's approach to determining a fair rent now relies heavily on statements made in *Rathborne V Abel.*[3] In a press statement of 22 January 1975, the Rent Controller said:

> In *Rathborne V Abel* the High Court (per Barwick C.J.) said that the direction to have regard to the list of matters was no more than a direction to consider each of the matters and determine whether any or any particular weight should be given to them.
>
> The Chief Justice also said that the wide discretion granted by certain sections of the legislation would make the adoption of some mechanical formula by which to calculate the fair rent highly inappropriate.
>
> Consequently the Rent Controller considers he is bound not to determine fair rents by means of a formula, but to consider the matters in Section 20 disjunctively . . .
>
> The Controller does give great weight to the rents of comparable premises in the locality.

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* Editor's note: As it happened, this tax on 'unearned income' was not introduced.

However *Rathborne V Abel* was related to a situation of relatively few rent controlled properties in an otherwise free market. In that situation, comparable rents could have had some significance but where the market is totally controlled, as in Canberra, then comparable rents are meaningless because they are not determined in a free market.

It is noted in passing that despite the Chief Justice's statement regarding the inappropriateness of a mechanical formula, it continues today to be used by the Rent Controller's Office and the Fair Rents Board in Sydney, New South Wales, for determining a fair rent on the declining number of premises still controlled.

In the Introduction to *Verdict on Rent Control*,[5] there is comment on this matter:

> Unfortunately, there is also an inevitable tendency for 'fair' rents to be determined by the 'fair' rents already established for comparable properties in the area. This form of economic incest is common to most forms of valuation based on statutory rules. What it means in effect is that situations of shortage are not only perpetuated but also likely to be exacerbated unless further compensatory 'rules' are established.
>
> In these circumstances there is little comfort to be drawn from the observed result that many applications to Rent Officers have produced increases in rent. What matters for investment incentives is the return achieved: not whether rent has been increased but by how much. A reduction in a rate of slide downhill does nothing much for morale if everyone else is climbing.

While controls remain in a totally controlled rental accommodation situation, only the use of a formula offers scope for determining a fair rent. A fair rent can be readily determined by allowing supply and demand forces to operate in the market place. Protection to the tenant and landlord can easily be afforded by other simple legislation which does not generally interefere with the market.

IV. SIDE EFFECTS

Black market

There seems no doubt that the community is now experiencing undesirable practices such as bribes, key money and the like. The provision of more rental accommodation and the elimination of rent controls will eliminate the black market.

Property management

Property mangement is becoming, or in some instances has become unprofitable.

One tendency is for fees to rise so that property manager's ever-increasing overheads can be met from stagnant rents. The return to the owner will therefore diminish providing further disincentive to invest.

A second tendency is for there to be fewer property managers. There will be increasing difficulty, especially for the owner temporarily transferred from Canberra and wishing to let his home, in obtaining these services.

Group accommodation disappearing

The rent controls will virtually eliminate accommodation for groups unless there is recognition by the authorities that a higher risk is involved for the landlord.

The landlord and the tenant

The notion seems established in the minds of those who propose landlord and tenant legislation (anywhere, not just in Canberra) that there exists a very unbalanced situation of an innocent tenant at the mercy of an unscrupulous landlord. It would seem that only some such notion could be responsible for unnecessarily cumbersome and costly introduction of rent controls in Canberra. The truth is that, while examples to the contrary can always be found, tenants are well aware of their rights and responsibilities and avenues for correcting injustices, and landlords seek a reasonable return on their investment from reliable tenants.

Removal of controls

The rental accommodation shortage has become critical in

Canberra and if rent controls are suddenly abandoned there is likely to be an increase in rents. This simply illustrates another classic economic objection to controls - when the controls are eventually removed the situation can be worse than that which existed before the controls were introduced.

The present rental situation is not going to be corrected by government expenditure and the situation is rapidly getting worse. Private investment in rental accommodation is essential and a prerequisite is the removal of the rent controls. But they will now have to be phased out, and adjusted during the period to provide a reasonable return, whilst there is a substantial encouragement to invest.

Existing high interest rates provide a further discouragement to investment at present but they could return to acceptable levels within the time taken to dismantle the rent controls and to make the land available.

The provision of low interest finance to prospective home owners would reduce their requirements for rental accommodation and further ease the situation.

V. CONCLUSIONS

A major effect of creating a housing shortage because of the marked reduction in the construction of rental accommodation by private investors has been demonstrated in the Canberra situation. One interesting result of the study has been the short time within which this effect has become apparent.

Other effects have become apparent too: the emergence of a black market, matters related to occupancy criteria and some of the elements of waste. It is also obvious that the controls have not been effective in helping the low income earner and do in fact provide more benefit to the higher income earners.

Although there have been reports of some landlords reducing maintenance, it is too early for accelerated property deterioration to have become apparent. However the existence of the effect is well established and there is no reason to expect that Canberra can avoid it.

Recommendations

There is clearly a need for some urgent actions within the framework of a coherent housing policy:

1. The first is to make vast increases in the supply of rental accommodation in Canberra. Government expenditure alone appears quite incapable of meeting this requirement and so there should be every incentive to encourage the private investor to once again build rental accommodation in Canberra. The retention of rent controls will alone prevent this action.
2. So long as rent controls remain in force, the determination of the fair rent must be related to an index so that the owner is given a return which is related to current prices. If this is not done there will be a continuing withdrawal from the private sector. (This will provide for some home ownership as rental properties are sold, offsetting current reduced construction, but will further reduce the supply of rental accommodation.
3. Home ownership should be encouraged to reduce the demand for rental accommodation. This implies increased government allocations to home loans, lower interest rates on housing loans, and increased value of loans or other assistance to overcome the deposit gap.
4. Rent controls must be phased out during which period the restored incentives to private investment are allowed to take effect so that the supply of rental accommodation catches up with the demand.
5. More efficient and equitable means should be introduced to assist low income earners, such as a rent subsidy. This will allow a free market to operate and investment will not be driven away.

NOTES

1. A. Lindbeck, 'Rent Control as an Instrument of Housing Policy' in A.A. Nevitt (ed.) *The Economic Problems of Housing*, Macmillan, New York, 1967, p. 53.
2. J.H. Gelting, 'On the Economic Effects of Rent Control in Denmark', in A.A. Nevitt (ed.), *op cit.*, p. 85.
3. *Australian Law Journal Reports*, Vol. 38, pp. 293-307.
4. F.G. Pennance, 'Fifty years, five countries, one lesson', Introduction to; Arthur Seldon (ed.), *Verdict on Rent Control*, Institute of Economic Affairs, London 1972, p. xv.

Chapter 10

Wheeling and Dealing Under Rent Control

R.H. Webster

Wheeling and Dealing Under Rent Control*

R.H. Webster

In actual practice, residential rent control has the reverse effect to that intended by those who impose it. While existing tenants become an elite group, there are many who suffer as a result of controls. The most seriously effected come from those groups comprising young couples who want to get married, families on low incomes who cannot get a Government house, young people starting out in their careers, students, newcomers to a city, pensioners and widows. While protected from high rents, they cannot find a home.

Few people understand the real implications of rent controls. Those who have had long and intimate experience of this type of legislation know that there are inevitable and inescapable side-effects which counter any advantages. It is a constant source of wonder to those who have close experience of rent control that any Labor Government would permit it, much less advocate it. I would go as far to say that there is nothing with which I have been associated which brings out the worst characteristics of human nature more

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* This paper is an amalgamation of two papers written by R.H. Webster in 1975. They were titled 'Wheeling and Dealing Under Rent Control' and 'Rent Control - Who Really Benefits?'. They were offered to a Canberra newspaper at the time rent control was in operation in the Australian Capital Territory, as Mr Webster wished to warn of the dangers inherent in rent control. The newspaper refused to publish the papers, disbelieving their contents.

than the control of rents.

Rent control undoubtedly leads to a shortage of rental accommodation. The advantages of a manipulated low rent and over-emphasised security greatly increase the attraction and the demand, while the lucky tenant is much less likely to leave, even forgoing promotion or a change of jobs to retain the benefits. On the other hand, if the landlord can get vacant possession by any means, legal or otherwise, he immediately sells the dwelling to the ever more avid homeseeker and it is never again available for rental. Furthermore, no new houses will become available. Who would leave money invested in a rent-controlled house when riskless and less bothersome investments yield a higher return? The exodus of private investors means that the provision of rental housing is left to the Government.

There will be a queue for every house that becomes available. Landlords, who get the same rent whoever they put in, will select childless couples, relatives or friends. Those in genuine need will go homeless or make other, less satisfactory, arrangements.

In addition to the elite group of sitting tenants, there are many 'sharks' who gain from rent control. Being prepared 'to go on the black market' and take advantage of growing numbers of desperate homeseekers, the 'sharks' seek the 'hot money'. Illegal deals are extremely difficult to stop. Tenants will be happy enough to enter illegal contracts if it means having accommodation, probably at a rent no greater than they would be willing to pay on the free market. Many estate agents will wash their hands of illegal transactions and will withdraw from rental housing matters. It is mainly the 'sharks' who remain.

Many of the problems with rent control can be illustrated by reference to the vicious social catastrophe created by post-war landlord and tenant legislation in New South Wales. While wartime legislation was a necessity, the 1948 *Landlord and Tenant Act* had disastrous consequences. I had plenty of opportunity to study the mess. Because of my job as auctioneer for the biggest real estate agents in the country, I was right in the middle of it.

The pegging of rents at 1939 levels, while building costs and all prices had inflated, was at the root of the problem. Most tenants had greater equity in the property than the owner. Hence the battle for tenancies became a savage struggle with big rewards for the victors. The inevitable 'sharpies' made fortunes from the cruel and often criminal exploitation of desperate and frustrated

homeseekers.

When a tenanted property was sold, the tenant had to be offered the property at the agreed price.* Only if he refused it, could it be sold to anyone else. Hence most tenanted properties were put up to auction where the tenant had to bid if he wanted to buy, although his tenancy was still preserved. Otherwise most of the transactions contained a secret cash payment somewhere, a cash gift with no witnesses, an under-the-lap sale of furniture at an inflated price, a substantial gift in no way connected with real estate. There seemed to be no shortage of methods of evasion and no chance of proving an illegality. Both parties were equally guilty in law.

Two classes of people not restricted by the legislation were returned servicemen with no money and large families, and Totally and Permanently Incapacitated (T.P.I.) people. They could obtain vacant possession of a house they owned. I knew one character who cashed in on this.

When he saw a cheap tenanted house advertised for sale he would make a detailed inspection, wearing shabby clothes and a Digger's slouch hat, prominently displaying a T.P.I. badge and with several grubby kids in tow. Tenants were always well aware of the legislation and he would frighten them into believing that if he bought they would get no compensation, and would be evicted immediately. He would make a tough arrangement with the tenant to get him to quit voluntarily. Then he would buy the place for peanuts at the auction, because if the tenant did not bid there was rarely any competition, except from speculators, who attended every auction in the hope that a tenant would not bid too high. I suspected he was a phony. He looked healthy enough to be a life-saver and he brought different kids on inspections.†

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* Editor's note: The nature of this 'agreed' price is of special importance. In fact, under S.88A of the Act this was 'a price not greater than the price at which the premises are actually sold or agreed to be sold'.

† Editor's note: If the tenant was so aware of the special powers of the T.P.I. pensioners, then why didn't he bid against them at auction? This strategy would seem to be in the best interests of the tenant.

Immigrants and rent control

If the home-grown 'shark' was tough, he was well matched by some of the migrants. Many of these came from poor and war-ravaged countries and had been forced to live by their wits all their lives. Even if they could not understand English, many could understand *Landlord and Tenant* legislation. I can describe the method used by one group to get themselves a flying start in their new homeland.

A family would pay 'key money' to get the tenancy of a terrace or semi-detached house. Three or four families, with children, would then move in. They would harass the neighbours with brawls, late parties, acts of indecency, trucks and cars parked in gateways, and even threats and insults to the women-folk when they met them on the street with no witnesses. Soon the neighbours would leave in disgust. The group would take over the vacated flat and set to work on the next. An effective display of the 'domino theory'.*

There was a well-to-do bottle-o, who, whenever he got a few pounds together, would buy a tenanted slum house in Redfern, Waterloo, The 'Warren', or some similar decrepit area. The going price of such a tenanted house in derelict condition was about £200 ($400). When he died he had 119 of them and the Estate had no money to pay probate, which was based on the 1939 vacant possession Valuer-General valuations plus a small increase later on. The trustees put them to auction in batches. Most were sold to the tenants. Whoever the *Landlord and Tenant Act* was supposed to protect, its a fact that many of these tenants came from European countries. They made a killing, paying as low as four or five hundred dollars a house and getting up to five thousand with vacant possession, at the cost of a few gallons of war-disposal paint.

Serviced flats

One housing section not included in the controls was the serviced flat, which was treated as a boarding house. Unscrupulous tenants of big houses in handy areas like Mosman and Strathfield would let serviced rooms, which

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* Editor's note: Presumably, the reason why the landlord did not sell the vacated house was because its value was depressed by the bad neighbours just as much as it was by rent control. Otherwise, the landlord would sell.

included a meagre breakfast and rough cleaning in the rental. They would get more for each room than the landlord was getting for the whole house. The sub-tenants rarely complained because they considered themselves lucky to get any accommodation.

To regain possession

Some tenancies went on into the second generation of families, which was legal, or through several lucrative changes of tenancy which was not. The landlords seldom gained possession and then only after expensive and protracted litigation. Later, however, the law was amended to allow landlords to get possession if they could prove that the tenant was wealthier than the landlord. It took some proving!

The Act provided that the mortgage gaining possession through the mortgagor's default in payment or failure to comply with the mortgage conditions could eventually get an eviction order. Without this clause no owner of a tenanted house would have been able to raise money on the security of the house because his equity and control weren't good enough. Another clause stated that if a landlord offered to sell the house at a 'reasonable' price and under conditions which he could afford, the tenant had to buy or face eviction. So the canny landlord would offer to sell the house to the tenant on £1 deposit, a time limited mortgage for the balance, and interim payments equal to the rent he was paying. The reasonable price was the Valuer-General's valuation which, while only about half market value, was still more than the price subject to tenancy. The tenant had to accept, and the landlord had to get his money so long as he was patient. At least he was freed of the cost of maintenance, rates and other outgoings.

Tenants of old, dilapidated houses would threaten to take owners to court to enforce expensive improvements, which would result in the owner outlaying more than the rent he could recoup. He would often unwillingly have to sell to the tenant, who was in the box seat in the deal and got a windfall.

A motor manufacturing company from England started a huge motor works in Sydney and sponsored many first class mechanics as migrants from the Old Dart. To house them they purchased a large block of new, vacant flats in Neutral Bay, one of the few blocks built then. The newcomers were bonded to the company for two years, but as soon as that

period was up they hawked their skills on a starved labour market and nearly all left for other employment. The company found itself subsidising the rent of people no longer working for them, but still protected by the tenancy legislation.

They called my firm in to advise them of the best manner in which to dispose of the property. About that time the Government had amended the Act to make it legal for an agreed amount of key money to be authorised by the court (surely the ultimate confession of defeat!). The flats were very saleable and vacant accommodation had increased greatly in value so we advised the company to offer each tenant an amount of key money which would be sufficient to pay a deposit on a new house in the booming outer suburbs. The company agreed and the tenants all accepted with alacrity. Prior to completion of the deal, however, a couple of tenants saw a chance of forcing an even more generous result. They refused to accept the offer and vacate unless they were paid about twice what they had agreed to previously. The company refused point blank and even though the other twenty-odd bitterly disappointed tenants tried to pay off the black-mailers themselves, the deal fell through. The company auctioned the whole building to the highest bidder. I heard later that the buyers converted the flats to strata unit title, and using all the tricks of the control-wise owner, drove a much tougher deal with each tenant individually.

These are just a few of the lurks that were employed. No matter how much skill the legal draftsmen exercised in their efforts to close the loopholes the ingenuity of the 'sharks' was equal to the occasion. Books could be written about the double-crossing, reneging and violence which followed the rich trial of 'hot-money', and the devious deals that took place.

Besides its emotional and sociological appeal, rent control is said to have attractions as a redistributor of wealth. It must be the most inefficient, costly, and callous method ever devised.

PART III

RENTAL MARKET REGULATION

Chapter 11

Regulation: History and Overview

Robert Albon

Regulation: History and Overview

Robert Albon

I. RENT CONTROL AND 'RENTAL MARKET REGULATION'

Rent control

As it has been known in Australia, rent control involves the very rigid regulation of dwelling rents, coupled with severe constraints on a landlord's ability to evict tenants. Commonly, rents have been frozen at the level which prevailed at a prescribed date and a rent controller is frequently given the task of making rent determinations based on the capital value of the dwelling at that prescribed date. Increased outgoings (on rates, insurance and maintenance) are normally accounted for in making determinations. However, the use of base period capital values has the effect of holding capital values down to levels prevailing at the prescribed date. Where free market capital values are rising (as they typically have where rent control has prevailed), there is a big incentive for landlords to evict tenants and sell their properties to an owner-occupier, yet they are frustrated by eviction controls which only allow the landlord right of repossession on certain grounds (such as inability of the tenant to pay rent or the landlord requiring the dwelling for his own occupation). The specified grounds have commonly only provided a *prima facie* ground for eviction and considerable notice has typically been required.

Rental market regulation

'Rental market regulation' usually involves some form of rent control which is not particularly rigid. For example: tenants may have the right to seek a 'fair rent' determination based on the dwelling's current capital value; annual rent increases may be limited to some maximum percentage; the periodicity of rent increases may be restricted; and considerable notice of rent increases may have to be given. The regulators do, however, refrain from blanket rent freezes and rent determinations based on unrealistic base period capital values.

Severe eviction controls are part of the regulator's portfolio. Regulatory legislation specifies allowable grounds for eviction and periods of notice required to attain evictions. Landlords may be able to get around these controls by raising rents in an attempt to encourage a tenant to leave 'voluntarily'. However, this may not be possible where there is also some form of control on rents or rent increases.

Interference and supervision

In addition to rent and eviction controls, regulators attempt to control many other aspects of the landlord-tenant contract the security bond system being a popular candidate for attention. Security bonds are often seen as a hangover from the days when 'key money' was demanded from tenants seeking to lease controlled premises. Their real purpose, is, of course, to act as an insurance policy. Often the regulation limits the size of a security bond to some maximum, usually a multiple of the weekly rent. In addition, the government may establish a 'bond bank' and require all bonds to be lodged with this fund. The regulators may then supervise the size and return of bonds, as well as expropriating the interest income.[1]

Another area of intervention is in relation to repairs. In some cases, tenants are able to withhold rent payments to finance repairs they deem necessary. Regulations regarding repairs may take other forms as well, such as compulsory repair orders.

The regulatory machinery may contain other items. For example; the right of entry of the landlord or his agent may be controlled; parties to a tenancy agreement may be required to enter a written lease arrangement; parties may be forbidden from 'contracting out' of provisions in the

legislation; and discrimination (for example, on the basis of a potential tenant having children) is often outlawed.

While even many proponents of rental market regulation are aware of the horrors of 'rent control', they can see no wrong in 'regulation'. Indeed, by some mystical process, rental market regulation is believed to create benefits for both tenants and landlords. It is a little difficult to concur with this view.

Implications of regulations

The possible implications of rental market regulation are discussed at length in this section by Ross Parish who concentrates on the short-run effects of the enactment of the regulations proposed in the Victorian *Residential Tenancies Bill of 1978*. In the short-run a subtle form of market adjustment can be expected to take place. The enhanced rights of tenants will lead to an increased demand for rental accommodation while the extra costs borne or anticipated by landlords will cause them to seek higher rents. If the market is allowed to adjust in this way, rental housing will become more scarce while rents will tend to rise. However, these adjustments may be thwarted: controls on eviction may prevent dwellings from being withdrawn and controls on rents may cause rents not to rise. If rent control provisions are widely used, then de facto rent control may subsequently arise. Rent control (proper) is also a strong possibility if policy-makers respond to the short-run effects on rents by stiffening up controls on rents.

II. OVERSEAS CASES

Canada

The early and enthusiastic involvement of certain Canadian provinces with rental market regulation makes it possible to dub this type of legislation, with some justice, the 'Canadian Disease'. The provinces which enacted regulatory legislation include Ontario, British Columbia and Quebec. Ontario's laws were first enacted in 1970. A great debate has taken place in Canada, the extent of which can be gauged by observing the bibliography in a publication of the Canadian Council on Social Development.[2] The CCSD has argued strongly for what it calls 'rent regulation' while groups like the Fraser Institute[3] and the Urban Development Institute have been firmly opposed to such legislation. Victoria's

Community Committee on Tenancy Law Reform has drawn heavily on the alleged success of Canadian legislation to bolster its case for reforming Victorian landlord and tenant law.

U.S.A. and U.K.

In the United States, New York City's rent control has attracted much attention, and a system of controls in Massachusetts has long been in operation. Very recently, however, a mania for regulation has swept the country. The pro-control movement has been able to boast the vocal support of such celebrities as Jane Fonda who has argued for the removal of the 'greed quotient' which she claims is inherent in rents.[4] The American push for regulation of rents has had most success in California - the home of 'Proposition 13'. According to the regulation agitators, tax reform and the rent control movement are not unrelated. They argue that property tax cuts have not been passed on to tenants.

We have already seen, in the study by Cooper and Stafford, that the United Kingdom's legislation has elements of both 'rent control' and 'rental market regulation'. The United Kingdom has tried to define 'fair rent' objectively and has very rigid security-of-tenure provisions.

New Zealand

In New Zealand, there seems to be considerable support for regulation of the landlord and tenant relationship, legislation having been enacted in 1972 and 1973. In two recent articles, B.H. Easton, and R. Stephens, were broadly in favour of some form of control.[5] Easton saw 'rent controls as a viable form of social policy',[6] while Stephens suggested that 'some form of limited rent control could be advocated, as the usual criticisms are less applicable'.[7] Support for regulatory legislation also seems to come from the legal profession. In a collection of studies on landlord and tenant law, P.B.A. Sim assets that the 'social rationale of rent control lies in the fact that . . . land is a commodity which we all need but cannot afford to own'.[8] Sim also asserts that landlords have a bargaining superiority over tenants. With 'facts' like these, the case for some form of control seems beyond dispute.

Soon after the Labour Government came to power in 1972, they established Rent Review Regulations, and Rent Review Authorities were set up within the Department of Labour. Tenants could appeal against rent increases which

had occurred since April 1 1972 (inclusive) and only rent increases which could be shown to be due to increased costs were allowed. The Regulations also imposed maxima on rent payments in advance and on bonds, disallowed evictions where tenants had made an application under the Regulations, allowed tenants to recover any excess payments, and disallowed 'contracting out' from the provisions of the Regulations.

The Regulations evoked little response from tenants. According to Frame and Harris, the 'government was clearly expecting a great number of applications, and must have been disappointed (and perhaps more than a little bemused) when only 208 applications for review were received by early February 1973 . . .'[9] Not to be deterred, the government began work on the *Rent Appeal Act* which came into force on February 1, 1974. This Act has all the characteristics of the archetypical rental market regulation scheme. Rent Appeal Boards were established to set 'equitable rents' namely, 'that rent which . . . a reasonable landlord might expect to receive and a reasonable tenant might expect to pay'. Rent determinations did not have to be sought and remained in force for 12 months when made. In relation to evictions, the Act said little. Evictions were disallowed if the tenant was exercising his rights under the Act (e.g. applying for an 'equitable rent' assessment), and in practice this has meant that a landlord attempting to gain possession has had to prove that he was doing so for reasons other than those resulting from a tenant exercising his rights under the Act. The Act, like the Regulations, placed a limit on advance rent payments and on security bonds. Receipts had to be given for all payments and tenants could deduct 'excess payments' from their rent. Payment of key money, and discrimination against tenants with children was made illegal.

III. THE ORIGINS OF AUSTRALIAN RENTAL MARKET REGULATION

Commission of Inquiry into Poverty

If we seek internal origins of rental market regulation in Australia we need not look beyond the Commission of Inquiry into Poverty* and the growth of the consumer protectionist

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* Often known as the Henderson Report after its Chairman Professor R.F. Henderson of Melbourne University.

movement. Quite clearly, advocates of this kind of interference in the private rental market see it simply as another branch of 'consumer protectionism'. Rental housing is one of many products where consumers are susceptible to falling prey to avaricious traders. It was inevitable that the oldest bogey-man of them all - the landlord - would eventually attract the attention of these 'guardians' of the consumer's interest.

The Poverty Commission was clearly not in favour of rent control, despite suggestions made to it that 'there should be a major extension of measures of rent control'. Rent Control was rejected for three reasons: (i) landlords will 'have a clear incentive to get rid of their tenants'; (ii) rent control 'can lead to landlords attempting to cut costs by not spending money on maintenance'; and (iii) 'even more serious is the overall effect of a sharp reduction in the supply of rental accommodation'. I can only concur with the Commission when it concludes that 'we do not agree that rent control is in the long-term interest of tenants'.[10]

It is also easy to agree with the Commission when it maintains 'that the market mechanism does operate, with imperfections for private rental housing', and suggests that 'many of the problems of low income private renters result from their low incomes'.[11] Here the agreement must stop, for in spite of these very sensible observations, the Commission spoils it all with the following:

> The cheap private rental market has many other unsatisfactory aspects such as insecurity of tenure, illegal retention of bond money, biased leases, and legislation which gives tenants few legal rights. Professor Sackville will be proposing legal changes which are needed to improve the situation.[12]

Here lies the germ of 'rental market regulation' in Australia. The legal reforms suggested in the report of the Poverty Commission involve setting up in each State a Residential Tenancies Board and a Tenancy Investigation Bureau. These bodies would be vested with the full complement of regulatory powers. The solution was simple. All that was needed was for each State to enact the necessary legislation, and who could resist this panacea?

The Poverty Commission's proposals attracted considerable support from some quarters. For example, the Australian Institute of Urban Studies published a Report of a

Task Force which asserted that 'landlord and tenant meet in an unequal contest'[13] and urged 'the Australian Government to take the initiative in getting adoption of the Bradbrook proposals on uniform Australia-wide fair rent legislation'.[14]

New South Wales and South Australia act early

In line with their past record of experiments with rent control legislation, New South Wales was the first State to act. Eviction provisions were tightened up considerably in 1977 such that a court order was necessary to effect an eviction whether a lease was current or not. Penalties for illegal evictions of up to $500 for an individual and $5,000 for a corporation were included. The New South Wales *Landlord and Tenant (Rental Bonds) Act*, 1977 set up a Rental Bonds Board to administer the security bond system, the effects of which are analysed by Alan Mitchell[15] in an article in the *Sydney Morning Herald*.

South Australia also acted early and its legislation, the *Residential Tenancies Act*, 1978 conforms quite closely to the Henderson model and carries over rent-setting powers from the former *Excessive Rents Act*. A Residential Tenancies Tribunal was established to adjudicate on disputes between landlord and tenants and to set rents - if desired by the tenant. The size of bonds was limited to a maximum of three weeks rent, bond money had to be deposited with the Tribunal, and eviction controls were tightened up.[16]

The A.C.T. and Victoria

The Australian Capital Territory has also been active in a regulatory direction. At the same time as the removal of compulsory rent control in Canberra, the Rent Control Ordinance was altered to include some of the Poverty Commission recommendations. Not content with a partial adoption, there has been lobbying from within the Department of the Capital Territory to go further and fully implement the Henderson proposals. These efforts have so far been resisted.

Not to be left behind, Victoria introduced its own *Residential Tenancies Bill*, 1978 which attempted to cover everything. The draft bill was immense, running to 98 pages and left no stone unturned in its attempt to enact the most comprehensive legislation possible. Every weapon in the rent regulator's arsenal was there. The likely effects of this legislation are analysed further by Ross Parish in this section.

A new and watered-down version of the Bill was introduced in 1979, but has not yet been enacted.

Disputation low

What is curious about the implementation of rental market regulation is that it has arisen in the context of very little disputation between landlords and tenants. On this matter the Henderson Committee's assessment that many of the problems that do exist are due to low incomes, is worth noting.

Problems that do occur in the rental market tend to manifest themselves in disputes over rents and security bonds. In Victoria, where a rent-setting facility has been available since the abolition of compulsory rent control, it has had a low degree of utilisation.[17] The same is true in the Australian Capital Territory where, even after attempts to 'drum up business', requests for rent determinations have been miniscule compared to the size of the rental market. A similar picture emerges if we look at disputes over bonds. In Victoria, a R.E.S.L. survey, reported in the Community Committee's study, reveals that 86 per cent of tenants received full repayment of their bonds. Some 96 per cent received at least 50 per cent of their bond. These figures reveal a very high reimbursement rate, especially when it is considered that very few tenants would deserve full reimbursement. It can scarcely be doubted that the effect of regulatory legislation will be to provoke friction between landlords and tenants rather than to reduce it.

NOTES

1. The interest income may be used to run the regulatory body (as in New South Wales) or may be returned, in part, to the rental market (as in South Australia where the landlords may be compensated for damage to their premises caused by tenants). The capital sum may be utilised in some fashion. In New South Wales, it is used to finance loans to low-income persons to enable them to purchase houses.
2. J. Patterson and K. Watson, *Rent Stabilisation: A Review of Currency Policies in Canada*, The Canadian Council on Social Development, July, 1976.

3. Michael Walker (ed.), *Rent Control: A Popular Paradox*, The Fraser Institute, Vancouver, 1975.
4. See *Time*, April 30, 1979, p. 69. An article on the same subject also appeared in the *Economist*, April 28, 1979, pp. 50,53.
5. R. Stephens, 'Towards a Housing Policy for New Zealand', *New Zealand Economic Papers*, 10, 1976, pp.30-56; and B.H. Easton, 'New Zealand Housing Market', *New Zealand Economic Papers*, 10, 1976. pp. 1-29.
6. Easton, *op cit.*, p. 20.
7. Stephens, *op cit.*, p. 51.
8. P.B.A. Sim, 'Rent Control Legislation in the Seventies' in G.W. Hinde (ed.), *Studies in the Law of Landlord and Tenant*, Butterworths of New Zealand, Wellington, 1975, p. 431.
9. A. Frame and P. Harris, 'Formal Rules and Informal Practices - A Study of the New Zealand Rent Appeal Boards', *New Zealand Universities' Law Review*, Vol. 7, No. 3, April 1977. pp. 213-236.
10. A.J. Bradbrook, *Poverty and the Residential Landlord-Tenant Relationship*, Commission of Inquiry into Poverty, Law and Poverty Series, Australian Government Publishing Service, Canberra, 1975 pp. 161-162.
11. *ibid.*, p. 162.
12. *ibid.*
13. Australian Institute of Urban Studies, *Housing for Australia: Philosophy and Policies*, The Report of a Task Force of the AIUS, AIUS Publication No. 58, Canberra, December 1975. p. 46.
14. *ibid.*, p. 70.
15. Alan Mitchell, '18 Months of Guarding Rent Bonds', *Sydney Morning Herald*, April 16, 1979.
16. A good summary of the provisions of the South Australian Act is contained in: S. Whitely, *Private Rented Housing in Australia*, Nuffield and Leverholme Travelling Fellowship 1978/79, April 1979. Ch.8.
17. A.J. Bradbrook, 'An Empirical Study of the Need for Reform of the Victorian Rent Control Legislation', *Monash University Law Review*, 2, 1975-76. pp.82-114.

Chapter 12

The Economic Effects of Victoria's Residential Tenancies Bill

Ross Parish

The Economic Effects of Victoria's Residential Tenancies Bill

Ross Parish

Author's Note

This article analyses the Victorian Residential Tenancies Bill of 1978. The Government sought and received many submissions from the public regarding this Bill. It was withdrawn and replaced by a new version in December, 1979, and further amendments have been foreshadowed. I have not altered (except trivially) my original text to take account of these changes. This is partly because the original Bill remains of interest (if only as an Awful Example), but mainly because I believe my analysis of such matters as rent regulation, the role of security deposits and minimum notice provisions, etc., remains valid, and is generally applicable to legislation of this type.

In the 1979 Bill many of the more egregiously objectionable features of the 1978 Bill have been removed. For example, the fair-renting procedures are to be made available only to tenants whose rents have been increased or from whom goods, services, or facilities have been withdrawn, and rent is to be deemed excessive only if significantly higher than for comparable premises; rent increases are to be permitted at six (rather than 12) month intervals, or on change of tenant; the minimum period of notice of eviction without cause is to be four, (not six) months; landlord's consent is to be required for assignment or sub-letting; the number of punishable offences has been reduced and so have some of the maximum fines.

I. INTRODUCTION

Consumer protectionists have recently turned their attention to residential tenants, and new landlord-tenant legislation has been enacted in several Australian states. Victoria was the latest to move in this direction, a Residential Tenancies Bill having been introduced in Parliament in December 1978, where it remained tabled while public reaction to it was sought.

Although the Attorney-General not surprisingly, described the Residential Tenancies Bill as being 'very even-handed', it was widely interpreted by the media as favouring tenants. Certainly the authors of the Report of the Community Committee on Tenancy Reform[1] (henceforth Report) had no doubts that existing law is 'plainly biased against tenants', and their recommendations (many of which were incorporated in the Bill - albeit in a watered down form in some instances) and their rhetoric embodied a view of landlords and tenants not far removed from Victorian melodrama. Furthermore, the Attorney-General has said that since present law has virtually no provisions establishing tenants' rights '. . . any balanced legislation is going to be seen to be talking more about tenants' rights than about landlords' rights'.

The principal 'tenant protection' features of the Bill were the following:

- provision for the 'fair-renting' of residential premises by Residential Tenancies Tribunals;
- limitation of the frequency of rent increases to once in twelve months;
- prescribed minimum periods of notice that would give the tenant - in the Attorney-General's words - 'greater security of tenure than any other legislation in Australia';
- provisions regarding assignment and sub-letting of premises which reduce substantially the landlord's control over the disposition of his property;
- limitation of the value of security deposits ('bonds') to one month's rent. (Bonds would also have to be held in approved interest-bearing trust accounts, with the interest being expropriated by the State.)

These provisions, while benefiting tenants, would clearly harm landlords. Indeed, in almost all cases the benefit to the tenant consists of the loss by the landlord of some of his

rights. While some other provisions of the Bill might benefit both landlords and tenants - the establishment of institutions (the Residential Tenancies Bureau and the Tribunals) intended to adjudicate tenancy disputes and act as small claims courts may be a case in point - the general thrust of the Bill was to alter the mix of legal rights and obligations so as to favour residential tenants and to disfavour landlords.

Demand and supply analysis

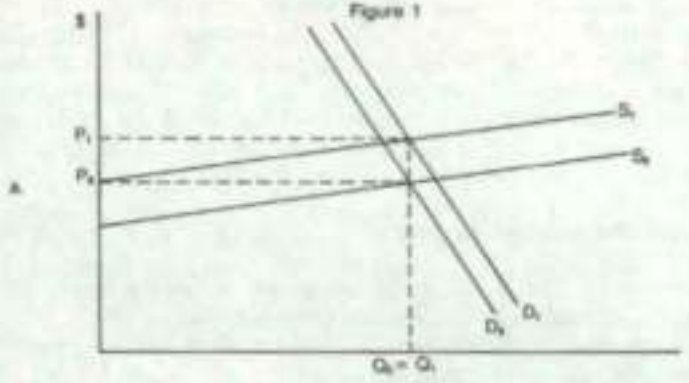
Enactment of the Bill would increase the costs and risks of being a landlord. It would also enhance the security and the rights generally of tenants. Unless they were prevented from doing so, rents could be expected to rise, at least in the long run, since both supply and demand forces would be operating in this direction. The rental accommodation supply curve, and its demand curve, would both shift upwards. The net effect of these changes on the equilibrium quantity of rental accommodation, and on the welfare of landlords and tenants, would depend on the relative size of the two shifts. There are three possible outcomes, depicted in Figure 1.

The first possible result, equal shifts in the two curves (Figure 1a) is the neutral case. This outcome requires that tenants' valuation of, and willingness to pay for their increased rights be equal to the additional costs borne by landlords. All of the additional costs would then be passed on to tenants in the higher rents, with no change in the quantity of accommodation rented. Landlords would on average be no worse off since they would be fully reimbursed for their higher costs; and tenants would be no better off, since they would be paying as much for their new rights as these rights were worth to them.

The second outcome (Figure 1b) would follow if tenants valued their new rights more highly than the cost of their provision. Rents, and the quantity of accommodation rented, would both rise, and both landlords and tenants would be better off.

The third possibility (Figure 1c) is the reverse of the second. Tenants are not willing to pay as much for their new rights as the provision of these rights cost landlords. Rents would rise, the quantity of accommodation rented would fall, and both landlords and tenants would be worse off.

Figure 1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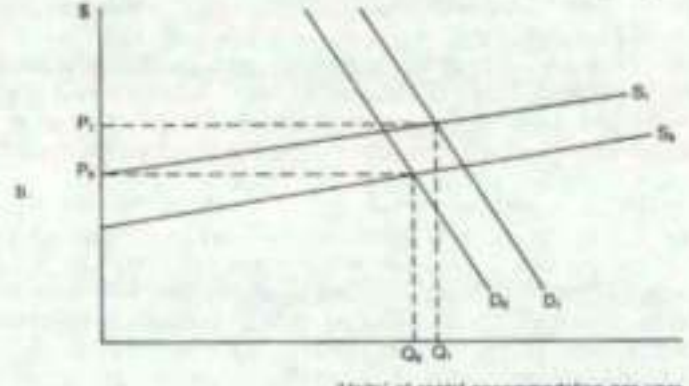
P_1
P_0
S_1
S_0
D_0
D_1
$Q_0 = Q_1$
'Units' of rental accommodation per year

A.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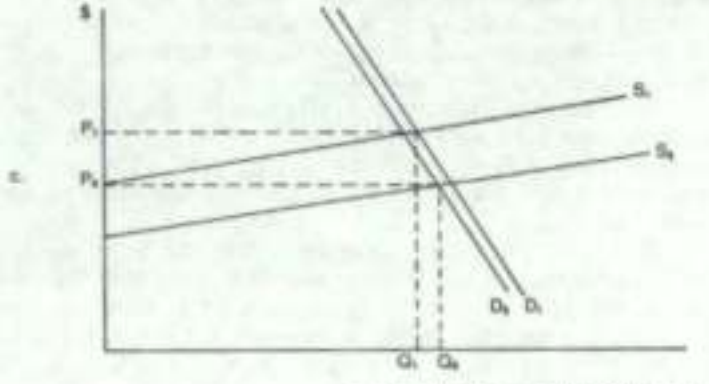
P_1
P_0
S_1
S_0
D_0
D_1
Q_0 Q_1
'Units' of rental accommodation per year

B.


$
P_1
P_0
S_1
S_0
D_0
D_1
Q_1 Q_0
'Units' of rental accommodation per year

C.

For the second outcome to obtain, it would have to be supposed that landlords and tenants are currently failing to exploit contractual opportunities that would be mutually beneficial. That is, a landlord who offered a tenancy contract that protected tenants' rights in the manner envisaged by the Bill would be able to charge a rent that more than compensated him for his increased risks and costs. Or a tenant proposing such a contract could reach agreement with a landlord on rent that was less than the value of the contract to the tenant. Now while it may be that market participants are so subservient to habit and tradition that they fail to recognise the opportunities for such gains from trade, this seems unlikely, more particularly as rental contracts have changed over time in response to economic forces. (For example, during the recent period of rapid inflation the term of fixed-term leases tended to be reduced from 12 to 6 months.) Furthermore, even if the invisible hand were to be somewhat palsied, there is little reason for thinking that the government fist would be more successful in guiding landlords and tenants to new, mutually-beneficial arrangements.

In my view the most likely outcome is the third: I doubt whether the increased costs and risks experienced by landlords would be matched by a similar or greater increase in tenants' willingness to pay.

Lack of tenant demand for change

There does not seem to be any widespread demand by tenants for the new rights offered them. Rather, the demand has come from the Community Committee, which cannot be said to have articulated the views of tenants, for among its 17 members, only two were representatives of tenants' associations - associations which themselves would speak for only a minority of tenants. The Committee, which contained no landlords' representatives, was dominated by social service organisations and radical groups.[2] Its Report was oriented almost exclusively toward the problem of poor tenants, and reflected the ideology of radical consumerism. Both the social service establishment and the radical consumerists believe that their clients (the poor and consumers in general) are incapable of looking after their own interests, and that improvements in their welfare require paternalistic interventions by the State. The Report - and, in large measure, the Bill - thus reflect the views of particular elites as to what tenants, especially poor tenants, **should** want, or

what **should** be done for them.

Landlord losses

If the costs and risks of being a landlord increased, potential landlords would require a higher gross return on their investments as compensation. If demand did not rise sufficiently to allow a compensatory increase in rents, the short-run adjustment would take the form of a fall in the value of existing properties, or a smaller increase in their value than if the legislation had not been enacted. Existing landlords would thus experience capital losses or lower capital gains than otherwise. In the long run, the adjustment would take the form of a reduction, or a smaller increase, in the supply of rental accommodation. This would be accomplished by conversion of rental premises to owner-occupancy, by earlier demolition of properties nearing the end of their economic lives, by some properties being left empty, and by a lower rate of construction of new buildings for rental. As the supply of rental accommodation fell, rents would tend to rise. Although the return to rental investments would be restored eventually, landlords would suffer reduced returns (and capital losses) in the adjustment period, and some would be driven from the market.

This analysis of the likely effects of the Bill is subject to one major reservation. I have assumed that the rent increases, stemming from landlords' higher costs and risks, would not be suppressed by the 'fair renting' procedures proposed in the Bill. In this respect the outcome I have sketched is the optimistic outcome: it assumes that rents would continue to be determined largely by market forces, with the Tribunals exercising their power to control rents with respect to only a small minority of cases where the existing or proposed rent was deemed to be excessive. However it is quite possible that the Tribunals would come to play a much more active role, and issue rent-fixing orders for many tenanted premises, so that something close to general rent control would come into effect. The consequences would then be much more adverse for landlords, for prospective tenants, and for the supply of rental accommodation and its efficient allocation, the only gainers being existing tenants.

Proponents of the Bill have represented its fair-renting provisions as being quite different from, and incapable of leading to the well-known adverse - and even perverse - consequences of traditional types of rent control. This issue is

clearly an important one, and will be discussed below. But before embarking on a detailed analysis of some of the Bill's provisions, two general types of defence of the proposed legislation against the sort of criticism I have made of it deserve to be mentioned, and disposed of.

Unconvincing arguments

One argument is that some proposed changes that favour tenants and ostensibly disfavour landlords in reality benefit the latter as well as the former. For example, reasonable security of tenure for tenants has been cited as something capable of benefiting both parties, since greater security for tenants encourages them to take better care of the premises. While such a tendency may operate, it does not follow that the **net** effects of greater security of tenure are beneficial to landlords, since it also involves costs for landlords. It seems unlikely that **compelling** landlords to give their tenants greater security of tenure would be beneficial to landlords. For it to be so, it would have to be supposed that landlords were ignorant of their own self-interest, for otherwise they would have offered the greater security voluntarily. The attribution to economic agents of irrational behaviour is rather presumptuous, and an unconvincing basis for argument or analysis.

The second argument for denying that the proposed legislation would result in a smaller stock of rental accommodation and higher rents runs as follows. Only 'bad' landlords have anything to fear from the Bill: 'good' or 'fair' landlords, who constitute the vast majority, would be unaffected. In the Community Committee's words:

> How will such (i.e. 'fair') landlords be affected by the present proposals? It is true that all landlords will have fewer 'rights' to act unfairly than before; but if they are fair landlords, none of the obligations in the new laws will require them to act differently or do more than they will now be prepared to concede is fair. Nor should the new laws affect profits because landlords of this kind will presumably not be charging excessive rents. On the whole it is true to say that fair landlords, like fair manufacturers, have nothing to fear from fair consumer laws.
>
> (Report, p.71.)

This argument is, of course, tautologically true if 'fair landlord' is defined as one who would be perfectly happy with the additional constraint imposed on him by the Bill. But if that is how it is to be taken, I doubt whether any but a tiny minority of landlords - or manufacturers - would qualify as 'fair'.

Furthermore, even if it were true that the Bill did not impose 'any more rigorous duties on a landlord than those that any reasonable landlord would already be undertaking' it is simplistic to argue that such landlords would not be adversely affected by the proposed changes. It is not just a question of good and bad landlords, but of good and bad tenants too. A fair landlord might, in the ordinary course of events, give his tenant more than the legal minimum period of notice, yet he might reasonably feel oppressed by a lengthening of that legal minimum, since resort to short notice is a quick way of cutting his costs if a tenant proves to be unsatisfactory. All landlords run the risk of having to deal with bad tenants, and insofar as the Bill strengthens the tenant's position it increases the landlord's costs.

II. RENT CONTROL

Tribunal investigations

The Bill provided for the investigation by the Director of Consumer Affairs (on application by a tenant or on his own initiative) as to whether a rent is excessive, and for the fixing of the rent by a Residential Tenancies Tribunal. On the face of it, this does not represent a major change from the current situation, whereby tenants can ask the Rental Investigation Bureau to consider whether their rent is excessive - a procedure which may result in the premises being declared a 'prescribed premises' and its rent determined by the Fair Rents Board. From the relatively small number of complaints received by the Rental Investigation Bureau (386, or about 0.15 per cent of the number of tenancies in 1977), and the relatively small proportion of those where the rent was considered excessive (about one-sixth), one receives the impression that the Bureau has had a minimal effect on the price of rental accommodation in Victoria. One might hope that under the new dispensation the Director of Consumer Affairs and the Tribunals would continue to show such commendable restraint, but there is no guarantee that they would. Indeed there is reason to believe that the new procedures might encourage many more tenants to try their

luck. This is because the procedures are simpler and seem to be slanted very much in favour of the tenant, tenants occupying rent-controlled premises would also enjoy greater security of tenure, introduction of the new arrangements would be attended by much publicity, and enactment of the Bill is likely to engender an adversary climate of opinion.

Provisions regarding 'excessive rents'

The Bill provided that any tenant who 'feels' that his rent is excessive may ask the Director of Consumer Affairs to investigate the rent. The investigation shall be made 'without unnecessary delay'. Furthermore, the Director may undertake an investigation on his own initiative, without a complaint having been made. If the Director believes the rent to be excessive, he shall try to get the landlord to reduce the rent. (The Bill does not specify what the Director should do if he believes the rent to be not excessive - perhaps it was not envisaged that this contingency would ever arise!) If the rent is not sufficiently reduced within a reasonable time, the tenant may apply to a Tribunal for an order declaring the rent to be excessive and fixing it at a lower level. Such an order will be made 'unless the landlord satisfies the Tribunal that the rent is not excessive' i.e. the onus of proof is placed on the landlord. However, the Bill in section 81(4) also allows the Tribunal to refuse to make an order where the landlord satisfies it that

(a) the rent has not been increased since the tenant went into occupation;
(b) the tenant knew at the time he went into occupation that the rent was excessive; and
(c) having regard to all the circumstances surrounding the making of the application (including the time which separated the making of the application and the tenant's going into occupation) the order ought in the interest of justice to be refused.

Presumably these clauses were a small concession to the view that tenants are responsible adults capable of entering into enforceable contracts and that their incentive to exercise ordinary prudence in entering into rental agreement should not be removed by giving them immediate access to fair-renting procedures. However it has been suggested by a legal analyst that 'it is difficult to know how in the normal course of events the landlord can ever make out ground (b),

having regard to the fact that the rent does not become excessive until after the Tribunal has made a determination to that effect and this usually occurs after the tenant has gone into possession. Therefore there will be few (if any) circumstances in which the tenant can be said to have known at the time he went into occupation that the rent was excessive'.[3]

It may be, then, that 81(4)(b) is a Catch-22 clause which would render unavailable to the landlord the defence that the tenant went into the agreement with his eyes open. Even if this pessimistic conclusion is unwarranted, the Bill provided only that a Tribunal 'may', not that it 'should', refuse to make an order for the reason stated. Subject to these substantial caveats, it is nevertheless possible that the Tribunals would adopt a policy of refusing to vary rents that tenants had agreed to pay when first occupying the premises, thus restricting their activities to cases where the landlord had sought to increase a sitting tenant's rent, and the tenant had disputed the fairness of the new rent. This might even have been the intention of the framers of the Bill. Such a policy would certainly make more sense than allowing tenants to enter into an agreement today and seek the Tribunal's intervention tomorrow.

In determining whether or not rent is excessive, a Tribunal is directed to take into account the rent payable for comparable premises in the locality, as well as any special characteristics of the premises or the tenancy agreement. A valuation of the premises may also be taken into account. Two other considerations are also mentioned: any rent increases since the tenant went into occupation, and, where the landlord is not permitted to require rent increases under a tenancy agreement, the period for which he will not be able to increase the rent.

The Attorney-General has said that 'in essence, rent is excessive if it is above the market rent'. The relevant sections of the Bill are consistent with this intention, except for (77(h)) which directs the Tribunals to take into account 'any rent increases since the tenant went into occupation of the premises'. This could be taken to mean, for example, that too rapid an increase in the rent should not be countenanced, irrespective of whether the level reached was above or below the 'market' level.

How might these procedures work in practice?

Every housing unit is unique in some respect, and one cannot

expect an outside arbitrator to be as sensitive to the particular features of a dwelling or to the nuances of neighbourhood as owners or occupiers. Hence, the determination of fair rents by reference to freely-negotiated market rents for comparable premises in the same locality is a rough-and-ready procedure. It is similar in principle to the valuation of properties by means of the 'comparable sales' approach. This works tolerably well, but it must be remembered that it is not normally used to determine a **transaction price.** Property valuations are usually carried out for rating purposes, or to provide a ball-park estimate of market value for buyers or sellers: actual transaction prices are ordinarily arrived at by market processes of making bids and offers at auctions and/or private negotiations. And if valuations get out of line with market prices, they tend subsequently to be corrected.

By contrast, fair renting does determine some transaction prices, viz those rents fixed by the Tribunals. Furthermore, it is bound to affect market rents as well, and since fair rents are based on market rents, induced changes in the latter will tend to be fed back to the former.

The notion that 'fair' rents can be determined by reference to 'the rent payable for comparable premises in the locality', without affecting the level of market rents, is false. To speak of 'the' market rent for a class of premises is misleading, for there is always a range of rents, and 'the' market rent must be conceived as some sort of average value. Rent fixing by the Tribunals will tend to remove the high observations from the observed range of market rents, and hence will tend to lower the average market rent. If we think of the observed average market rent as the 'ruler' used by the Tribunal in determining particular 'fair' rents, the length of the ruler will depend upon how frequently it is used: each time it is used, it will shrink a bit. It is not difficult to imagine an outcome in which the Tribunals, seeking conscientiously to fix rents in accordance with the 'comparable premises' criterion, came to exert continuous downward pressure on market rents.

Another way in which fair renting procedures could depress market rents is by the suppression of incipient market-induced upward movements in rents. For example, if some landlords in a locality, correctly noting an excess demand for accommodation, raised their rents, a Tribunal, using the comparable premises criterion, would be likely to deem the raised rents to be excessive, and to reduce them. In this way, rent increases fully justified by market criteria might nevertheless be inhibited, and, in the extreme case,

completely stifled. Since downward adjustments in rent would not be interfered with, the net effect would be to depress market rents.

Finally, landlords are likely to be inhibited from asking for high rents for fear of being taken to (and by?) a Tribunal.

The main point to emerge from this discussion is that it is false to believe that by fixing some rents at 'market' levels, interference with market forces and the general level of rents can be avoided. The interference might be trivial or it might be substantial, its magnitude depending on a number of factors, but particularly on (i) the proportion of tenants seeking rent reductions; (ii) whether and to what extent Tribunals exercised their discretion not to make orders where rental agreements had been freely entered into be tenants; (iii) rent levels set by the Tribunals; (iv) landlords' responses to the actvities of the Tribunals; and (v) the hypothetical rate of unconstrained increase in money rents.

Some proponents of the Bill clearly believe that the Tribunals' rent-fixing powers would be used only to lower a few egregiously high rents extracted by greedy landlords from ill-informed or otherwise exploitable tenants. The fact that rents, when controlled, would be fixed by reference to market rents for comparable premises is, on the face of it, reassuring, but this feature on closer analysis, is seen to be a most dubious safeguard.

Some critics of the Bill argue that if it were enacted, it would not be long before most residential tenancies in Victoria were subject to rent control. They point to the fact that any tenant who 'feels' his rent to be excessive may approach the Tribunal; that there is little deterrent to his doing so since the Tribunal cannot award costs against unjustified applications by tenants; that the onus of proving the rent to be not excessive is put on the landlord; and, most importantly, that by seeking and obtaining a rent order from a Tribunal a tenant can obtain greater security of tenure. This last effect arises from a provision of the Bill which denies the landlord the right to terminate an agreement without giving a specified reason when the premises are the subject of an investigation by the Director or a Tribunal, or of a rent-fixing order by a Tribunal. This means that tenants of such premises can only be given notice to vacate on grounds prescribed in the Bill, whereas tenants of uncontrolled premises may be given six months' notice without the landlord being required to give any reason. In short, the costs to the tenant of approaching a Tribunal are negligible, and the possible gains substantial.

Either of these outcomes is possible, as is any intermediate case. And that, of course, is one of the principal problems with legislation of this type. The Bill contains the threat of rent control, but whether the control that would emerge would be relatively benign or relatively severe is uncertain. Even if it were benign, it need not stay so and so the threat of severe control would remain, with consequential adverse effects on the confidence of investors in residential real estate.

Professor Henderson has argued that opponents of rent control should welcome the Bill, since 'so long as abuses continue unchecked under the current archaic legislation, there will continue to be agitation for general rent control. The way to avoid rent control is to have improved legislation fair to both parties'.[4] Even if we assume, along with Professor Henderson, that the rent regulation proposed in the Bill would not have the nasty effects of general rent control, his argument is unconvincing. The many tenant protection features of the Bill would cause rents to rise. Surely a **milieu** of accommodation shortages, rising rents, and of agitators urging tenants to assert their new rights would be more conducive to demands for general rent control than is the present situation. The demand might be met, spontaneously as it were, by the activities of the Tribunals (who might be expected to be influenced by the general climate of opinion), without further legislation being required. Or, it would be a simple matter to amend the legislation to give more bite to the rent regulation powers. For example, a simple amendment requiring the Tribunals to set 'fair' rents by reference to the rent payable for comparable premises **but without regard to a scarcity premium** would do the trick - and would, moreover, be following a precedent: in the 1974 Rent Act of the United Kingdom, fair rent is defined as a rent established in a free market **without** a scarcity premium.[5]

Following a Canadian model

One of the models for the proposed Victorian legislation is that enacted in Ontario in 1970. The Ontario reforms were singled out for high praise in the Community Committee's Report, and have subsequently been referred to with approval by Professor Henderson, who also has asserted that they did not have the effect of leading to withdrawal of funds from the rental market. The facts of the matter appear to be as follows. First, the Ontario 'reforms' of 1970 were followed

in 1975 by legislation (Residential Premises Rent Review Act) limiting rent increases generally to 8 per cent per annum. Professor Henderson's theory that 'having improved legislation fair to both parties' is the way to avoid general rent control was certainly not confirmed by events in Ontario.

Second, there has been a decline in investment for rental purposes in Ontario in recent years. However, in the opinion of the Ontario Minister for Housing, this 'can largely be attributed to high interest rates, escalating costs, and more recently, to the introduction of rent control'. It is his judgement 'that the modifications to the Landlord and Tenant Act, per se have not been an important consideration in the building decline'. It is evidently this statement, made in a letter to the former South Australian Attorney-General, and quoted in the Community Committee's Report (p.74), on which Professor Henderson relies for his assertion (as reported in the *Financial Review*, March, 23 1979) that similar legislation in Ontario, Canada, did not have the effect of leading to a withdrawal of funds from the rental market.

III. ASPECTS OF THE BILL

Limitation of rent increases

As well as seeking to reduce 'excessive' rents by direct controls (and by the threat of their being invoked) the Bill sought to moderate rent rises generally, by obliging landlords to give 60 days written notice of a rent increase, and by limiting the frequency of rent increases to no more than once in twelve months. The latter restriction applies, irrespective of any changes in the identity of the tenant.

My impression is that landlords are reluctant to increase the rents of existing tenants frequently: they prefer to keep rents stable for a reasonable period. To the extent that this is the case, restricting the frequency with which rents may be increased could be of little consequence. However, it is also my impression that landlords frequently do take the opportunity of a change of tenant to raise the rent. (I am referring to a situation of inflation and no great disequilibrium in the rental housing market, or of a tightening rental market, so that a steady rise in money rents would be expected). I suspect that the reasons for this practice are partly psychological, and partly practical. A new tenant will have been searching the market and hence be in a better position to assess the reasonableness of the rent being asked than a sitting tenant. He is thus more likely to accept a rent

in line with current market conditions than is a sitting tenant, who might be quite out of touch with the market. Timing rent increases, as far as possible, with changes in tenants may thus simply be a means of reducing friction between landlords and tenants. Under the Bill, the landlord's flexibility in this matter could be much reduced (particularly in times of a high rate of inflation or a booming rental market), and more disputes engendered.

A practical reason why rent increases tend to coincide with changes in tenants is that landlords frequently make improvements to premises while they are vacant. This clearly involves less inconvenience to tenants than if the improvements were made while the premises were occupied.

Limitation of rent increases to once a year would not necessarily hold rents down. If market rents were expected to rise over the year, this expectation would tend to be embodied in the rent bargain concluded between landlord and tenant, so that it would approximate the anticipated average market rent for the period.[6] Two other considerations tend to work in opposite directions. Since there is no limitation on the frequency of rent reductions, these might be forced on landlords by unfavourable market changes at any time. The situation is thus asymmetrical with respect to rises and falls in rent, and hence the net effect of the limitation might be for rents to be lower, on average. But, on the other hand, landlords might seek a risk premium, in the form of a higher average level of rent, to compensate for the chance of their being adversely affected by unanticipated market developments.

The purpose of limiting the frequency, and requiring long notice of rent increases can only be to hold down market rents. Many other provisions of the Bill have the same intent. To the extent that these intentions were realised, tenants would be better off and landlords worse off. However, tenants would also incur some offsetting costs. For one thing, landlords are usually willing to trade off some rent for securing a good tenant, i.e. someone who seems likely to pay the rent regularly and not destroy the property. The existence of various pressures, including a latent threat of rent control, might encourage landlords to moderate their rents but also to be more selective in their choice of tenants. Discrimination against those who do not seem to be good tenants is thus likely to be more severe. Second, with rents below market-clearing levels, occupancy rates are likely to be high, and a tenant's ability to change his place of residence easily, to be reduced.

Notice

The purpose of giving notice of your intention of withdrawing from a contractual agreement of indefinite length is to reduce the costs and inconvenience to the other party of your withdrawal. From the point of view of the receiver of notice, the longer - and from that of the giver of notice, the shorter - the minimum required period of notice, the better.

At present tenancy agreements normally treat both parties symmetrically with respect to minimum notice. In a month-to-month agreement, a month's notice by either party is usually required. The Bill would change this, as it would require landlords in most circumstances to give tenants longer notice than tenants are obliged to give landlords. A summary of its provisions is given in the table on the following page.

The Bill provided that a tenant may terminate a tenancy without giving a reason on 14 days' notice, but a landlord must give 6 months' notice. In the case of fixed-term tenancies, the vacation date cannot be sooner than the day on which the agreement ends. Landlords are entitled to give shorter notice (zero to 14 days) if tenants are in breach of the agreement, or 60 days' notice if vacant possession of the property is required for certain specified purposes. Tenants on fixed-term tenancies may give 14 days' notice if the landlord is in breach of the agreement. A minor point is that a fixed-term agreement can be truncated by the tenant receiving 60 days' notice if the property is acquired by a public authority, but not otherwise. If breaches of duty by tenant or landlord, or non-payment of rent by tenants, are remedied before the notice expires, the notice can be disregarded (except in cases where breaches have been committed previously).

The Bill did not give the landlord vacant possession before a sale, but gave the purchaser given vacant possession (on 60 days' notice to the tenant) after a sale. This failure has been criticised by the Real Estate and Stock Institute of Victoria, on the grounds that '. . . the desire to sell a property is probably the most common reason for a landlord wishing to obtain vacant possession, and a sale may be prejudiced by difficulties of inspection and by buyer resistance. In addition renovation before sale is an important factor in determining the owner's desired time of possession.'[7]

Either party to a fixed-term agreement can give notice terminating it before it has run its full course if the other party is in breach of the agreement. In addition, a tenant

may apply to a Tribunal for release from the agreement on the grounds that either a change in his place of work or in his financial position make it necessary or desirable that he live in other accommodation.

Type of notice	Minimum notice required to be given by: Landlord	Tenant
Notice without specified grounds	6 months*	14 days*
Notice on specified grounds		
- endangering safety of neighbours or malicious damage to property	Immediate	n.a.
- 14 days or more arrears of rent	14 days	n.a.
- other breach of duty by tenant	14 days	n.a.
- breach of duty by landlord	n.a.	14 days#
- compulsory acquisition by public authority	60 days	n.a.
- demolition	60 days*	n.a.
- substantial repair or renovation**	60 days*	n.a.
- use of premises for business other than letting as a residence	60 days*	n.a.
- occupation by landlord or his immediate family	60 days*	n.a.
- to give vacant possession to a purchaser	60 days*	n.a.
- to resume occupancy of landlord's principal place of residence at end of fixed term agreement	14 days*	n.a.

* But not sooner than the expiry date of a fixed-term agreement

\# Fixed-term tenancy only

** 'Substantial' means (a) the need for a written permit from the relevant authority, (b) need for premises to be vacant for more than 30 days, and (c) expenditure of not less than 20 per cent of market value of premises.

The Tribunal may permit the landlord to recover from the tenant reasonable costs incurred as a result of the tenant's early departure. If a landlord gives notice that specifies a vacation date later than the end of a fixed-term agreement,

the tenant is entitled to remain in occupancy until the later date. If a tenant gives his 14 days' notice less than 14 days before the end of a fixed-term agreement, he does not have to leave until the date specified in his notice. It is evidently intended that tenants should benefit both from landlords' and their own mistakes.

I have already mentioned that if the rent were being investigated by the Director or a Tribunal, or the premises were subject to a rent-fixing order, the landlord could not give six months' notice without cause, but could only give notice for reasons of breach of contract or his need for vacant possession of the premises. The effect is that if the landlord found the tenant unsatisfactory but could not convince a Tribunal that the tenant was in breach of the contract, he would be stuck with him, if not indefinitely, then at least for a very long time. If the tenant secured a rent-fixing order, he would have effective security of tenure for the 12 months of its duration, and unless the landlord was willing not to increase the rent at the expiration of the order - which might involve considerable sacrifice in inflationary times - the tenant might be able subsequently to secure another order. It may well be true that if the Bill was enacted it would be easier in Victoria to divorce your spouse than to get rid of your tenant!

Rationale and likely consequences of minimum notice provisions

Being asked to leave your house and find another is more traumatic than losing your tenant and having to find another. The greater trauma may be assuaged by ensuring that tenants are given relatively long notice, while the lesser trauma does not justify equally long notice being given to landlords. That, presumably, is the rationale behind the Bills' minimum notice provisions. The argument has some appeal, but is simplistic.

First, it ignores the relative frequency with which the parties are traumatised (more soberly, subjected to cost and inconvenience) by receiving notice. My guess is that landlords are given notice far more frequently than they give it. If this is so, the aggregate cost and inconvenience suffered by landlords from receiving short notice from tenants may well exceed that suffered by tenants from receiving short notice from landlords.

Second, it ignores the cost imposed on the landlord by requiring that he give the tenant long notice. A landlord

ordinarily gives notice only when he finds the existing tenant unsatisfactory or when he wishes to repossess the premises for his own use. In either case the cost and inconvenience of not being able to proceed quickly may be substantial, and fully comparable with the costs borne by the tenant if the landlord were able to proceed quickly.

These considerations show that it is not obvious that extending the notice that landlords are obliged to give tenants, and reducing that that tenants have to give landlords,[8] would produce net benefits to tenants and landlords taken together.[9] Tenants would benefit, in the first instance, but landlords would be disadvantaged. In the long run, the increased costs imposed on landlords would be passed on to tenants in the form of higher rents.

Assignment and sub-letting

Under existing law, leases may and commonly do contain a covenant whereby the tenant is prohibited from assigning or sub-letting all or part of the premises without the landlord's consent. The law also provides that 'such covenant, condition, or agreement shall, unless the lease contains an express provision to the contrary, be deemed to be subject to a proviso to the effect that such consent shall not be unreasonably withheld, and that no fine or sum of money in the nature of a fine shall be payable for or in respect of such licence or consent'. Many standard-form leases do, in fact, contain an 'express provision to the contrary', indicating a desire by landlords to retain absolute discretion as to who shall occupy their premises.

According to the Bill, tenants shall not assign or sub-let without first getting the landlord's consent, and specifies a penalty of $500 for doing so without permission. However - and also under pain of penalty of $500 - a landlord shall not unreasonably withhold his consent. The landlord may not make a charge for giving his consent, and to withhold consent because the tenant refuses to pay a charge is deemed to be unreasonable withholding of consent. (Standard-form leases often provide that the tenant shall pay all costs and expenses reasonably incurred by the landlord or his agent in connection with the application for such consent.) Where a landlord withholds his consent he shall be presumed to have unreasonably withheld it unless he proves otherwise; and in proceedings where a person alleges that as assignment or sub-letting was without the landlord's consent, the onus of proving that allegation shall lie upon him. A Tribunal, on a tenant's

application, can make an order authorising an assignment or sub-letting without the landlord's consent, provided the Tribunal is satisfied that the landlord has withheld his consent, and the landlord has not satisfied the Tribunal that the withholding of consent was reasonable.

These provisions of the Bill imply a substantial loss of control by the landlord over the disposition of his property. A tenant could, in effect, choose his successor, unless the landlord was able to convince the Tribunal that his grounds for not wishing to let his premises to a person chosen by the tenant were reasonable.

Security deposits

The Bill would limit the value of security deposits to a maximum of one month's rent, require them to be held in interest-bearing trust accounts at approved institutions, expropriate for the purposes of the State the interest so earned, and require the landlord to make any claim against the deposit, or refund it, within seven days of the tenant vacating the premises.

In his second-reading speech, the Attorney-General referred to the question of security deposits as 'one of the most contentious matters in the landlord/tenant relationship'. The Community Committee in its Report (pp.46–7) roundly condemned security deposits, claiming that they 'are widely and rightly regarded as a major area of exploitation and discontent in landlord-tenant relations'; also, that 'although the bond system has advantages for landlords, it is a burden upon tenants and seriously conflicts with the objectives of a reasonable social housing policy'. The Committee also stated (misleadingly, in my opinion) that 'it is probably true that the modern bond system in Victoria is a descendant of the illegal "key money" payments which were commonly demanded in the post-war era'.

The characterisation of the security deposit system as a 'major area of exploitation and discontent' does not jibe very well with data (derived from a survey conducted by the Real Estate and Stock Institute of Victoria)[8] which indicate that 86 per cent of deposits are returned in full, and that no more than 6 per cent of tenants lose half or more of their deposit. Admittedly, these data do not throw any light on how much hassle might be involved in getting one's deposit refunded, nor do they apply to non-R.E.S.I. lettings, but they do not support the contention that deposits are a form of rental premium.

The Community Committee's antipathy to bonds, and the Government's proposal to limit their value and tax them, seem to me to be wrongheaded, and based on an incomplete and misleading analysis of their role. To say that bonds are 'a very significant cause of disputes and bad feeling between landlords and tenants', is, at least in part, to confuse cause with effect. Disputes and bad feeling are bound to arise in landlord-tenant relations for all sorts of reasons, including differing conceptions of what constitutes 'fair wear and tear', damage, cleanliness, proper maintenance, etc. With a bond system these disputes, or a large subset of them, are focussed on the bond. But getting rid of bonds would not usher in an era of sweetness and light in landlord-tenant relations: disputes would still arise, but would centre on some other instrument or institution or remain unresolved and contribute to a higher cost structure in the industry.

To say that the bond system 'penalises the great majority of good tenants who cause no damage and pay their rent in full'[11] is the exact opposite of the truth. The system penalises 'bad' (or potentially 'bad') tenants, either by constraining their impulses to damage or neglect the leased property or not to pay the rent, or by exacting a money penalty if they do give in to these impulses. Under the insurance scheme proposed by the Community Committee the costs of bad tenants' behaviour (property damage, rent defaults) would be borne by all tenants equally and by taxpayers generally.[12] Private, unsubsidised insurance schemes would spread the costs across all tenants, although some rough-and-ready apportionment of the costs in accordance with liability could be achieved by such devices as no-claim bonuses, and age-related premiums, already commonly used in motor vehicle insurance. Insurance schemes are therefore less equitable than the bond system. But that is not the only objection to them. The less that the costs of bad behaviour by some tenants are borne by those tenants, the less the incentive for tenants generally to behave responsibly. Hence if the bond system is abolished or substantially eroded, it is to be expected that property damage, cleaning costs, and rent defaults would increase and that these costs would be borne by tenants generally.

The Bill envisaged a mixed scheme, allowing tenants the choice between a security deposit of limited size, and insurance. It seems likely that bad tenants would tend to opt for the insurance scheme as being the least costly alternative - at least initially. Insurance premiums could then be expected to rise, and insurers to attempt to vary premiums in

accordance with their assessment of relative risk.

The deterrent effects of the bond system, as it currently operates, has been questioned on the grounds that the bond 'could not possibly cover serious damage' and that 'it is relatively easy for tenants to frustrate the purpose of bonds by not paying their last few weeks' rent'.[13] These criticisms are valid, but do not establish the fact that bonds have **no** deterrent effect, but simply show that the protection they afford the landlord is incomplete and imperfect. And the inference to be drawn is not, I would have thought, that the system should be abolished or that the value of bonds should be limited, but rather the reverse - that larger bonds may be needed.[14]

It should also be noted that if the bond system is rendered less effective, or replaced by some alternative that landlords find less satisfactory, landlords are likely to become more discriminating in their choice of tenants, for example by requiring good references or simply by making subjective assessments of the tenant's character and likely behaviour. In such circumstances it is minority and deviant groups that tend to lose out. Hence far from it being (as is claimed) a means of discrimination in the housing market, the bond system tends to reduce it. This is a particular illustration of the general proposition that a market system is destructive of privilege and standing, and a good friend of members of unpopular groups, whose dollar is as good as the next man's.

It has been argued that bonds may be justified 'because of the inadequacies of legal remedies available to the landlord'. It is probably not so much the inadequacy as the high cost of legal remedies that is the problem: protection is available but at a cost that is higher than it is typically worth. The establishment under the proposed legislation of the Residential Tenancies Bureau and the Tribunals, which are intended to provide a low-cost means of arbitrating and resolving disputes, would presumably help redress this problem, and it might be that the operations of these new institutions would make the bond system redundant. This, however, cannot be determined in advance. If the Bureau and the Tribunals did provide 'cheap justice' that was generally thought to be fair by landlords and tenants, then they might find it mutually advantageous to remove security deposits from rental contracts, and the bond system might wither on the vine. Or, again, it might not: the new institutions might not live up to expectations, or even if they did, a place might remain for security deposits, since dealing with these institutions would still entail some costs and risks.

An objection to security deposits raised by the Community Committee is that 'it is unfair that landlords should have a legal self-help remedy when no similar remedy is provided for the tenant to ensure that the landlord performs his part of the agreement'.[18] This argument might have some appeal, particularly if one espoused the 'levelling' philosophy inherent in it. But as is so often the case with legalistic arguments, it neglects to consider the consequences of the situation in a market context. If tenants run the risk of having their bond withheld unjustifiably, the demand for rental accommodation will be less than if their rights were better protected. (Fewer people will become tenants, and the amount they are willing to pay in rent will be less). On this account rents will tend to be lower. And if security deposits allow landlords to protect themselves, to some degree, against irresponsible tenants, the supply of rental accommodation will tend to be greater than if they had less protection, and on this account rents will also tend to be lower. Hence the market will take account of the lop-sided nature of the contract and will tend to redress the balance of the whole situation, via the determination of the price. If the balance of rights is changed by legal 'reform' compensating changes in price can be expected to occur.

IV. OTHER PROVISIONS OF THE BILL

Space does not permit a full description - let alone analysis - of the Bill, which runs to almost 100 pages. Some of its features, other than those analysed above, are listed below.

Repair of premises

The landlord would be required to keep 'the rented premises in a reasonable state of repair'. Failure to do so could result in a Tribunal ordering a reduction in the rent or a refund of rent already paid; the landlord to carry out the repairs within a stated time; and/or the rent to be paid into the Residential Tenancies Fund until the repairs are completed.

A tenant would be permitted to make urgently required repairs and recover their cost from the landlord, provided the costs are reasonable and do not exceed two months' rent.

Discrimination against tenants with children

The Bill would outlaw discrimination against tenants with

children. However, on application by an owner, a Tribunal may declare premises to be unsuitable or not designed for occupation by a child.

Time limits

A landlord who required a security deposit would be obliged to provide the tenant with a condition report on the leased premises 'on the day on which the agreement begins'; if the tenant amended the report and returned it to the landlord within 14 days, the latter would be deemed to have accepted the accuracy of the amended report unless, within 7 days of having received it, he applied to the Director of Consumer Affairs to investigate the matter.

Where a written tenancy agreement was involved, the landlord would be required to provide the tenant with a copy of the agreement within 14 days of it having been signed.

The landlord would be obliged to refund the security deposit within seven days of the tenant having vacated the premises, unless the tenant had agreed to the landlord retaining some of it, or the landlord had claimed some of it in proceedings before a Tribunal.

These time limits have been criticised by the Real Estate and Stock Institute of Victoria as being impracticably short. One wonders whether the bureaucratic bodies charged with administering the Act would be able to perform their duties with comparable alacrity.

Penalties

The Bill provides that a wide range of acts or omissions by landlords and tenants may be punished by fines. Many more of the punishable offences are applicable to landlords than to tenants. Some examples follow, the figure quoted being the maximum fine:

- discrimination against tenants with children, $1,000;
- failing to ensure the tenant has quite enjoyment of the premises without interruption by the landlord, $1,000;
- requiring tenant to redecorate, repair, improve, or alter premises as a condition for continuing or renewing an agreement, $500;
- making a false statement in a notice of entry, or a false or misleading statement in a notice to vacate, $500;
- entering premises otherwise than in accordance with the Act, $500;

- failure to give tenant a copy of written agreement within 14 days of signing, $200;
- failure to give tenant notice of landlord's change of address, $200.

V. PHILOSOPHY OF THE BILL

Landlord-tenant relationship

Under existing law and practice, the landlord-tenant relationship is an agreement, a **voluntary** association between two parties in which a flow of housing services is exchanged for a flow of money. The law places certain constraints on what the parties may agree to, and on what either of them may do by way of enforcing the agreement. But within these constraints, the parties are free to contract as they please.

The Bill would greatly narrow the area of discretion in tenancy agreements. While not going so far as to prescribe a standard contract, it would nevertheless impose a high degree of standardisation. The freedom of the parties to negotiate mutually-agreeable terms, trading off one contract dimension for another, would be much circumscribed.

For landlords - but not for tenants, who would generally be better off in this respect - a second and more serious loss of freedom is the increased likelihood that they would have to participate in involuntary relationships with the other party. At present, the maximum period that a party might have to participate involuntarily in an agreement is determined at the outset by the terms of the contract specifying the duration of any fixed-term lease and the minimum notice requirement. (At least this is true for the tenant: a landlord may be forced by a recalcitrant tenant to remain in an involuntary relationship for the additional period required to secure an eviction order). The Bill, by requiring of landlords much longer periods of notice than is customary, by its provisions regarding sub-letting and assignment, and by its fair-renting procedures and associated eviction control, would increase the frequency and duration of periods in which the landlord would prefer, but be unable, to terminate the agreement.

The traditional view of the landlord-tenant relationship is that it is an association voluntarily undertaken on mutually-agreeable terms and voluntarily maintained so long as it is desired by both parties. The contrasting view, espoused by the Community Committee, is of an association which, while it might (but need not necessarily) be initiated

voluntarily, is subject to detailed social control and from which the landlord cannot withdraw except on specified grounds and with the permission of a legal or regulatory agency. Such a relationship requires that rent and other contractual terms be determined, and disputes resolved, by a third party, since, if the landlord cannot withdraw his asset, he has no bargaining power whatsoever. We know from experience in Australia and elsewhere that the voting power of tenants ensures that a regime of rent and eviction control is used to expropriate much of the landlord's interest in his property, and leads to a cessation of investment in rental housing, and to disinvestment when the opportunity arises.

The Bill embraces the second philosophy in large measure, but not totally: the right of the landlord to give six months' notice without cause is a concession to the first. The Bill is an uncomfortable three-quarter-way house on the the road to an over-regulated, politically-exploited and moribund private rental housing industry.

VI. SUMMARY

The proposed legislation would increase the costs and risks of being a landlord, in the following ways:

- Loss of interest on security deposits
- Limitation on the amount of security the landlord may require of the tenant by way of deposit or insurance
- Increased obligations regarding record-keeping and managerial input generally
- Increased obligation to keep premises in good repair
- Risk of having to pay a fine and compensation to a tenant
- Optimal timing of repairs, renovations, etc., hampered by limitations on frequency of rent increases
- Greater probability of disputes with tenants having an outcome that is unsatisfactory from the landlord's point of view. This arises from limitations on the landlord's right to terminate tenancy agreements quickly, and from the arbitration of disputes by a Tribunal
- Longer periods of involuntary association with a tenant
- Likelihood of more disputes with tenants: timing of rent increases will tend to increase friction between the parties; and general 'consciousness-raising' among tenants will cause them to be more assertive
- Reduced control over choice of tenants because

of prohibition of discrimination against tenants with children and provisions regarding sub-letting and assignment.

An increase in costs and risks would be expected to cause rents to rise, particularly in the long run. However a number of the proposed changes would be likely to induce landlords to keep rents below market-clearing levels. These are the fear of being 'fair rented' by a Tribunal, on complaint by a tenant; limitation of the frequency, and the long notice required, of rent increases; and deterioration of the landlord's bargaining position vis-a-vis sitting tenants. (This arises mainly from the latter's greater security of tenure). These pressures are of course additional to any direct rent-fixing by Tribunals.

If landlords were forced or induced to charge lower rents than the market would bear, they would naturally seek to reduce their risks by being more selective in their choice of tenants. In any case, the whole thrust of the legislation would push them in this direction, since enhancement of tenants' rights makes the unsatisfactory or vexatious tenant more difficult to deal with. Hence the new legislation would increase landlords' discrimination against 'risky' tenants. In an unconstrained market environment, members of groups that are discriminated against can compensate for their unpopularity or their perceived riskiness by paying a higher rent, and hence can usually secure accommodation. But this opportunity would be closed to them under effective rent regulation of the type proposed in the Bill, since any premium designed to compensate the landlord for additional perceived risks associated with a particular type of tenant would make the rent excessive in the eyes of the the regulators. As a result more high-risk tenants would be pushed out of the private market and become dependent on public housing, and members of ethnic minorities would become more dependent upon accommodation provided by members of their own communities.

If the legislation were enacted, tenants could expect to experience some combination of higher rent, shortages of accommodation, and more severe discrimination against high-risk tenants. The more rent increases were suppressed by rent regulation, the more serious would shortages and discrimination become. Sitting tenants with no desire or need to move house would probably benefit from severe rent control. Prospective new tenants, mobile people, and high-risk tenants would be worse off. These effects on tenants would be more serious in the long run than in the short run.

It is very doubtful whether tenants and displaced tenants would find their new rights sufficient compensation for these costs.

Initially, landlords would probably experience reduced rates of return and hence capital losses (or reduced capital gains). In the long run, rates of return might be restored by shrinkage of the rental sector, but adjustment along these lines could be hampered greatly if rent and eviction control were widespread. Landlords would be expected to become, on average, 'tougher' and more inclined to resort to extra-and quasi-legal means of dealing with tenants.

In short, the Bill is likely to have perverse effects, benefiting neither tenants (on average) nor landlords. The costs of administration, borne by taxpayers (including those who bear the 100 per cent tax on security deposit interest) would not be negligible. The only obvious beneficiaries would be the bureaucrats.

NOTES

1. Victorian Council of Social Services, *Reforming Victoria's Tenancy Laws*, Melbourne, 1978.
2. The following organisations were represented on the Community committee: Victorian Council of Social Services; Real Estate and Stock Institute of Victoria; Institute of Applied Economic and Social Research, Melbourne University; Women's Liberation Halfway House Collective; Royal Australian Planning Institute; The Salvation Army; Tenants Union of St. Kilda; Law Institute of Victoria; Australian Union of Students; Tenants Union of Victoria and Housing Commission Tenants Union; Youth Council of Victoria; Council for the Single Mother and Her Child; Action and Resource Centre. Four members were described as elected community representatives.
3. Draft Submission by the Property Owners Association of Victoria in the matter of the Residential Tenancies Bill. (mimeo)
4. Ronald F. Henderson, *Victorian Tenancy Law Reform*, Submission to Attorney-General of Victoria, 21.12.78.
5. Duncan Maclennan, 'The 1974 Rent Act - Some Short Run Supply Effects', *Economic Journal*, 88 (June 1978).
6. This is implicity recognised in the Bill, where one of the factors to be taken into account in determining

whether rent is excessive is as follows: 'Where the landlord is not permitted to require rent increases under a tenancy agreement, the period for which he will not be able to increase the rent'. (Clause 77 (i)).

7. Real Estate and Stock Institute of Victoria, Submission on Residential Tenancies Bill, 1978, p. 62.
8. The terms of their existing agreements oblige many tenants to give a month's notice, not the 14 days prescribed by the Bill.
9. It would be surprising if the benefits of such a change were obvious, for then one would wonder why such arrangements had not risen spontaneously. There is nothing to stop parties to tenancy agreements agreeing to asymmetrical clauses regarding length of notice, but so far as I am aware, they almost invariably do not.
10. And published in the *Real Estate and Stock Journal*, April 1975. The data are also cited in Community Committee's Report, p. 50.
11. Community Committee's Report, p. 47.
12. The Committee recommended that 'a government guaranteed system of insurance of rented premises, operated by the State Insurance Office, should replace the present bond system'; and that 'the maximum premium cost payable by tenants should be $5. Any higher cost, and any operating losses, should be subsidised by the Government, if necessary from Commonwealth-State housing funds, as a legitimate government housing expenditure in an area of need'. Recommendations 61 and 62 (Community Committee's Report, p. 79).
13. Community Committee's Report, p. 47.
14. A friend who recently had occasion to house his family in Geneva for a short period found that in that city the common practice was for a tenant to post bond equal to three months' rent (a very substantial, sum since the rent for a small, modern two-bedroom flat was about A$700 per month); the bond was placed in a trust account and interest paid to the tenant; meticulous inspections were carried out on the tenants entering and vacating the premises, and a standard - in his view, rather steep - scale of charges levied for the various categories of damage detected.
15. Community Committee's Report.

Conclusion

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Very strong case against controls

The case against rent control is very strong. The major objective of rent control must be the bestowal of benefits on tenants - in other words, a redistribution of income towards the occupiers of privately-rented housing. Most would see that redistribution as being of the 'Robin Hood' type, going from rich to poor. However, there are many problems with this form of redistribution. The burden of the transfer falls on one group - landlords. The well-meaning and paternalistic middle-classes can salve their consciences at the expense of rental property owners. Furthermore, landlords are not all rich nor are all tenants poor so that the redistribution can go the 'wrong way'.

Rent control creates many costs in the quest to effect a capricious transfer to some people. Not the least of these is the adverse effect on the supply of rental housing. This harms mainly people seeking to become tenants - a politically weak and diffuse group, whose plight it is all to easy to overlook. The lucky sitting tenants get all the benefits, but their subjective valuation of the benefits is less than the difference between market and controlled rents: hence landlords' losses will generally exceed tenants' benefits. The other costs of rental control include the inefficiencies associated with labour immobility and the costs of administration. All in all, it is difficult not to concur with Webster's conclusion that rent control as a redistributor of wealth, is the 'most inefficient, costly and callous method ever devised'.

Some might argue that, while 'rent control' is not a 'good thing', 'rental market regulation' is necessary to protect the rights of tenants. The arguments in this volume tend to disfavour regulatory intervention, largely because it does not seem to be in the interests of most tenants.

These conclusions may seem to be negative or even destructive. However, the intention is not to leave the reader floundering in the ruins of rent control and rental market regulation. It is conceded that there are problems in the rental housing market which are largely due to the low incomes of may private tenants. This also happens to be the view of the Henderson Report into Poverty. If there is a desire to alleviate these problems then we should attack their root cause - low-income.

Furthermore, we are not so naive as to believe that only some private tenants have low incomes. Others in the community also suffer from poverty. Shouldn't we be concerned about these people as well? Western societies use (or have used) a large variety of redistributive devices including old-age and other pensions, subsidised health schemes, tax rebates, rent control, public housing, etc.

Alternative policies more desirable

Why not scrap this plethora of complicated and administratively unwieldy devices and replace them with one simple scheme? Milton Friedman, Lord Harris and many others have strongly advocated a negative (or reverse) income tax (NIT) which would effectively provide a minimum income for all. This proposal has many advantages, not the least being that it attacks the basic cause of poverty - that is, it is directed at low income. In addition, the NIT-type scheme would be far less costly administratively, freeing valuable resources for other purposes, thus making everyone potentially better off. We should also keep in mind the interesting empirical observation for the United States, known as 'Director's Law' which notes that most existing redistribution boils down to the socially useless process of shifting income backwards and forwards between middle-income families. Very little 'Robin Hood' redistribution is observed to occur.

Suppose, however, that the housing market is, for some reason to be the medium of income redistribution. Would we be led to recommend rent control in these circumstances? The answer is an unequivocal 'no'. Various alternative policies are available including subsidisation of tenants ('hous-

ing allowances'), subsidisation of landlords, and public housing provision. It can be argued forcefully that each of these policies is better than rent control if it is conducted on a rational, business-like, basis. For example, a policy of public housing provision would not follow the model of, say, the New South Wales Housing Commission: individuals would not be herded into large estates nor would they be allowed to occupy subsidised accommodation if they failed to satisfy a strict means test.

The policy that has attracted most attention is the payment of housing allowances to low-income families. While not measuring up to a NIT, a properly-run scheme would have many adavantages. The attraction of the housing allowance approach is that it works with the housing market rather than against it. Consider the remarkable contrast between subsidising the demand for housing and taxing its supply; between the freedom of choice of tenants under the housing allowance scheme and the severe locking-in effect of rent control; between the subsidisation of tenants from taxes paid by those who are better off, and coercion of landlords who may or may not be wealthier than their tenants. Finally consider the finesse with which a housing allowance can be directed at the poorest families as compared with the bluntness of rent control as an instrument for the alleviation of poverty.

Rent control and rental market regulation, in any of their many possible forms, are not policies which can command endorsement and the evidence presented in this volume certainly lends weight to this assertion.

Glossary

BOND - Sometimes known as a 'security bond'. An amount of money a tenant is required to put up as security against damage or default of rent payment. It may be held by the landlord or his agent. In New South Wales and South Australia bonds must be lodged with a government agency known as a 'rental bonds board'.

CAPITAL VALUE - The market value of a property at a particular point of time. Capital value is usually thought to be related to the present value of a stream of net rentals.

COMPETITIVE MARKET - A market where there are many buyers and many sellers and where no buyer or seller is large enough to have an individual effect on price or quantity.

CONTRACT - An agreement made between two parties which sets out the rights and obligations of each party.

DEADWEIGHT LOSS - A loss in potential output due to a misallocation of resources. A tax on a commodity might, for example, force resources out of production of that commodity into less valuable uses. This loss in value is a deadweight loss.

DEMAND - The willingness to pay for quantities of a good. Demand is usually thought of as a schedule of prices and quantities. Willingness to pay for another unit will usually decline as quantity increases.

EFFICIENCY COSTS - Synonymous with **DEADWEIGHT LOSS**.

EQUILIBRIUM - A balance of economic forces between demand and supply such that there is no tendency for a change in price or quantity.

EVICTION - Process of ejectment of a tenant from his rental dwelling.

FAIR RENT - A legal term often used to describe the legal maximum rent on a dwelling set by a rent controller.

HOUSING SERVICES - Dwellings vary in space, mode of construction, plumbing, age, location, etc. The amount of housing services produced by a dwelling depends on these attributes and can be proxied by willingness to pay for the whole package.

HOUSING STOCK - The total quantity of housing services (or dwellings) in a geographical area. The stock of housing services may be increased by the addition of new dwellings or the improvement of existing stock.

INELASTIC SUPPLY - A situation where the quantity supplied of a good responds less than proportionately to any change in its market price. It is sometimes loosely used to mean that the quantity supplied is totally unresponsive to changes in price - a condition which is often alleged to be the case with housing.

KEY MONEY - This is a sum of money required by a landlord, over and above any rent payment, to secure a tenancy. Key money arises in situations of rent control and is usually illegal. It is symptomatic of a housing shortage at the controlled rent.

LANDLORD - The party to an agreement who supplies housing services to a tenant in return for a rent. There may be other rights and obligations associated with the agreement.

LEASE - The agreement between a landlord (the lessor) and tenant (the lessee) whereby housing services are exchanged for a rent

LESSEE - See **TENANT**

LESSOR - See **LANDLORD**

MARKET - The 'place' where a commodity is traded such that the wishes of demanders and suppliers are reconciled in an equilibrium price and quantity.

OPPORTUNITY COST - The cost of an activity in terms of the alternatives foregone by pursuit of that activity.

OUTGOINGS - Term used to describe the direct expenses involved with a landlord supplying housing services to a tenant. These comprise rates, maintenance expenses and

insurance.

PRICE CONTROL - The imposition of a legal maximum (or sometimes minimum) price at which a commodity can be traded. If the price control is effective it will create a shortage. Rent control is a particular kind of price control.

PRINCIPAL TENANT - Where a tenant sub-lets part of his dwelling to a sub-tenant, he becomes the principal tenant.

PROFITEER - Literally someone who makes profits, but usually there is a connotation of excess profits made in some 'unethical manner'. That is, there is an alleged element of exploitation.

PROFITS - Profits may be divided into two types - 'normal' and 'super-normal'. Normal profits are those which neither attract new entry to, or stimulate exit from, an activity. Super-normal profits (or excess profits) are those in excess of normal profits. These may arise due to monopoly power or they may be a more transitory phenomenon arising due to the equilibration of a competitive market. The latter are usually known as quasi-rents.

REDISTRIBUTION - The process of transfer of income or wealth from one group in the community to another group. In the process deadweight losses may well be involved.

RENT - The per period payment required by a landlord, from a tenant, in return for the provision of housing services. There may be other rights and obligations attached to the contractual arrangement between landlords and tenants. The term 'rent' sometimes is used to describe monopoly profits. This is not the sense in which we use it here.

RENT CONTROL - A legislative form which usually involves (i) the imposition of a legal maximum on rents which may constitute a rent freeze and/or the availability of 'fair rent' determinations. (ii) The control of evictions such that they are only allowable on certain grounds after a certain period of notice has been given to the tenant. The 'rent control' part of the legislation is a form of price control.

RENT CONTROLLER - Authority or individual vested with the legal responsibility of controlling rents.

RENTAL MARKET REGULATION - Legislation which can be distinguished from 'rent control' but which does involve some controls on rents and evictions. This type of legislation controls other aspects of the landlord-tenant contractural arrangement including security bonds, repairs, landlords' rights of entry, discrimination, etc. Rental market regulation is closely related to 'consumer protection' and sees the tenant as a consumer of housing services requiring protection from landlords.

SHORTAGE - The situation where the quantity demanded for a commodity exceeds the quantity supplied at the prevailing (usually controlled) price. For example, rent control may create a shortage of housing services.

SITTING TENANT - Literally a tenant in occupancy but more commonly a tenant in occupancy when rent control is in force and may entail a connotation of reluctance on the part of the tenant to move.

SUB-LEASE - The leasing arrangment between a principal tenant and a sub-tenant whereby the principal tenant allows the sub-tenant use of housing services in return for a pecuniary consideration. The process of granting a sub-lease is sometimes known as sub-letting.

SUB-LETTING - Process of granting a sub-lease.

SUB-TENANT - Tenant who rents housing services from another tenant (the principal tenant) rather than directly from the landlord.

SUPPLY - A schedule of prices and quantities of a commodity reflecting suppliers' willingness to provide the commodity in a market. The supply prices will reflect costs of provision including a normal profit.

TENANT - The party to an agreement with a landlord whereby the landlord supplies the use of housing services to the tenant in return for a rental payment. There may be other rights and obligations associated with the agreement.

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Steven N.S. Cheung was born in Hong Kong in 1935 and received his doctorate in economics at the University of California at Los Angeles in 1967. He taught at the California State College at Long Beach from 1965 to 1967, where he received the Distinguished Teaching award of the Board of Trustees of the California State Colleges. His dissertation on *The Theory of Share Tenancy* won him the Fellowship of Political Economy awarded by the University of Chicago in 1967, where he was appointed Assistant Professor of Economics in the following year. In 1969 he went to teach at the University of Washington, since 1972 as a Professor of Economics.

His research comprises the economic explanation of pricing and contractual arrangements, including share-cropping, bee-keeping rentals, ticket pricing, rent and price controls, patent and trade-secret licensing, and the pricing and contractual structures in various industries.

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H. V. Evatt (1894-1965) was a leading Australian politician and jurist. He lectured at Sydney University, and in 1930 was appointed to the High Court of Australia. He at various times in his political career was Attorney General and Minister of External Affairs and was leader of the Australian Labor Party in opposition for many years. He was the first President of the General Assembly of the United Nations and in 1960 became Chief Justice of the Supreme Court of New South Wales.

Milton Friedman was born in 1912 in New York City and graduated from Rutgers before taking his M.A. at Chicago and Ph.D at Columbia. From 1935-37 he worked for the U.S. National Resources Committee and from 1941-43 for the U.S. Treasury. In 1946 he began teaching at the University of Chicago, where he became the Paul Snowden Russell Distinguished Service Professor of Economics. He has also taught at the Universities of Minnesota, Wisconsin and Columbia as well as lecturing at universities throughout the world from Cambridge to Tokyo. Professor Friedman was awarded the Nobel Prize in Economic Science in 1976. He is currently Senior Research Fellow at the Hoover Institution at Stanford University.

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