

---

**New York City Rent Guidelines Board:**

Aston Graves  
*Chairman*

Public Members

Hilda Blanco  
Ellen Gesmer  
Victor Marrero  
Agustin Rivera

Tenant Members

Oda Friedheim  
Galen Kirkland

Owner Members

Joseph Forstadt  
Harold Lubell

**Rent Guidelines Board Staff:**

Timothy Collins  
*Executive Director*

Douglas Hillstrom  
*Director of Research*

Annie Georges  
*Research Associate*

Ashley How  
*Research Associate*

Patricia Stone  
*PIOC Survey Manager*

Andrew McLaughlin  
*PIOC Survey Supervisor*

Leon Klein  
*Office Manager*

Cecille Latty  
*Public Information*

**Rent Stabilized Housing in New York City**  
**A Summary of Rent Guidelines Board Research, 1992**

# Table of Contents

|                                  |   |
|----------------------------------|---|
| A Letter from the Chairman ..... | 5 |
| Acknowledgments .....            | 7 |
| New in 1992.....                 | 9 |

## **Owner Income and Expense**

### ***1992 Price Index of Operating Costs***

|                                    |    |
|------------------------------------|----|
| Introduction .....                 | 13 |
| Rent Stabilized Apartments:        |    |
| Summary.....                       | 14 |
| Elements of the Price Index.....   | 15 |
| Changes in PIOC Components .....   | 17 |
| Rent Stabilized Lofts.....         | 22 |
| Projection of Price Index for 1993 |    |
| Summary.....                       | 22 |
| Components .....                   | 22 |
| Price Index Methodology:           |    |
| Summary.....                       | 25 |
| Changes in Methodology .....       | 25 |

### ***Income and Expense Studies***

|                                 |    |
|---------------------------------|----|
| Introduction .....              | 29 |
| Cross Sectional Study:          |    |
| Sample and Methodology .....    | 30 |
| Rents.....                      | 31 |
| O&M Costs .....                 | 32 |
| O&M Ratios .....                | 34 |
| Longitudinal Study:             |    |
| Sample and Methodology .....    | 35 |
| Rents.....                      | 35 |
| O&M Costs .....                 | 37 |
| O&M to Income Ratios .....      | 39 |
| Income and Expense Audits:      |    |
| Sample Size and Selection ..... | 40 |
| O&M Costs .....                 | 41 |
| Income .....                    | 43 |
| O&M to Rent Ratios .....        | 44 |

### ***Mortgage Financing***

|   |    |
|---|----|
| Introduction .....                      | 45 |
| RGB Mortgage Survey:                    |    |
| Summary.....                            | 46 |
| Response to the Survey.....             | 46 |
| Changes in Underwriting Practices ..... | 47 |
| Financial Availability and Terms .....  | 48 |
| Lending Criteria.....                   | 50 |

### ***The Vacancy Allowance***

|                    |    |
|--------------------|----|
| Introduction ..... | 51 |
|--------------------|----|

### **Vacancy Allowance Study:**

|                                     |    |
|-------------------------------------|----|
| History of the Vacancy Allowance... | 52 |
| Arguments For and Against .....     | 54 |
| Policy Options.....                 | 58 |
| Regulatory Responses to             |    |
| Preferential Rents .....            | 59 |

## **Tenant Income and Housing Affordability**

### **Income and Affordability Report:**

|   |    |
|---|----|
| Income and Job Growth .....                                     | 64 |
| Rents .....   | 66 |
| Public Assistance and Homelessness ...                          | 67 |
| Housing Court Actions and Evictions...                          | 71 |
| Effects of Rent Regulation on Economic and Racial Integration:  |    |
| Introduction .....  | 71 |
| Selected Literature on Racial and Economic Integration .....    | 72 |
| Measuring the Effect of Rent Stabilization on Integration ..... | 74 |
| Conclusion.....   | 76 |

## **Population and Housing Supply**

### **Analysis of 1980 and 1990 Census Data:**

|                        |    |
|------------------------|----|
| Summary .....          | 78 |
| Housing Stock.....     | 78 |
| The Rental Market..... | 79 |

### **Housing Supply Report:**

|  |    |
|--|----|
| New Construction, Tax Abatements and In Rem Housing..... | 81 |
| Real Estate Tax Arrearage .....                          | 85 |
| Tax Foreclosure.....                                     | 86 |
| Residential Co-op and Condominium Activity .....         | 87 |

## **Rent Stabilized Hotels**

|   |    |
|---|----|
| Price Index of Operating Costs for Rent Stabilized Hotels ..... | 90 |
| Transient Rentals in SRO-Type Buildings:                        |    |
| Background/Summary.....   | 91 |
| Findings.....   | 92 |

## Appendices

### **Appendix A: Guidelines Adopted by the Board:**

- A.1 Apartments & Lofts .....97
- A.2 Hotel Units.....97

### **Appendix B: 1991 Price Index of Operating Costs for Rent Stabilized Apartments:**

- B.1 Expenditure Weights, Price Relatives, Percent Changes and Standard Errors, All Apartments, 1991 .....98
- B.2 Price Relatives by Building Type, All Apartments, 1991 .....99
- B.3 Percentage Change in Real Estate Tax Sample by Borough and Source of Change, 1991 PIOC .....100
- B.4 Tax Change by Borough and Community Board, 1991 PIOC .....100

### **Appendix C: 1992 Price Index of Operating Costs for Rent Stabilized Apartments:**

- C.1 PIOC Sample, Price Quotes per Spec, 1991 vs. 1992 .....101
- C.2 Expenditure Weights, Price Relatives, Percent Changes and Standard Errors, All Apartments, 1992 .....102
- C.3 Price Relatives by Building Type, All Apartments, 1992 .....103
- C.4 Distribution of Matched 1991 and 1992 Tax Sample by Borough and Building Size.....104
- C.5 Percentage Change in Real Estate Tax Sample by Borough and Source of Change, 1992 PIOC .....105
- C.6 Tax Change by Borough and Community Board, 1992 PIOC .....105
- C.7 Changes in Price Index of Operating Costs, Expenditure Weights and Price Relatives, 1982-1992 .....106

### **Appendix D: 1992 Price Index of Operating Costs for Rent Stabilized Lofts:**

- D.1 Expenditure Weights and Price Relatives, Lofts, 1992.....108

### **Appendix E: Income & Expense Studies:**

- E.1 Longitudinal Study: 1989 and 1990 Average Operating Costs, Rent, and Income...109
- E.2 Cross Sectional Study Sample: Number of Buildings by Size and Cell Weights .....109
- E.3 Cross Sectional Study: Estimated Average O&M Costs, Average Rent and Average Gross Income by Borough, Building Size and Age ....110

### **Appendix F: Mortgage Financing:**

- F.1 Interest Rates for New Financing and Refinancing, 1992 .....111

- F.2 Loan Characteristics, 1992.....111

- F.3 Interest Rates for New Financing and Refinancing for Lending Institutions Responding in 1991 and 1992.....112

- F.4 Comparison of the CPI (U.S. Avg.) with Change in Median Sales Price (per sq. ft.) of Pre-1975 Rental Buildings.....112

### **Appendix G: Vacancy Allowance:**

- G.1 Vacancy Allowances, 1968-1992.....113

### **Appendix H: Tenant Income and Housing Affordability:**

- H.1 Annual Average Unemployment Rates by Borough, 1987-1991 .....114
- H.2 Payroll Employment by Industry for NYC as of December, 1988-1991 .....114
- H.3 1980 and 1990 Census Median Contract Rent of Renter Occupied Housing Units by Borough .....114
- H.4 Consumer Price Index for All Urban Consumers, New York-Northern New Jersey, 1987-1991 .....115
- H.5 1980 and 1990 Contract Rent of Renter Occupied Housing Units in New York City, Decennial Census .....115

### **Appendix I: Housing Supply:**

- I.1 1980 and 1990 Census - Changes in New York City's Housing Inventory .....116
- I.2 1980 and 1990 Census Rental Vacancy Rate .....116
- I.3 Permits Issued for New Housing in New York City, 1987-1991 .....116
- I.4 Units in Buildings Receiving Preliminary Certificates for 421-a Tax Abatements, 1989-1991 .....117
- I.5 J-51 Tax Abatements, Final Certificates Issued, 1988-1991 .....117
- I.6 HPD Vestings of Occupied Multiple Dwellings, FY'85-FY'92.....117
- I.7 Tax Arrearages, 1988-1991 .....118
- I.8 Number of Residential Co-op and Condominium Plans Accepted for Filing by the Attorney General's Office, 1985-91 .....118

### **Appendix J: 1992 Price Index of Operating Costs for Rent Stabilized Hotels:**

- J.1 Expenditure Weights, Price Relatives, Percent Changes and Standard Errors, All Hotels, 1992.....119
- J.2 Price Relative by Hotel Type, 1992 .....120
- J.3 Percentage Change in Real Estate Tax Sample by Source of Change and Hotel Type, 1992 PIOC.....121

---

# A Letter from the Chairman

The 1992 “guideline season” was dominated by discussions concerning the current recession and its impact upon the rental housing industry. While operating costs rose at a modest pace owners experienced notable increases in collection and vacancy losses. In filling vacant apartments many owners found themselves unable to negotiate the full amount of legally allowed rents. The softening of the rental market has begun to restore some of the bargaining power which has eluded tenants for decades. In normal economic times this would be an appropriate period for the city to begin considering a “transition from regulation to a normal market of free bargaining between landlord and tenant” as contemplated by the authors of the rent regulation laws.

Three observations should lend caution to such discussions.

First, there is the practical reality that so many of the city’s tenants are suffering under the fallout of the current recession. Unemployment in the city surpassed 12% in July and public assistance rolls have reached the highest levels in decades. The loss of rent and eviction protections could add an untimely and unconscionable burden to this present hardship.

Second, there is the simple fact that times change. While the citywide vacancy rate has risen (to 3.8% as of last count) it remains within emergency levels (below 5%) and there is no clear trend indicating which way the market will turn next. Related to this is the fact that economic hard times have forced many families to double up - perhaps adding to the vacancy rate and partly concealing the continuing shortage. The next housing and vacancy survey, due in 1994, should give us a better sense of long term trends.

Third, among real estate investments - commercial, co-op, and regulated rentals - the regulated rental sector has proven to be the most stable and secure. A broad perusal of business failures and distressed properties will demonstrate that, relative to other investments, rent stabilized housing has provided the kind of steady and predictable returns that make it less vulnerable to recessionary forces. While there is no question that regulated rental housing is not a booming industry, neither is it undergoing the kind of bust experienced in other sectors. In short, losses in the regulated housing sector do not present a compelling case for deregulation.

Here a serious cautionary note must be added. While the income producing ability of rent stabilized properties may have weathered the recession so far, fixing our hopes on past results is a risky undertaking. To borrow the analogy often used by management expert, Dr. W. Edward Deming: anticipating future performance by reading past results is like driving a car with your eyes on the rear view mirror. In the coming years the Rent Guidelines Board will be called upon to look ahead - at demographic and economic indicators, changes in regulatory burdens, taxes, water and sewer charges, building conditions and a host of other factors that might influence the viability of rental housing. The Board must commit itself to ensure that reasonable rents will be maintained and that housing will not be lost due to the impact of its decisions on the system.

Once again the Board’s research staff has proven itself up to the task of producing a broad range of quality data and professional analysis. As a team, Tim Collins and Doug Hillstrom have led the staff to significant new levels of accomplishment in each of my three years with

the Board. Doug remains largely responsible for the research including, this publication. Tim provides the administrative and legal support necessary to navigate the new challenges and opportunities which regularly arise. It remains a pleasure to work with each of them.

As in the past I would like to close with a special note of appreciation for the Board members. Throughout the Winter and Spring we met in twelve sessions to consider numerous staff

reports and hours of public testimony. Meeting attendance was always very high and the quality of member participation was excellent. Establishing rents for a million apartments is not the kind of activity the public finds particularly endearing.

"Thank you's" are few and far between. But the members of the Rent Guidelines Board should take pride in a job well done.

Thank you.

Aston L. Graves  
September 15, 1992

---

# Acknowledgments

This volume summarizes all the major research projects - including the 1992 Price Index of Operating Costs (PIOC) - produced by the staff of the Rent Guidelines Board during the 1992 guideline "season."

This is the second year that the staff has produced the PIOC in addition to its other research projects. Pat Stone and Andrew McLaughlin computerized all of the PIOC forms and data this year, making administration of the 1992 survey far easier than previous efforts. Pat's redesign of the owner survey mailing materials and Andrew's excellent supervision of the PIOC survey staff were also valuable contributions. Annie Georges and Ashley How gathered fuel oil prices throughout the year and were also responsible for the Labor and Fuel calculations. Their diligence alleviated some of the PIOC "crunch" and improved the quality of the PIOC data.

The staff benefitted greatly from the professional assistance and technical support of Speedwell, Inc. Tony Blackburn assembled the Speedwell team and, as usual, provided valuable comments on the PIOC drafts. Jim Hudson prepared the tax and water & sewer relatives and worked with RGB staff on data verification. Finally, members of the survey team included John St. Victor, Malcolm Riddick, Nicole Latham, David Sealy, Bert Bryan, Marcia Campbell, Idica Wilson, Kevin Blakely, Wil Knowles and Shirley Fenelon. They gathered 1200 price quotes and deserve praise for their dedication and thoroughness.

The RGB also benefitted greatly from the assistance of several city and state agencies. The Department of Finance (DOF) helped to prepare files used in computing the PIOC tax relative. For the third consecutive year, DOF also

supplied the RGB with crucial data from owner income and expense (I&E) filings. Lisa Avruch produced much of this information, often under tight time constraints. We would like to extend special thanks to Julie Walpert for acting as liaison between the DOF and the RGB in these and other matters.

This year the DOF was able to audit a sample of owner income and expense statements - one of the RGB's long-standing goals. Under the direction of Deputy Commissioner Glenn Newman, DOF staff completed detailed audits of 46 owners. This information greatly enhanced the RGB's understanding of the I&E data. None of this would have been possible without the continuing support of Commissioner O'Cleireacain. Finally, Martha Stark provided essential assistance with various issues, in particular obtaining sales data for rent stabilized housing.

We would like to thank Commissioner Michetti and the Department of Housing Preservation and Development (HPD) for supporting a number of projects, including this year's hotel study. Moon Wha Lee, Assistant Commissioner of Housing Policy and Supervision at HPD has assisted in many ways and is already helping out with research projects which will come to fruition in 1993.

A number of other agencies supported this year's research agenda. Joe Salvo, Deputy Director of City Planning's Population Division, provided 1990 Census data. City Planning also supplied the RGB with important data on real estate tax arrearages. The New York State Division of Housing and Community Renewal made it possible for staff to undertake the first in-depth study of transient income in rent stabilized hotels. Howard Hecht and Eddie

Blanco, in particular, were very helpful. Finally, we are also indebted to other government agencies such as the Real Estate Financing Bureau of the New York State Attorney General's Office, the New York State Public Service Commission, and the New York City Water Board for providing information and relevant data for a number of this year's research projects.

Lastly, two disclaimers must be made regarding this report. First, while this volume includes this year's staff research, the Board was

provided with a wide variety of additional sources of information including written submissions and oral testimony from building owners, tenants, housing scholars, public officials and other interested parties. Second, although this report does include a summary of the Board's guidelines for 1992-93, it is not intended as an explanation of these guidelines. Those who are interested in this issue should consult the Board's explanatory statements which are issued in conjunction with this year's rent orders.

Tim Collins  
*Executive Director*

Doug Hillstrom  
*Director of Research*



---

# New in 1992

This is the fourth annual compilation of research from the Rent Guidelines Board. While a fair amount of the material in *Rent Stabilized Housing in New York City* remains similar from season to season, we thought it would be useful to point out some of this year's research highlights, as well as additions to the appendices which might be useful to other housing researchers.

For readers who are unfamiliar with the Price Index of Operating Costs, a short **Introduction to the PIOC** has been added describing its purpose and historical evolution (Page 13). Appendix C7 includes **Changes in the PIOC from 1982 to 1992** for all apartments and the Pre '47 and Post '46 sectors.

The owner income and expense (I&E) study was greatly expanded this year. The cross-sectional study examined income and expenses for more than 14,000 buildings, compared to 500 in previous years. Due to the enormous expansion of the sample, it was possible to break down **Average Operating and Maintenance Costs, Rent, and Gross Income** by borough, building size and age of structure (Page 32 and Appendix E3). The longitudinal I&E study was staff's first attempt to compare changes in actual expenses with the measurements of the PIOC (Page 38). Finally, the **Department of Finance Audits** of 50 buildings gave the RGB a more complete understanding of the accuracy of the I&E data (Page 40).

One of the special studies undertaken this year was an **Examination of the Vacancy Allowance** (Page 51). This piece looks at the history of the vacancy rent increases, arguments for and against the allowance, some of the policy options available to the RGB, and the emerging issue of preferential rents. Appendix G describes

the vacancy allowances authorized by the RGB from 1968 through the present.

Details of the **1990 Census** were first released last fall. An analysis of this data shows some striking changes in the housing stock over the past ten years, including a large increase in the owner-occupied stock and overcrowding which is much more serious than previously supposed (Page 78).

One of the issues which the RGB has debated with some energy over the years is the extent of "transient" rentals in rent stabilized hotels. Tenant advocacy groups have argued that owners benefit greatly by short term rentals not subject to rent stabilization regulations, making rent increases unnecessary. Owner groups have contended that such a policy has merely punished "good" owners who rent to long-term stabilized tenants. This year's study of **Transient Rentals in SRO-type Buildings** breaks new ground by examining rent and income data for a sample of rent stabilized hotels (Page 91). It appears that hotel owners derive a considerable portion of their revenue from transient rentals while rooming houses and SROs which are registered with the State Division of Housing and Community Renewal seem to have little or no transient income.

The **Value of Rent Stabilized Buildings** was another issue which beguiled the RGB throughout the 80's. This year the RGB was able to obtain information from the Department of Finance showing the enormous increase in sales prices for rent stabilized buildings which occurred in the 80's. The data also illustrates the equally sharp drop in property values thus far in the 90's (Appendix F.4).



---

## *Owner Income and Expense*

---

---

# 1992 Price Indices of Operating Costs

Prior to establishing its annual guidelines, the Rent Guidelines Board (RGB) is obligated by law to examine operating and maintenance costs that are incurred by owners

of stabilized  
buildings.

In the early  
70's, the

## INTRODUCTION

RGB relied heavily on its *Price Index of Operating Costs for Rent Stabilized Apartment Houses* to measure changes in these charges and costs. However, since the late 70's, some critics as well as RGB members felt that additional data was needed to determine the profitability of stabilized housing rather than just changes in costs.

The PIOC measures the price change in a market basket of goods and services which are used in the operation and maintenance of stabilized buildings. The original PIOC expenditure weights and market basket were devised by the U.S. Bureau of Labor Statistics (BLS) which was retained by the RGB as the PIOC contractor from 1970 to 1981. From 1982 to 1990, the PIOC was prepared by private consulting firms. In 1991, the RGB staff's growing expertise and familiarity made it possible to move the PIOC "in house." This is the second year that staff has produced the PIOC.

In order to address the ongoing concerns about the accuracy of the PIOC methodology in estimating cost changes, the RGB commissioned the PIOC contractors to undertake various PIOC-related studies in the 80's. However, for a variety of reasons, these studies did not lead to substantive changes in the PIOC expenditure weights, methodology, or the way the study was administered.

Since 1989, staff has completed a substantial amount of PIOC-related research in

an effort to improve the accuracy of the PIOC. The major topics of concern have been the reliability of the 1982 expenditure study (which re-weighted the PIOC components), the accuracy of the PIOC between 1970 and 1982, and the true level of the O&M to rent ratio. In addition, the availability of landlord income and expense (I&E) information from the Department of Finance has made it possible for staff to produce reliable estimates of the average rent and operating and maintenance costs for stabilized buildings. Staff found that the I&E information tended to confirm the reliability of the PIOC expenditure weights.

Beginning with the 1991 PIOC, several administrative changes were made to facilitate the data collection process. Staff reorganized and computerized the PIOC vendor database, updated the mailing list for the owner survey, and completely redesigned the owner survey mailing materials. In addition, price quotes for fuel oil were gathered on a monthly basis rather than once a year.

Following completion of the 1992 PIOC, further efforts have been made to improve the quality of data collection and our understanding of the PIOC. Utility rates and charges are now tracked on a bi-monthly basis instead of on a yearly basis. An effort to gauge the accuracy of the PIOC by comparing cost increases with actual expense increases will be continued in forthcoming years. While the controversy concerning the accuracy and legitimacy of the PIOC can never be fully resolved, efforts will continue to improve the accuracy of the PIOC on both the administrative and technical levels.

# RENT STABILIZED APARTMENTS

## Summary

The overall increase in the Price Index of Operating Costs for Rent Stabilized Apartment Houses in New York City (PIOC) between April 1991 and April 1992 was 4.0%, the lowest since 1987. With the exception of the taxes, utilities, and labor components, increases in all of the other components were at or below the increase in the Consumer Price Index over the same period. Last year we noted that the recession had made it difficult for contractors and vendors to raise prices. In the current PIOC this effect is even more pronounced.

This year's increase in taxes was 11%. In previous years rising assessments had the greatest impact on taxes. This year was different. Billable assessments were up moderately, but most of the increase in the tax relative was due to a rise in the tax rate.

Labor costs were up 5.2%, the same increase as last year. The rate of increase in labor costs has been remarkably consistent during the past six years, ranging from 5.1% in 1989 to 5.7% in 1987 and 1990.

In last year's PIOC projection we estimated that fuel costs would fall by 12%. The fuel projection assumed that winter temperatures would be normal and that recessionary pressures would push prices down to 1990 levels. These assumptions proved to be reasonably well founded. Fuel prices this year decreased by 10.9%.

Most of the price relatives in the utilities component declined this year. The cost of electricity, steam, and telephone service were all down while gas costs increased moderately. However, water and

sewer costs were up sharply, rising by 15.7%. Since water and sewer charges now make up about half of the utilities component, the overall increase in utilities was 6.6%. In fact, utilities showed the second largest increase (after taxes) and accounted for a large part of the increase in the PIOC.

As we noted in last year's PIOC report, Contractor Services and Administrative Costs are largely labor-based and depend to a great extent on the strength of the local economy. Given current economic conditions in New York City, it is not surprising that the increases in the Contractor Services and Administrative Costs components (2.4% and 2.8% respectively) are the lowest in the last ten years, as well as BELOW the general rate of inflation.

This is the fifth consecutive year that increases in insurance costs were less than the overall PIOC increase. Increases in the Parts & Supplies and Replacement Cost components, which have been remarkably consistent (and low) over the past eight years, continued to follow the

### Change in the Components of the Price Index of Operating Costs for Rent Stabilized Apartments, April, 1991 to April, 1992

|                            |          |
|----------------------------|----------|
| Taxes .....                | 11.0%    |
| Labor Costs .....          | 5.2%     |
| Fuel Costs .....           | -10.9%   |
| Utilities Costs .....      | 6.6%     |
| Contractor Services .....  | 2.4%     |
| Administrative Costs ..... | 2.8%     |
| Insurance Costs .....      | 2.3%     |
| Parts & Supplies .....     | 2.5%     |
| Replacement Costs .....    | 3.8%     |
| <br>Overall .....          | <br>4.0% |

same pattern.

## Elements of the Price Index

### *Owner Survey*

The owner survey is used to gather information on management fees, insurance, and non-union labor. Survey forms, accompanied by a letter describing the purpose of the PIOC, were mailed to the owner or managing agent of the stabilized building. If the survey form was returned, the owner/manager was contacted by an interviewer to verify the information and to obtain additional information if necessary. All of the owner/managing agent's price quotes were verified by calling the insurance company, the management company or the non-union employee.

Last year we included all owners who registered with DHCR between 1984 and 1989 on the mailing list for the owner survey. For the 1992 PIOC we used only owners who registered in 1989 and/or 1990. By eliminating the earlier registrations, the mailing list was purged of some buildings which are no longer stabilized. In addition, this year's updated list included fewer incorrect addresses and fewer managing agents no longer associated with the properties.

A stratified sampling scheme was used to choose a total of 5674 addresses for the owner mailing - about 300 fewer than in 1991. The number of buildings chosen in each borough was proportional to the share of all buildings in that borough. In addition to the "new" sample, all of the owners who responded to last year's survey were contacted again this year. Including these "old" owners expanded the total sample size to 5894.

Although this year's owner survey sample was slightly smaller than last year's, the number of questionnaires returned increased by nearly

half, from slightly over 500 to 730. The improved response rate can probably be attributed to the aforementioned update of the mailing list and a complete redesign of the survey materials. This year the survey form, the letter accompanying the survey form, and the mailing envelope were all redone. The purpose was to simplify the survey instrument and to encourage owners to respond.

One of the greatest improvements in this year's PIOC was to expand the number of management company quotes. In 1991, only 20 verified price quotations were obtained, down from 35 in 1990. This year the figure was increased to 52. Upping the number of management company quotes has greatly decreased the standard error for this component. The number of verified price quotes in 1992 and 1991 for the owner survey is shown in Appendix C of this report.

### *Fuel Oil Vendor Survey*

Last year a special effort was made to scrutinize the fuel oil component. Specifically, we wanted to answer the following questions:

1. Is it true that a minority of units are heated by #6 fuel oil, even though the PIOC assumes the majority use this type of fuel?
2. Are there few vendors of #6 oil, and if so, do these vendors exercise any type of anti-competitive pricing power?
3. Would it be useful to survey vendors on a month-to-month basis rather than once a year?

The first two questions were answered in the negative. Based on responses to several questions incorporated in the 1991 owner survey it was found that a majority of units continue to be heated by #6 oil. In addition, although there

are not a large number of #6 vendors, price quotes were obtained from 12 companies, presumably enough for some degree of competition.

Based on last year's investigations, staff thought it would be useful to survey fuel vendors on a month-to-month basis rather than once a year. A monthly survey allows us to keep in touch with fuel vendors and to gather the data on a consistent basis (i.e. on the same day of the month for each vendor). Calling vendors each month minimizes the likelihood of misreporting and also reduces the reporting burden for the companies which don't care to look up a year's worth of prices. Finally, the monthly survey shifts some staff work out of the very busy Spring period.

The monthly survey has been conducted since August 1991. Only a few vendors declined to participate on a monthly basis. Several of these did agree to provide two year's worth of data in April 1992.

### *Tax Computations*

The list of buildings used to compute the tax relative was updated for the first time since 1986 for the 1991 PIOC. Last year's list included all buildings which registered at least once with DHCR between 1984 and 1989. This same building database has been used to compute the tax relative this year.

The most significant change made in the tax computations in 1992 was to obtain a list of in rem buildings from the Department of Housing Preservation and Development. Last year the "notes" in the Finance Department's Open Balance Register were carefully examined and buildings were excluded if it was reasonably clear that an in rem action was still pending. There was some ambiguity in this approach and both Speedwell and RGB staff thought it would be preferable to obtain a list of in rem buildings.

### *Vendor Survey*

The Vendor Survey is used to gather

price quotes for contractor services, administrative costs, parts & supplies, and replacement costs. During the summer of 1991 multiple "databases" were designed for the vendor survey portion of the PIOC. All of the vendor information from last year, which formerly occupied over 1500 separate folders, was manually entered into 18 computer databases. The computerization of the vendor data successfully improved both the administration of the 1992 vendor survey and the quality of the survey data by

- greatly reducing the amount of paperwork;
- making information on vendors readily accessible, thereby allowing customization of the vendor sample;
- providing ALL of the information the surveyors needed on one or two sheets of paper, which saved time and helped improve the quality of the data.

As in prior years, an effort was made to update the vendor database by adding new vendors and deleting those who no longer carry the products in question. Vendor quotes were obtained in person and over the telephone. The method used depended on the particular product or service being priced (e.g. all painters were contacted by telephone due to the difficulty of meeting with them during business hours).

The procedures used for gathering price quotes were unchanged from prior years. The number of price quotes for some vendor items was reduced this year in order to reallocate surveyors' time to more important items, such as management fees, insurance and painters. For a detailed description of the items priced and the number of price quotations obtained, refer to the Appendix C.

### *Other Items*

In addition to the items previously

discussed, a number of other pieces of information are needed to complete the PIOC. They are:

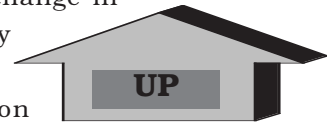
- Union contract and benefit information
- Social security rates
- Unemployment insurance rates
- Heating degree days
- Utility rate schedules

These items are used in computing some of the labor components, changes in utility costs for electricity, gas, steam, and telephone, and the cost-weighted change in fuel prices.

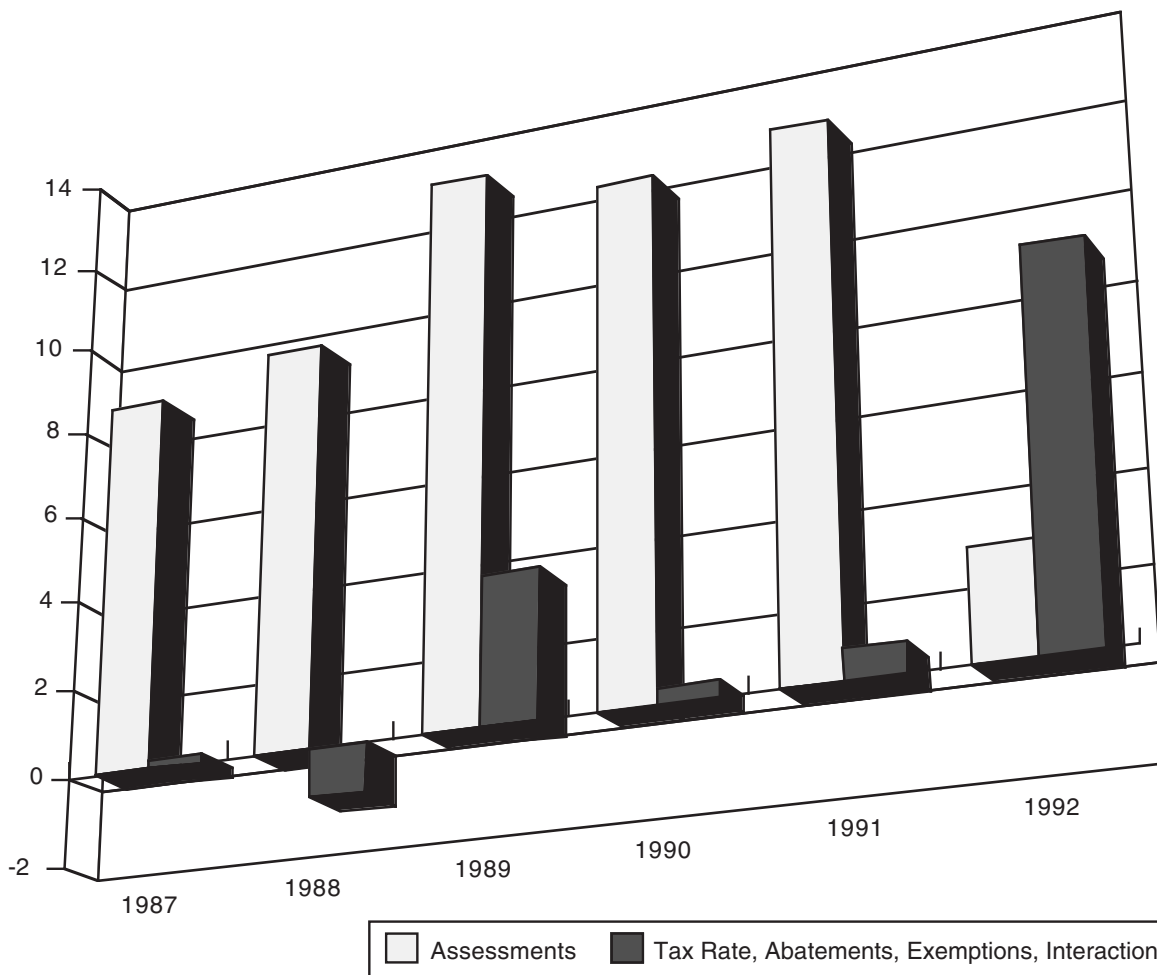
## Changes in PIOC Components

**Taxes +11%**

The tax component is based entirely on real estate taxes. The change in taxes is estimated by comparing the aggregate taxes levied on



### Components of Tax Change, 1987-1992



Source: *Price Index of Operating Costs, 1987 - 1992*

Note: Overall change in tax component by year: 1987 (8.7%), 1988 (8.1%), 1989 (15.8%), 1990 (12.0%), 1991 (12.8%), and 1992 (11.0%).

rent stabilized apartment houses in 1991 and 1992. (For additional detail on how the tax computation differs from last year see the earlier section on PIOC elements). The tax data was obtained from the Department of Finance.

Taxes levied on rent stabilized apartments increased by 11% in the past year. It was the eighth consecutive year in which the rate of increase in this component exceeded the overall PIOC increase.

The chart on the previous page disaggregates the increase in real estate taxes into changes in billable assessments, and the tax rate, tax exemptions, and abatements. Changes in assessments and the tax rate usually have the biggest impact on this component. The influence of exemptions and abatements is often negligible. We have grouped these with the tax rate for purposes of illustration.

Less than one-fourth of the overall tax increase this year can be attributed to the increase in assessments. This is in marked contrast to previous years, where rising assessments was by far the most important factor. The increase in the tax rate was largely responsible for the overall increase this year.

This year the percentage increase due to increases in billable assessments has fallen substantially below recent levels (i.e. 12.5% in 1989, 11.7% in 1990, 12.2% in 1991). Actual assessments for rent stabilized buildings fell last year, but since transitional assessments continued to increase, the so called "billable" assessments (i.e. the figure on which an owner's taxes are actually based) also rose.

As a check on the accuracy of the tax relative, the tax change was also computed using the Finance Department's open balance register (OBR). The OBR includes information on bills sent and payments received by Finance. Since the tax relative has never been computed using the OBR, we had to make some assumptions regarding the transaction codes in the OBR. Using a variety of assumptions, the tax relative varied from 10.4% to 11.3%, basically in accord

with the standard methodology.

### *Labor Costs +5.2%*

The labor component is based on several measures of labor costs, including union contracts (wages and benefits), non-union wage increases as measured by the owner survey, and changes in social security and unemployment insurance. Overall changes in labor costs have been remarkably consistent during the past several years, approximating just over 5% each year.

The consistency of the labor component masks some of the variation in recent years within the subcomponents. The wage portion of labor costs is declining while the benefits portion has skyrocketed. In the 80's wage increases were typically over 5% per year. In 1992, by comparison, union wage increases ranged from 3.2 to 4.0% while benefits rose over 13%.

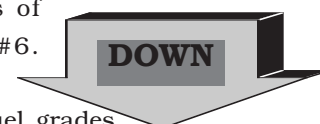


### *Fuel Oil -10.9%*

The fuel component measures changes in the price of three types of fuel oil - #2, #4, and #6. Within the fuel price component each of the fuel grades has a different weight which reflects the percentage of rent stabilized units using the particular type of fuel oil. In the current year's PIOC, #6 oil accounts for about half of the fuel oil component while the other grades make up roughly 25% each.

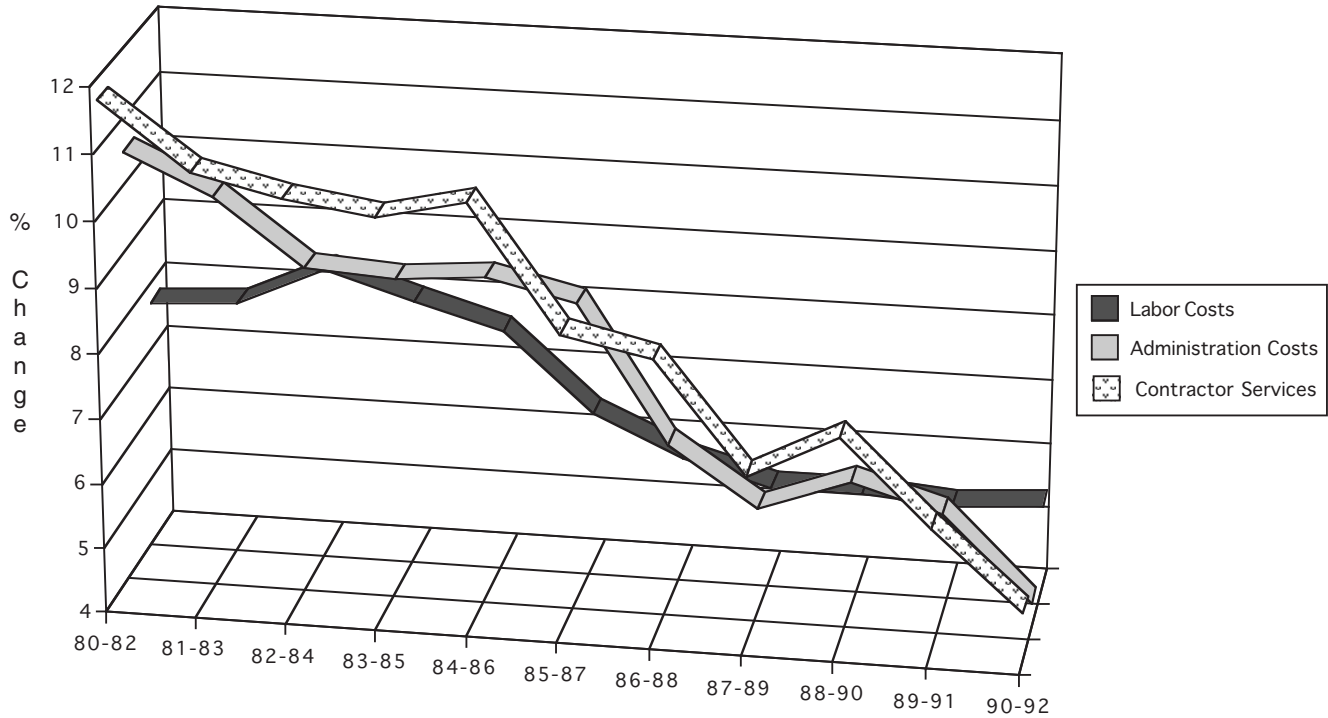
To calculate changes in fuel oil costs staff gathers monthly price data from fuel oil vendors and weights the data using a degree day formula. The number of degree days is a measure of average heating requirements.

Last year prices rose moderately (4.6%). The invasion of Kuwait in August 1990 was followed by a huge increase in fuel oil prices (see chart on opposite page). Although prices remained high throughout most of last year's



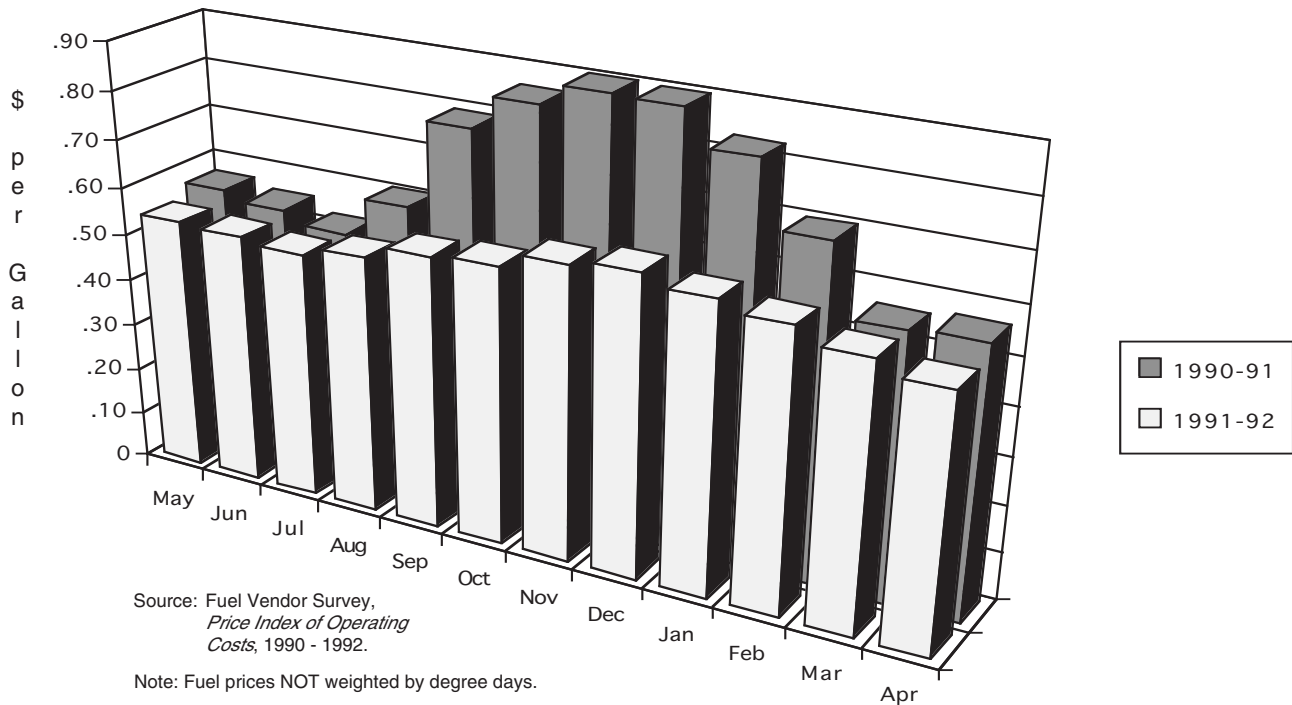


### Percentage Change in Labor Costs, Contractor Services and Administration Costs (Three Year Average)



Source: Price Index of Operating Costs, 1980 - 1992

### Price of #6 Fuel Oil, 1990-91 and 1991-1992



heating season, the weather was much warmer than usual. In fact, it was one of the warmest heating seasons on record. The higher temperatures nearly offset the increase in fuel oil prices, resulting in the relatively small change in the fuel oil price index.

This year the situation was much different. There was no devastating cold spell as in 1990, nor did a war erupt to drive prices higher as in 1991. The end of the Persian Gulf war and the deepening recession both acted to push down prices, as we predicted last year. Although the weather was slightly warmer than normal it was considerably colder than last year. This interaction of lower prices and cooler temperatures created the decrease of 10.9%.

Among the various fuel oil components, the decreases were: #6, minus 13.4%, #4, minus 11.3% and #2, minus 5.4%. The price volatility for the heavier grades of fuel oil is traditionally greater than for the #2 grade. This accounts for the larger decreases in #4 and #6 fuel oil.

### *Utilities +6.6%*

The utilities component of the index consists primarily of electricity, natural gas, and water & sewer charges. Telephone and steam costs are also part of the utilities index but the weight of these two items is very low. In the case of most of the utility components, changes in price are measured using the PIOC specifications (i.e. the quantity of electricity, steam etc. being purchased) and the changes in rate schedules.

Over the past several years water and sewer charges have come to represent half of all utilities costs. The double-digit increases in water/sewer charges during the 80's and 90's (including a 45% increase in 1990) make water & sewer costs an increasingly important part of landlords' operating budgets. This year total water & sewer charges were up 15.7%.

Electricity costs were down about 10% this year. Electricity costs have traditionally

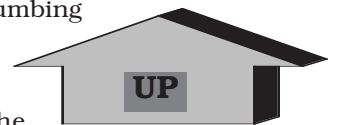
been measured on an April-to-April basis rather than a cost-weighted basis (as in the case of fuel oil and gas). This year a rate increase for Con Edison was approved as of April 24. According to Speedwell Inc., past procedure has been to include increases in the electricity rate in the PIOC if they occurred on or before April 15. Increases occurring after that date are included in the PIOC for the following year. We have adhered to this practice. As a result, the recently enacted rate increase will influence the 1993 PIOC.

The decrease in electricity costs was due entirely to a change in the fuel adjustment charge, which is a measure of the cost of raw materials needed to generate electricity. The decrease in the fuel adjustment charge reflects last year's price of oil, natural gas, nuclear materials, etc. The decrease in materials expenses is passed on to electricity consumers.

Gas costs increased marginally (about 4%) in the past year. Gas, like fuel oil, is measured largely on a "cost-weighted" basis which takes both price and heating degree days into consideration. The increase in gas costs is mainly due to this year's weather conditions (which were colder than last year) rather than to changes in rates.

### *Contractor Services +2.4%*

The Contractor Services component is composed of sixteen items, the most important of which are painting and plumbing repairs. The increase in the Contractor Services component this year is the lowest since 1969. Last year we reported that some contractors had reduced prices due to a shortage of business. The impact of the recession is even more apparent in the 1992 PIOC. For example, repainting, which accounts for almost half of the Contractor Services index, traditionally shows a substantial increase from year to year. This year the component was up less than 1.5%. Other important items



(plumbing repairs and roofing) were unchanged.

### *Administrative Costs +2.8%*

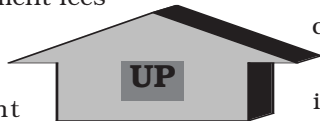
Nearly two-thirds of the administrative costs component consists of management fees while most of the remainder is accountant and attorney services. Management fees are obtained from owners and are verified by calling the management companies. The data is used only if the management company has no equity interest in the apartment building. We were able to greatly increase the number of management company quotes this year and to reduce the standard error for this component (see Appendix C.2).

In the 1991 PIOC management fees rose only 2%. We assumed last year that the small rate of increase in management fees was probably a reflection of the weakness in the real estate sector. Of the owners and management companies interviewed for this spec last year, 60% reported either the same management fee as in 1990 or a decrease in the fee. Only 40% reported increases - and most of these were quite moderate. The increase in management fees this year is slightly greater than last year (3.3%) but still quite low by historical standards.

Fee quotations were obtained from accountants and attorneys based on specifications in the PIOC. Traditionally these costs increase faster than the rate of inflation. It appears that the economy has finally caught up with these professionals. Accountant fees were up only 3.7% and the cost of attorneys' time was unchanged.

### *Insurance Costs +2.3%*

A total of 218 verified insurance quotes were obtained this year, an increase of 100% over 1991. Information on insurance costs and coverage (i.e. deductible, value, coverage change) was

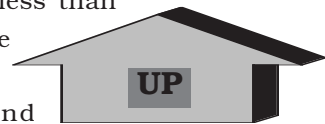


obtained through the owner survey. The survey staff used a policy number from the management company or building owner to confirm the 1991 and 1992 price quotes with the insurance carrier. To insure that the PIOC accurately measures the effect of changes in the price of insurance coverage, the influence of changes in coverage is statistically removed in the computation of the insurance component.

Following the enormous increases in insurance costs in 1986 and 1987, recent increases in insurance have been quite moderate - 1.6% in 1988, -.6% in 1989, 3.6% in 1990, 4.4% in 1991, and 2.3% this year.

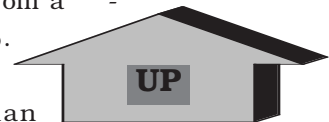
### *Parts and Supplies +2.5%*

Increases in this component have been remarkably consistent since 1983, ranging from 2.3% to 4.7%. This year was no exception. Given the low weight of the parts and supplies component in the PIOC (less than 3%) and the small price increase in this component, parts and supplies had scarcely any impact on the overall increase this year.



### *Replacement Costs +3.8%*

The replacement costs index is less significant than the parts and supplies component, accounting for slightly more than 1% of the price index. Price changes have been quite low since 1983, ranging from a - 0.4% decrease to 3.8%. The increase this year was slightly higher than usual (and the highest since 1983) but has very little effect on the overall increase in the PIOC.



# RENT STABILIZED LOFTS

## Summary

The overall increase in the loft price index was 3.9%, which is about the same as the increase in the apartment index (see table). The biggest difference between the apartment and loft indices is the weight for legal expenses. In the apartment PIOC legal fees have a weight of less than 1.5%, but comprise almost 12% of the loft index. Since legal fees were unchanged this year, the effect was to depress the amount of increase in the loft index. However, other factors worked in the opposite direction. Labor costs increased at a greater rate than in the apartment sector. Fuel costs fell less since fewer lofts use #6 fuel oil. All of these effects combined resulted in the 3.9% increase.

### Change in the Components of the Price Index of Operating Costs for Rent Stabilized Lofts, April, 1991 to April, 1992

|                                   |             |
|-----------------------------------|-------------|
| Taxes .....                       | 11.0%       |
| Labor Costs.....                  | 5.5%        |
| Fuel Costs.....                   | -9.6%       |
| Utilities Costs .....             | 6.6%        |
| Contractor Services .....         | 2.4%        |
| Administrative Costs, legal ..... | unchanged   |
| Administrative Costs, other ..... | 3.3%        |
| Insurance Costs .....             | 2.3%        |
| Parts & Supplies .....            | 2.5%        |
| Replacement Costs.....            | 3.8%        |
| <b>Overall.....</b>               | <b>3.9%</b> |

# PROJECTION OF PRICE INDEX FOR 1993

## Summary

The table on the next page shows the projected price increases for 1992-1993 compared to actual increases measured by the 1992 price index. The major differences between the 1993 projection and the 1992 PIOC are in the Tax and Fuel components.

During the next year, the momentum of economic recovery will probably bring somewhat larger increases in some of the PIOC components since market conditions in the past few years have depressed demand and prices for services to stabilized buildings. Components such as Contractor Services and Administrative Costs will increase at a somewhat greater rate. There will be modest increases for the Fuel and Tax Components.

## Components

### Taxes

The importance of real estate taxes has grown over the years. Its weight in the PIOC has increased from 18 percent in 1985 to about 25 percent in 1992. It has become the largest single component of the PIOC. In the previous eight years, increases in taxes exceeded the overall increase in the PIOC. Next year we expect a much smaller increase (about 4.9 percent), or slightly less than the overall projected PIOC increase.

Tax bills are based on changes in billable assessments, tax rates, and changes in exemptions and abatements. Based on the preliminary tax roll, the Finance Department

expects the overall increase in billable assessments for Class Two rental properties to be 4.9 percent. The tax rate has not yet been finalized but will probably remain unchanged. Based on an increase in billables of 4.9 percent and no change in the tax rate, we project an increase of 4.9 percent in taxes.

### *Labor-Based Components (Contractor Services, Labor Costs, and Administrative Costs)*

Each of these three components is based primarily on some type of labor cost. In the case of contractor services most of the expense is wages of plumbers and painters. The category "Labor Costs" is based entirely on wages of building staff (e.g. supers, porters). Administrative Costs are largely management fees, attorney fees, and accountant fees.

The larger increases among these three components may be in contractor services and administrative costs. The projected increases of 4.8 percent and 4.4 percent respectively are based on the latest three-year averages of the contractor services and administrative costs components. These projections are somewhat higher than this year's increases and consistent with an economic recovery which may boost both demand and prices.

It is generally quite easy to "project" the labor component since union wage settlements are known well in advance. This year's projected increase for the union-labor component (5.5%) is based on the actual wage and benefit increases under the current contracts, which cover the 1992-1993 PIOC period. The increase in the non-union portion of the labor component is based on this past year's increase.

### **1992 Price Index and 1993 PIOC Projection**

|                           | <u>Price Index<br/>1991-92</u> | <u>Projected<br/>1992-93</u> |
|---------------------------|--------------------------------|------------------------------|
| Taxes.....                | 11.0%                          | 4.9%                         |
| Labor Costs.....          | 5.2%                           | 5.5%                         |
| Fuel Costs.....           | -10.9%                         | 5.1%                         |
| Utilities Costs.....      | 6.6%                           | 8.8%                         |
| Contractor Services.....  | 2.4%                           | 4.8%                         |
| Administrative Costs..... | 2.8%                           | 4.4%                         |
| Insurance Costs.....      | 2.3%                           | 3.4%                         |
| Parts & Supplies.....     | 2.5%                           | 4.0%                         |
| Replacement Costs.....    | 3.8%                           | 2.6%                         |
| <b>Overall .....</b>      | <b>4.0%</b>                    | <b>5.3%</b>                  |

### *Utility Costs*

Utility costs consist of electricity, natural gas, water/sewer charges, purchased steam, and telephone bills. The first three items account for over 95% of the utility index.

The projected increase in the utility index represents the highest increase among all of the PIOC components. Con Edison and Brooklyn Union Gas will impose rate increases for gas and electricity in the 1992-1993 PIOC period. In fact, this projection accounts for two increases in electricity rates because the effective dates fall within the 1992-1993 PIOC period.

Con Edison has received approval from New York State's Public

Service Commission to increase electricity rates. The first two increases are effective April 17, 1992 and April 1, 1993. These dates fall within the 1992-1993 PIOC period. The increase this April is 5.2 percent and the next estimated increase will be about 7.7 percent, based on Con Edison's projected increase in revenue. However, it should be noted that the changes in total costs for electricity will also depend on the fluctuations in the fuel adjustment charge from month to month. As a result, the price of electricity may rise more or less than the changes in the rate schedules indicate.

Con Edison will also increase its natural gas rates by 2.2 percent and its steam rates by 3.3 percent in October 1992. In addition, Brooklyn Union Gas will increase its gas rates in October 1992 but the exact percentage is not yet known. This projection assumes that Brooklyn Union Gas will increase its rates by the same proportion as in October 1991.

The Water Board initially proposed an increase of 14.5 percent for water/sewer charges; however, the proposed increase has been scaled back to 9.9 percent because of the projected surplus in the Water Board's operating budget for the current fiscal year. This will account for about 60 percent of the overall increase in the utility index. Water and sewer expenses have risen substantially over the years. The weight of the water/sewer component in the 1991 PIOC was twice as much as the 1985 PIOC weight. It is more than likely that the water and sewer component will account for over 50 percent of the utility index in 1993.

Combining all of the increases and multiplying them by approximations of next year's weights yields a projection of an 8.8 percent increase in the utilities component.

### *Fuel*

Predicting changes in fuel oil costs is a risky undertaking. Since the break up of Soviet Union, which had been the world's largest petroleum producer for nearly 20 years, the level of petroleum supply now more than ever hinges on the stability of the Middle East countries. Barring any unforeseen wars or natural disasters, and assuming relatively weak but improving economic activity through much of the 1992-1993 PIOC period, our estimate is that cost-weighted fuel prices should increase about 5.1 percent.

On the supply side, production from OPEC countries will increase, especially in Kuwait as it expects to fully restore its pre-war capacity by the end of 1993. In fact, it is also possible for Iraq - because of economic needs - to comply with the United Nations' resolution so that it may increase its petroleum exports. Moreover, because of the sluggish economic growth in the United States during the past two years, there are ample petroleum stocks to meet any upshot in short-run demand if the needs arise. Lastly, the decrease in petroleum output by the former Soviet Union should not have any short-term effects in the petroleum market.

If the petroleum supply remains stable as we suppose, short-run prices will be contingent upon the magnitude of the economic recovery and the weather. According to the United States Department of Energy's "Mid-Price Case" scenario, assuming slow economic growth and a moderate rate of inflation, "the world oil price decreases to \$18 in the first quarter of 1992, recovers to \$19 in the third quarter, then stabilizes at \$20 in the fourth quarter and throughout 1993." Based on these projected prices and the actual prices for 1991 and the first quarter of 1992, crude oil price will increase about four percent in 1993. Our price projection assumes that the fuel oil prices will follow a similar pattern. Adding in the



assumption that the weather will be slightly cooler next year results in the projected increase of 5.1%.

### *Insurance Costs*

After a period of substantial increases in insurance costs, the insurance market finally stabilized in 1988. The combined effects of a weak economy and a soft real estate market have moderated increases in recent years. Assuming the 1992-1993 PIOC period to be relatively weak for economic recovery, there should be a 3.4 percent increase in insurance costs. The projected increase in insurance costs is based on the latest three-year average.

### *Parts & Supplies*

Price increases for Parts and Supplies have been relatively consistent during the past ten years. The Parts and Supplies component is a very small part of the PIOC, with a weight of less than 3 percent in 1992. The projected increase of 4 percent is based on the latest three-year average.

### *Replacement Costs*

Replacement Cost increases have been consistently low since 1983, averaging less than 2% per year. The weight of this item has fallen steadily over the years and now accounts for about 1% of the PIOC. The projected increase is based on the average price increases over the past three years.

## PRICE INDEX

## METHODOLOGY

### Summary

The issue of "PIOC Methodology" is extremely broad. It can encompass everything from the "big" issue of the reliability of the price index as a means of estimating increases in costs to the sources of lists used in the owner survey. Last year a report on "PIOC Methodology" was prepared for the Board (see *Rent Stabilized Housing in New York City: A Summary of Rent Guidelines Board Research*, 1991). In that report staff made a number of recommendations, both large and small, regarding possible improvements to the PIOC. Although the technical issues await discussion and resolution by the Board, staff has made progress on some of the administrative issues discussed in that report.

### Changes in Methodology

#### *Computerization of Vendor Data*

During the summer of 1991, multiple "databases" were designed for the vendor survey portion of the PIOC. The vendor survey is used to gather price quotes for the contractor services, parts & supplies, and replacement parts components of the PIOC. All of the vendor information from 1990, which formerly occupied over 1500 separate vendor folders, was manually entered into eighteen computer databases. The computerization of the vendor data improved both the administration of the survey and the quality of the survey data by

- greatly reducing the amount of



paperwork;

- making information on vendors readily accessible, thereby allowing optimization of the vendor sample;
- providing ALL of the information our surveyors needed on one or two sheets of paper, which saved time and improved the quality of the data.

The format of the newly created vendor forms includes all of the information which the surveyors need to know, including the name of the firm and phone number, last year's contact person, a brief specification of the item to be priced, and whether a backprice is needed.

### *Fuel Oil Vendor "Test"*

Last year staff enumerated three major advantages to gathering fuel oil price information on a monthly (rather than yearly) basis:

- the magnitude of the April data gathering "crunch" would be reduced;
- PIOC manpower could be shifted from gathering fuel quotes to other activities such as increasing the size of the owner survey or more thorough data validation. Alternately, the total size of the PIOC manpower budget could be reduced;
- the data would probably be more reliable. Gathering the fuel information every month insures that price quotes are obtained at the same time of the month for every firm. In addition, it is also easier to insure the consistency of the data by keeping in touch with one contact person at each company.

When we proposed a test of monthly fuel gathering, the major unresolved questions

were: "Will the vendors cooperate?" and "Will it be relatively easy to contact all vendors each month?" Both questions were answered in the affirmative. Forty-five companies agreed to participate in the survey; in August 1991 we obtained 45 quotes for #2 fuel oil, 20 #4 quotes, and 14 #6 quotes (vs. 41, 15 and 12 respectively for the previous year). In the second month of the survey, it took only 3.5 hours to contact all of the vendors.

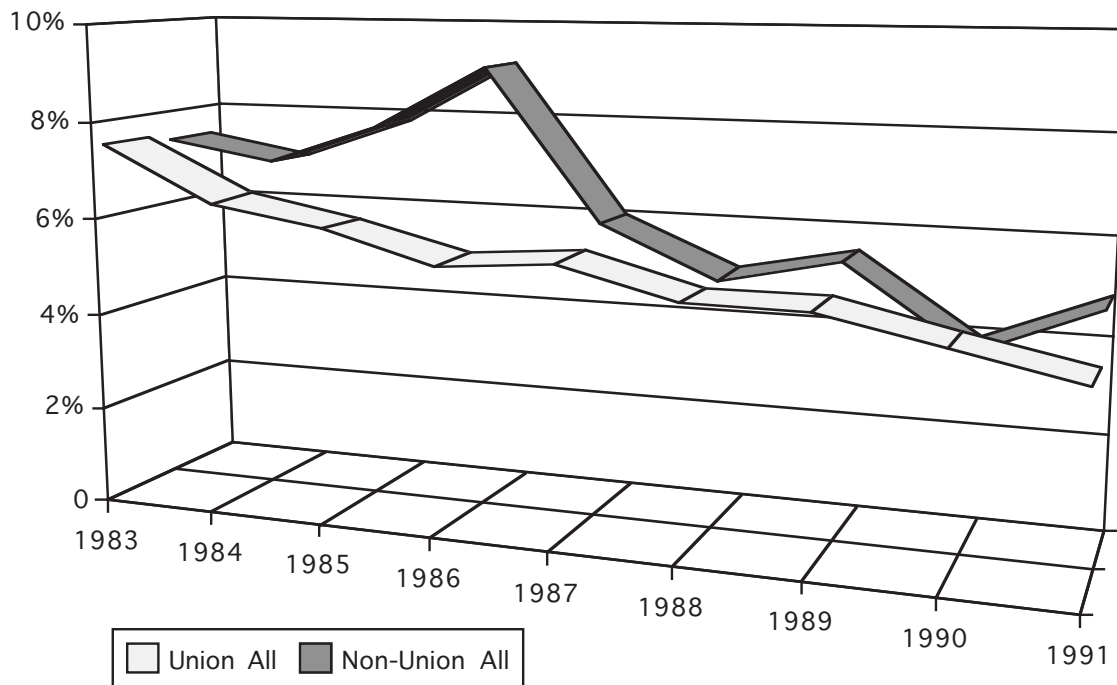
### *Non-union Labor*

Last year we pointed out that wage quotes for non-union labor are difficult to obtain. Abt Associates, in prior submissions to the Board, proposed alternatives to the current data gathering methods, such as using BLS data or union wage settlements as surrogates for non-union wage increases. During the summer of 1991 we examined the feasibility of these proposals.

It quickly became apparent that secondary data sources (e.g. BLS and NYS Department of Labor) are either incomplete and/or published too infrequently to be useful surrogates for the PIOC owner survey. For instance, although the Department of Labor gathers wage data for major industries and occupations, not all occupations are surveyed each year. The BLS publications cover a variety of subjects, including wages for hotel and motel workers, but there is a substantial lag between the time the data is gathered and its publication date. The results of the 1991 wage survey will not be published until July 1992 -- too late for the 1992 PIOC.

Another alternative which has been suggested is to use union labor settlements as a surrogate measure for changes in non-union wages. The graph on the next page shows changes in the PIOC for non-union wages since 1983. In seven of the nine years the two wage

## Comparison of the Percentage Change in Union Labor and Non-Union Labor Costs



Source: *Price Index of Operating Costs, 1983-91.*

indices are within one percent of each other; however, there were large differences in 1985 and 1986. These two discrepant years may reflect strong demand for labor during the booming mid-80's or the difference may simply be due to sampling or non-sampling error in the collection of the non-union wage data. In any case, it is interesting to note that non-union wage increases appear to have outpaced union increases during the 80's and early 90's.

Our investigation of the non-union labor component has not yet yielded any perfect solutions to the problem. Staff will continue to investigate the issue and explore other possible solutions before proposing any changes in the PIOC.

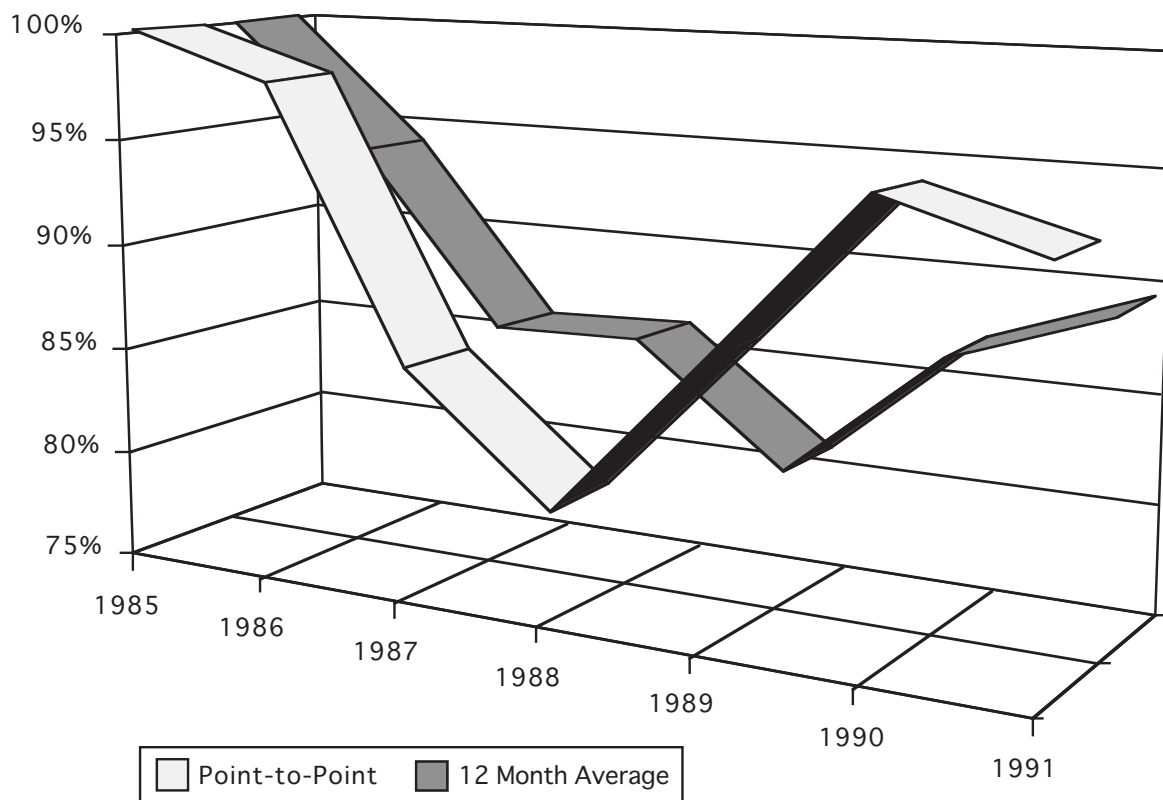
### *Electricity Price Relative*

In 1983 measurement of the fuel oil price relative was changed from an April-to-April to a "cost-weighted" formula. At the time of this change, RGB staff prepared a memo showing how the electricity relative would be affected by a similar alteration in methodology. For reasons which remain unclear, the Board decided not to alter the April-to-April formula.

The April-to-April method can lead to peculiar (and arguably fallacious) results. For instance, in 1989, the largest of the electricity relatives (spec 402) increased by 8.9% on an April-to-April basis. Yet, if all 12 months of the year had been averaged, the cost of electricity would actually have DECREASED by 5.8% and the overall PIOC would have been reduced from 6.7% to 6.2%.

The graph above shows the cumulative

### Change in the Price of Electricity, 1985-1991



Source: *Price Index of Operating Costs, 1985-91.*

Note: The chart uses 1985 as its base year. Subsequent years reflect comparisons with the 1985 cost level. Cost changes are based on PIOC spec #202.

change in electricity costs since 1985 for each of the two measurement methods. The cost of electricity declined from 1985 through 1988 and has been increasing since then. Even so, electric costs remain lower than in 1985.

It has been argued that any difference between the two measurement methods will balance out "in the long run." There is some evidence to support this position. Using the point-to-point method, the cumulative change in costs over the last six years is -7%; the comparable figure for the 12-month average method is -11%. The difference is barely noticeable in the overall PIOC.

The "everything will balance out" argument does ignore a number of possible

considerations. First, since "time is money," aberrations in the electricity relative will still benefit or deprive landlords EVEN IF the change measured by the two methods is identical in the long run. Second, there is no real assurance that costs will actually even out in the long run. Finally, it would be very simple to convert to a 12-month average method since the consultants (and now staff) have traditionally gathered the electricity data for the entire year. ○

---

# Income and Expense Studies

Since its establishment in 1969, the Rent Guidelines Board has utilized scores of independent studies and reports to determine whether its rent adjustments have adequately

## INTRODUCTION

compensated owners for changes in operating costs. Yet, disputes concerning data sources and methods rendered much of this information controversial and inconclusive. In 1990 the Board launched a new effort to examine past assumptions and methodologies. The RGB staff has since been able to develop and analyze unprecedented levels of new information.

In 1986 the City Council enacted Local Law 63, which requires owners of rental property to file annual income and expense statements with the Department of Finance. The law exempts buildings with 10 or fewer units or an assessed value of \$40,000 or less. Although the I&E statements are strictly confidential (RGB staff is unable to scrutinize information for individual properties), Finance has provided summary data for a random sample of rent stabilized buildings. The sampling strategy and list of rent stabilized properties were provided to the Finance Department by the RGB.

This is the third annual I&E study. In the first of these studies a sample of 500 properties was chosen and estimates of rent and operating expenses were calculated. For the first time, staff was able to compare O&M to rent ratios based on I&E data with previous estimates of the O&M to rent ratio.

Last year's I&E study was similar to the first but was refined in some ways. A new sample of 500 rent stabilized properties was chosen. I&E statements with no listed rental income were

excluded from the sample and Department of Finance assessors reviewed expenses in the "miscellaneous" category. Expenses which were inappropriate (e.g. mortgage interest) were deleted while other expenses (e.g. corporate taxes) were reallocated to the proper categories. Finally, the RGB was able to obtain information for buildings with O&M to income ratios in excess of 100%.

In the first two years the I&E study was limited to 500 buildings. This sample was sufficiently large to compute reliable estimates of rent and operating expenses, but was not so enormous as to overwhelm Finance staff with data entry work. This year, following computerization of all the 1991 I&E filings, the sample size for the I&E study has been greatly increased, to over 14,000 buildings.

In addition to this cross-sectional data, this year the RGB obtained "longitudinal" data for the first time. Comparing the same sample of buildings over time is the best way to measure increases in rent and O&M costs. The longitudinal sample is also a valuable tool for evaluating the price index.

Although the I&E forms were FILED in 1991, the cost and rent data for this year's studies is largely from calendar years 1989 and 1990 for the longitudinal study and for calendar year 1990 for the cross-sectional study. An analysis of filing dates for the submissions shows that 85% of landlords used calendar year 1990 as their fiscal year while about 7.5% used a period beginning prior to January 1990 and 7.5% used a period starting after January 1990. Based on this distribution, the average rents and costs reported in this study are as of July 1990 for the cross-sectional study. The longitudinal study measures changes from July 1989 to July 1990.

In addition to these two studies, the Department of Finance supplied several auditors over a three month period to conduct audits on the incomes and expenses of 46 rent stabilized buildings. The findings of these audits add a well documented point of reference for future discussions on industry conditions.

The audit results suggest that the current relationship between operating costs and rent revenues for typical properties has not deteriorated nearly as much as prior reports may have indicated. Although the proportion of each rent dollar devoted to operating costs has risen over the years, much of this rise may be explained by dramatic changes in the stabilized housing inventory as well as by differences in data sources:

- the stabilized stock is significantly older than it was in 1969;
- a large portion of the “better” buildings with low operating cost to rent ratios were converted to co-operatives;
- estimates of rent levels in the early period of stabilization do not adjust for collection and vacancy losses (the new rent data categorically excludes these losses reducing the denominator in the O&M to rent ratio); and
- with the passage of formerly rent controlled units into the rent stabilization system, over two thirds of the current stabilized stock is now composed of pre-war buildings which historically had high O&M to rent ratios.

With these observations in mind it becomes apparent that what remains of any recorded rise in relative operating cost burdens is far more benign than past characterizations admit. The clear implication is that the Rent Guidelines Board has fulfilled its legal obligation to ensure fair compensation for rises in operating costs. The findings of the audit report provide strong support for this conclusion.

## CROSS SECTIONAL STUDY

### Sample and Methodology

The RGB supplied the Department of Finance with a list of approximately 39,000 properties which registered with DHCR. Finance matched this list of block/lots with the 1991 I&E filings. This matching process reduced the number of properties on the list from 39,000 to about 14,000. Buildings were “lost” for the following reasons:

1. The number of units in the building was less than 11. Owners of buildings with less than 11 apartments (without commercial units) are not required to file I&E forms (17,000 buildings);
2. The owner did not file an I&E form (6,400 buildings, or about one-sixth of the buildings on the list. Some of these may have been co-ops);
3. No unit count could be found for the property (500 buildings);
4. No “apartment rent” was recorded on the I&E form. In these cases the form was improperly filled out or the building was vacant. (800 buildings);
5. No match was made with the Assessed Value File (100 buildings).

Using these 14,000 buildings, Finance produced “cell” statistics as they have done in the past. The procedure was slightly different this year. Due to the large number of buildings in the sample we were able to request cell statistics for all combinations of building sizes (e.g. 11-19 units) and all boroughs. As it turned out, some

of these cells contained too few properties to compute reliable statistics. Data for these cells are not reported.

## Rents

The average monthly rent collected by landlords (all units) was \$504. Rents for Post '46 units are substantially higher (\$688) while pre-war units rent for less (\$428). In the boroughs, rents follow the traditional pattern - Manhattanites pay the most (\$664), followed by residents of Queens (\$456), while rents in Brooklyn (\$405) and the Bronx (\$387) lag behind.

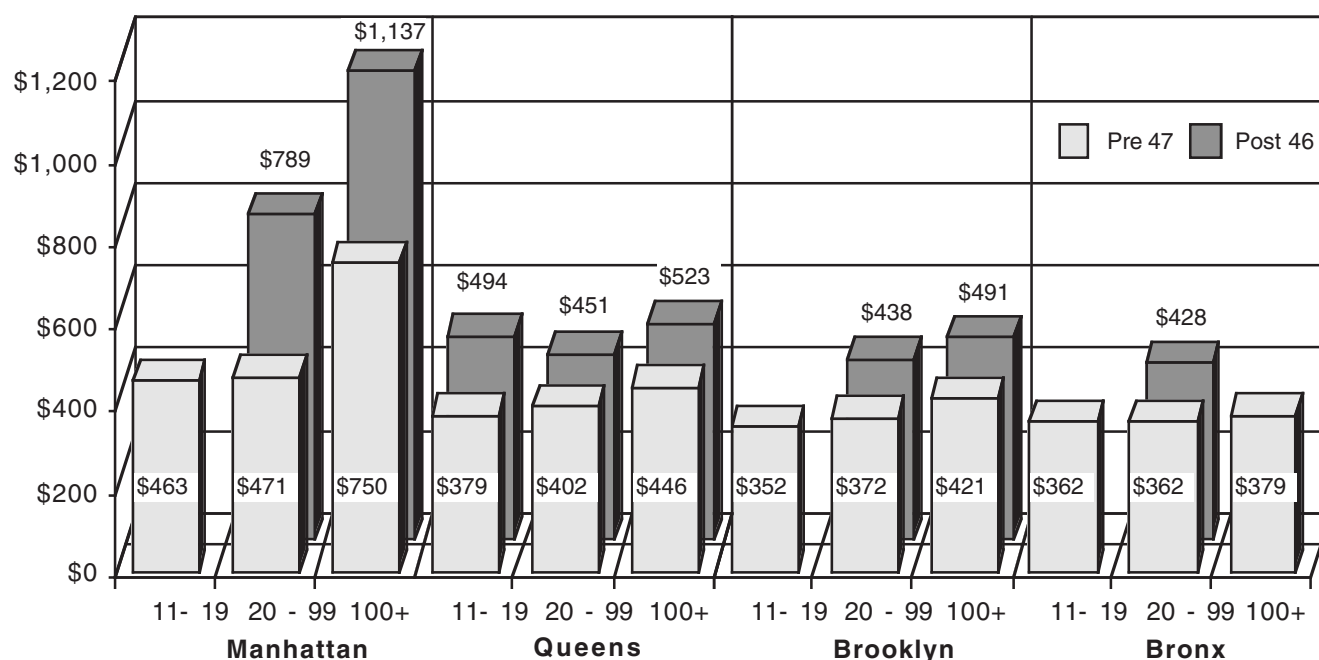
It is interesting to note the relationship between rents registered with DHCR<sup>1</sup> and the

rents collected by landlords as measured in our I&E study. Two years ago, using our 500 building sample, we estimated that rent collected was 90% of registered rent. The proportion is the same two years later. The percentage does not vary in the outer boroughs (.89) and is slightly higher in Manhattan (.93). The gap between legal rents and rents actually collected may reflect a number of factors, including preferential rents, collection losses, and/or vacancy losses.

With a sample size of more than 14,000 buildings (over 600,000 units) it is possible to compute reliable statistics on rent for most of the

<sup>1</sup> Since DHCR rents are measured as of April of each year, we computed a weighted average of 1990 and 1991 data. The figure for the city as a whole was \$562 for July 1990.

**Average Rent per Unit per Month  
by Borough and Building Size**



Source: 1991 Income and Expense Filings, New York City Department of Finance.

Note: Sample sizes for 11-19 unit Post '46 buildings in Manhattan, Brooklyn and the Bronx and Post '46 100+ buildings in the Bronx are insufficient in size for the computation of average rents. All rent statistics are based on an average of at least 40 buildings.

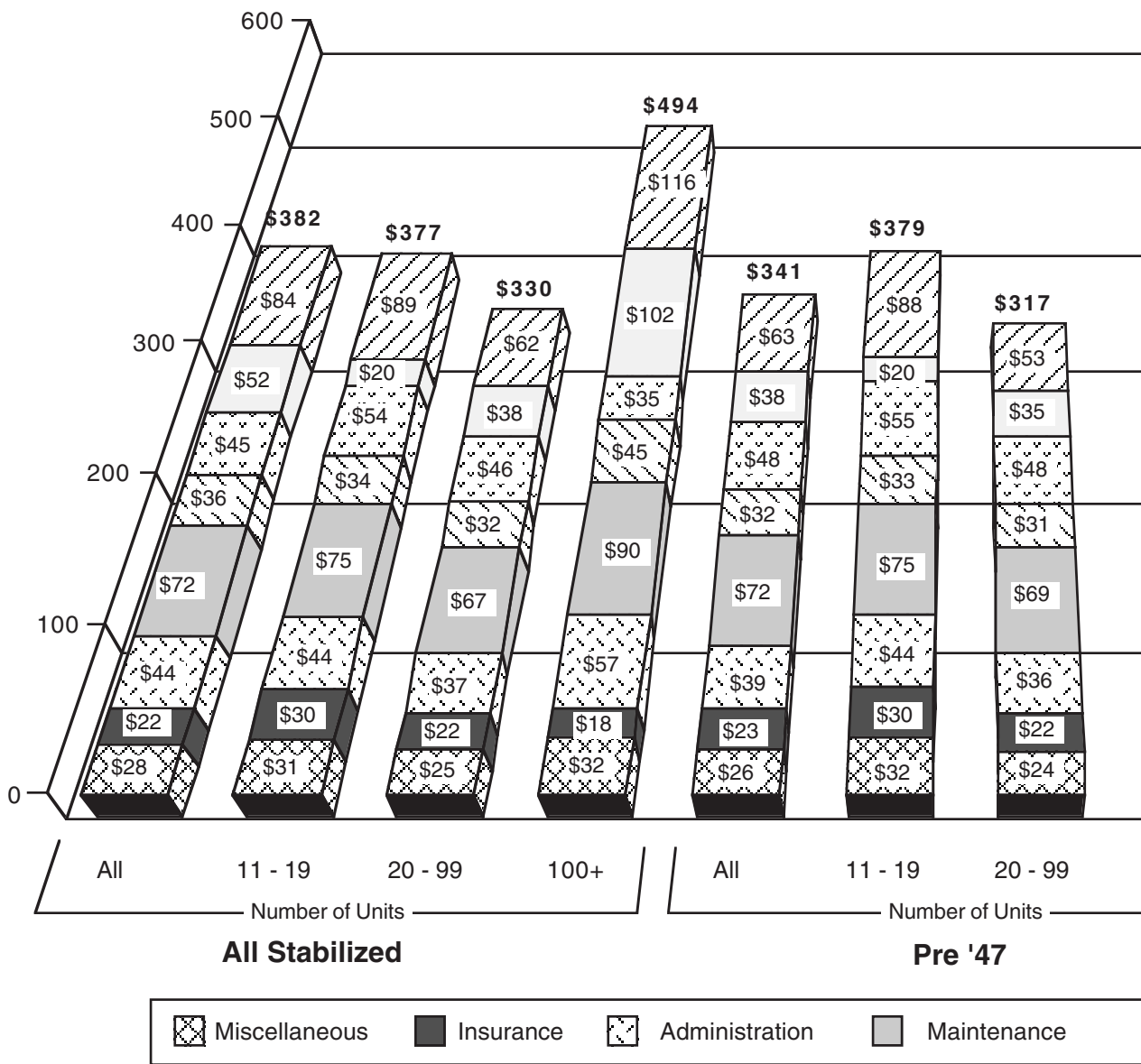
building types by borough. The chart on the previous page shows average rents for each of these building types.

Average gross income per unit, which includes income from the sales of services (e.g. laundry) as well as rent from commercial units, was \$564. In other words, landlords as a group derive about 11% of their income from sources other than apartment rents.

O&M Costs

The average monthly operating and maintenance cost for all the units in our sample is \$382. Compared with this average, costs are substantially higher for Post '46 units (\$483) and marginally lower for the pre-war stock (\$341). In the boroughs, costs generally parallel rents - lowest in the Bronx and highest in Manhattan.

Estimated Average Operating and Maintenance



Source: 1991 Income & Expense Filings. Note: Components may not add due to rounding. Figures are costs per apartment



The chart below shows costs broken down into the various components by building size and pre- or post-war status. Note that this chart does NOT adjust the miscellaneous expense category. For the longitudinal section of this income and expense study assessors from the Department of Finance examined the miscellaneous category and reallocated and/or eliminated expenses where this was appropriate. The expenses reported here are

NOT adjusted based on the assessors' work on the longitudinal study. If they had been, one would expect miscellaneous expenses (average for all buildings) to shrink from \$28 to \$8. About \$4 would be disallowed, while \$16 would be transferred to other categories, largely administration and maintenance.

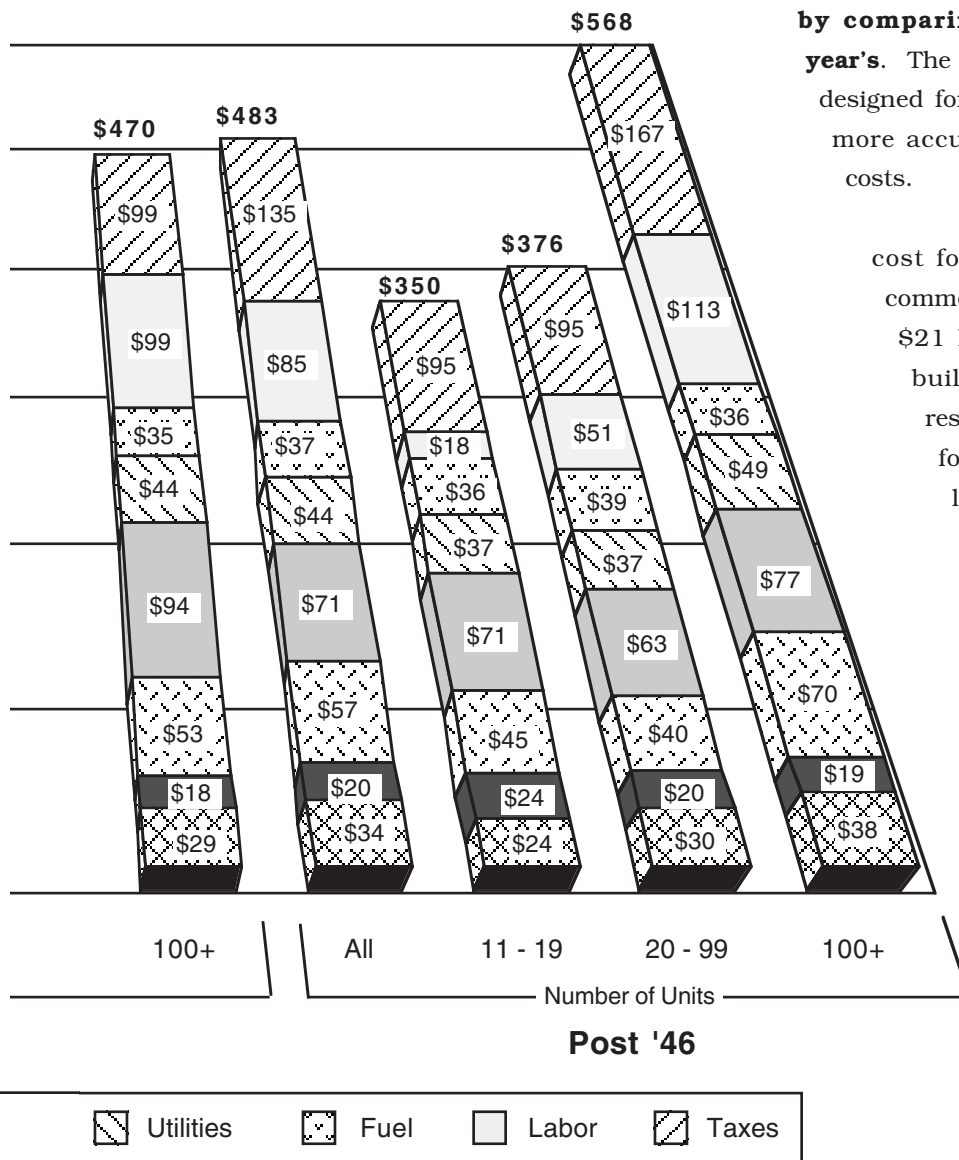
Expenses are very similar to those reported last year, indicating that the previous 500 unit sample was more than adequate for the purpose of estimating cost levels. **Note, however, that no attempt should be made to compute a percentage increase in costs by comparing these figures with last year's.** The longitudinal study (page 35) is designed for this purpose and is a much more accurate indicator of changes in costs.

The average monthly O&M cost for those buildings WITHOUT commercial units is \$361, or about \$21 less than the average for all buildings. In examining the "all residential" category last year we found that administration and labor costs accounted for more than half of the difference.

The distribution is somewhat different this time. Taxes for all residential buildings represent over 50% of the \$21 difference. Most of the remaining difference is attributable to the two categories of maintenance and administration.

**O & M**

## Costs by Building Size and Age



unit per month.

Ratios

The box to the right shows the O&M to rent and O&M to income ratios. In prior years these ratios were computed using O&M costs which reflected the assessors' reduction in miscellaneous expenses. To preserve continuity, and to allow comparisons with prior years, the overall expense level was once again deflated to account for reductions in miscellaneous expenses.<sup>2</sup> This adjustment reduces overall expenses about 1%, from \$382 to \$378. The ratios were calculated using this figure.

The O&M to rent ratio is .75, compared to .72 last year and the year before. The O&M to income ratio is .67 as opposed to .65 in the prior two years. Although some of the increase could reflect differences between the current group of buildings and the 500-unit samples, most appears to be due to worsening market

<sup>2</sup> The percentage reduction in expenses used was based on the findings of the assessors this year. For additional details see the longitudinal section of this report.

| O&M to Rent and<br>O&M to Gross Income Ratios |                |                           |
|---|----------------|---------------------------|
|   | O&M to<br>Rent | O&M to<br>Gross<br>Income |
| All Stabilized                                | .75            | .67                       |
| Pre '47                                       | .79            | .70                       |
| Post '46                                      | .70            | .63                       |
| All (residential)*                            | .73            | .70                       |

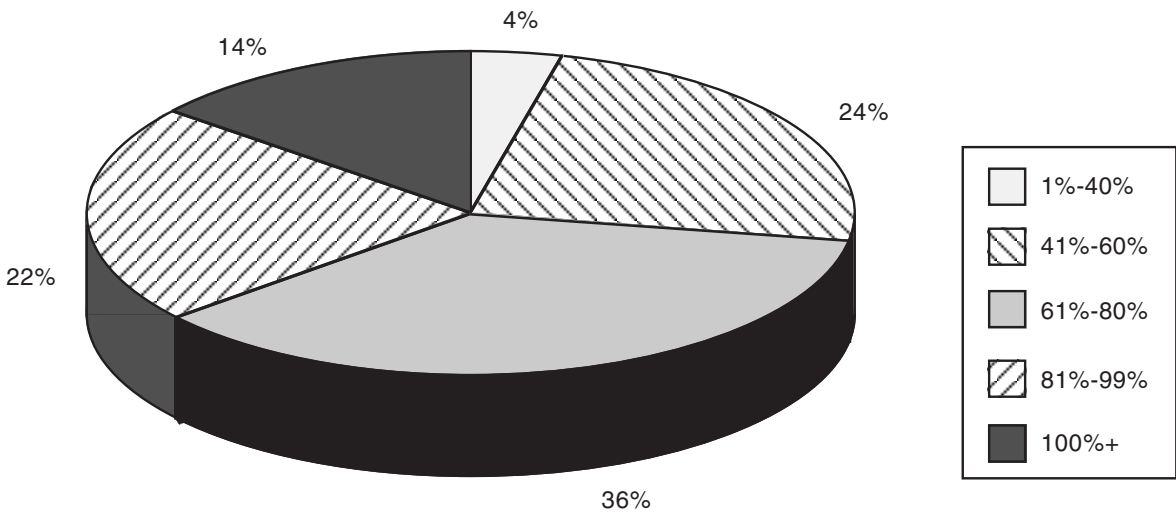
Source: 1991 Income & Expense Filings.  
\*Buildings without commercial units.

conditions. The longitudinal portion of this study also found an increase in the O&M to income ratio from .65 to .67, corroborating these figures.

The O&M to rent ratio for pre-war buildings is .79 compared to .75 in the two prior years. The ratio for Post '46 buildings is lower (.70), but also higher than in previous years.

Approximately 14% of all buildings had O&M to income ratios over 100% compared to about 10% in the past. Overwhelmingly, these are Pre '47 buildings. Only 6% of all buildings in the post-war stock have ratios over 100%.

Distribution of O&M to Gross Income Ratios



Source: 1991 Income & Expense Filings.

# LONGITUDINAL STUDY

## Sample and Methodology

Last year the RGB selected a sample of 500 rent stabilized buildings for its Income and Expense (I&E) Study. A cluster sampling scheme was used to insure that the sample included the appropriate mix of large and small buildings. The data was weighted to calculate monthly per UNIT figures for rent, income and O&M expenses.

A year later we have returned to this same sample of 500 buildings. As expected, some of the buildings have dropped out. Of the original 500 structures, 118 were “lost.” Approximately 80 owners filed an I&E statement last year but not this year. In addition, the assessors, who evaluated miscellaneous expenses this year using the same methods as last, were unable to locate I&E forms for about 30 buildings. We decided not to include these buildings in the sample. Finally, 8 owners reported no rental income. These too were eliminated from the sample.

It should be noted that the loss of buildings could conceivably bias the results of this study. For example, if economic conditions prompted some landlords who filed in 1989 not to file in 1990, the results might be skewed, if a certain type of landlord decided not to file. It does not appear that we have such a problem. The loss of buildings was quite evenly distributed among the boroughs and the average O&M expense computed this year for 382 buildings (\$368) is nearly identical to the figure calculated last year (\$370) for the entire sample of 500.

The assessors checked the I&E statements to make sure the forms were complete, to eliminate filings with missing

information, and to check the “miscellaneous” category. Miscellaneous expenses which properly belonged in other categories were reallocated. In some cases miscellaneous expenses were disallowed, for example, interest expenses and depreciation. The aggregate amount of disallowed expenses was quite small, amounting to less than \$500,000, or two-tenths of one percent of total expenses.<sup>3</sup>

As soon as the work of the assessors was complete, MIS staff at the Department of Finance put together three data files for the 382 properties filing I&E forms in both 1990 and 1991:

1. Last year's I&E data re-run without the 118 non-filing and missing properties.
2. Unadjusted data for the most recent I&E filings.
3. Adjusted data for the most recent I&E filings.

After the data was received from Finance, RGB staff checked it for accuracy and aggregated it to produce estimates of rent, income, and operating & maintenance costs.

## Rents

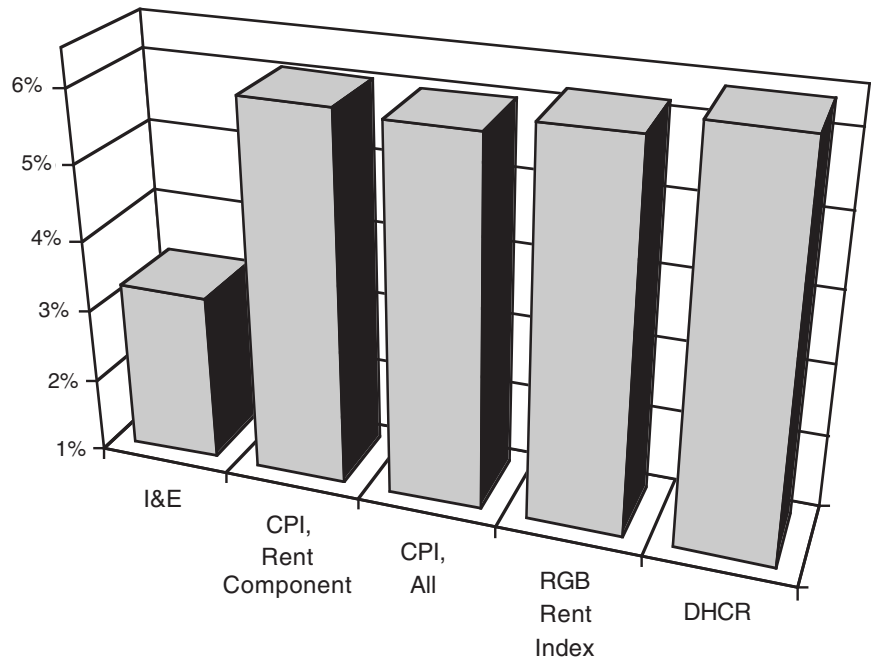
The average rent in our sample of 382 buildings (32,000 units) increased by 3.3% during the year between the I&E filings (roughly July 1989 to July 1990). Rents rose fastest in Queens (6.1%) and slowest in the Bronx (2.4%). The increases for Manhattan and Brooklyn were 2.7% and 4.1%, respectively. Rents in the Post '46 sector went up 3.8% while charges

<sup>3</sup> Approximately 15% of all miscellaneous expenses were deleted by the assessors. Of the remaining 85% of expenses, 30% was retained in the miscellaneous category and 55% was redistributed to other categories. Most of the redistributed expenses were placed in the maintenance and administration categories.

in older pre-war buildings rose only 3%.

The very small increase in rents collected by building owners contrasts vividly with the rent increases authorized by the RGB. The RGB "rent index" (formerly a part of "Table 14") predicted a 6.2% increase in rent for the period, based on the guidelines passed by the Board.<sup>4</sup> It appears that landlords were able to collect only about one-half of this amount. Reflecting the beginning of the current recession, the difference between the rent

### Changes in I&E Rent vs. DHCR, CPI, and RGB Rent Index



Sources: 1990 and 1991 Income & Expense Filings, U.S. Bureau of Labor Statistics, NYS Division of Housing & Community Renewal, and RGB Explanatory Statements #20 and #21.

<sup>4</sup> The RGB rent increase authorized by order #21, which largely covers the period under discussion, included a one-year lease renewal of 5.5% and a two-year renewal of 9%, a 12% vacancy allowance and a low rent supplement of \$5. Using a number of assumptions about lease renewals and the percentage of units which become vacant each year, the RGB rent index predicted a 6.2% increase in rents. This increase assumes, of course, that landlords raise rents by the maximum amount permitted. For more information see p. 72, note 1 of *Rent Stabilized Housing in New York City: A Summary of Rent Guidelines Board Research, 1989*. The staff calculations in the RGB rent index closely parallel legal registered rents filed with DHCR. The staff estimates contained in "Table 14" fall within 1% of actual changes in legal registered rent for every year from 1987 to 1991.

guidelines passed by the board and actual rent collections may be accounted for by increases in the rental vacancy rate, preferential rents, and additional rent collection losses.

During the period under consideration unemployment in the city increased from 5.3% to 7.2%. The increase in unemployment, and consequent softening of demand, probably affected all of the factors mentioned above. The increase in unemployment was greatest in the Bronx. It may not be a coincidence that this borough had the smallest increase in rent.

Data on registered rents was obtained from DHCR by the RGB to complement our I&E

findings. The average REGISTERED rent increased from about \$528 to \$562 during the time period under consideration, or 6.4%. The increase in the Consumer Price Index and the residential rent portion of the CPI were both up nearly 6%. In short, rent collections lagged behind all of the inflationary indicators. The fact that the residential rent portion of the Consumer Price Index increased nearly 6% seems to indicate that rents were increasing, but additional vacancies and/or collection losses limited landlords' rent gains.

The amount of income (i.e. apartment rent, sales of services, and commercial rent) collected by owners increased by 3.7%, only slightly more than the rate of increase in apartment rents. Once again, income in the Post '46 sector rose at a greater rate (4.4%) than in the Pre '47 stock (3.4%). Notably, the population which occupies pre-war buildings is generally less affluent than the occupants of post-war buildings. Thus any assertion that this drop in revenues primarily reflects the effects of the glut in the luxury end of the the market is not borne out by the evidence.

## O&M Costs

Overall operating and maintenance costs for our 382 buildings rose by 7.1%, compared to an increase in the Consumer Price Index of 6%. Expenses rose 7.7% in Manhattan and the Bronx, 7% in Brooklyn, but only 4.6% in Queens. Note that Queens is the only borough in which rents rose more than expenses (6.1% vs. 4.6%) while the Bronx had the widest discrepancy between rents and expenses (2.4% vs. 7.7%). In the four boroughs with a substantial number of rent stabilized units (i.e. excluding Staten Island), Queens renters are the wealthiest and renters in the Bronx the poorest.

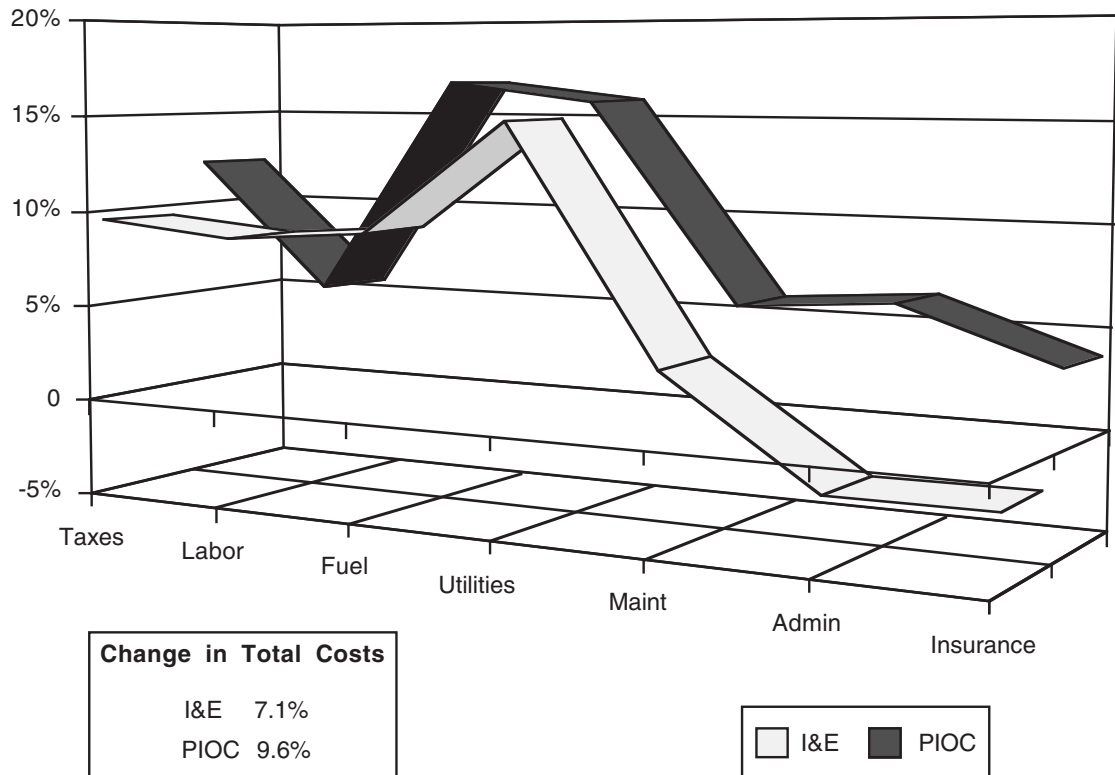
Among the various O&M components, utilities costs rose the most (15%), followed by taxes (9.5%) and fuel (9.4%). The smallest changes were registered for maintenance (3.6%), insurance (-1.4%) and administration (-1.5%). It may not be a coincidence that costs which are most easily reduced (e.g. administration and maintenance) rose the least while less discretionary costs (e.g. taxes, utilities, fuel) increased the most. Landlords may have been attempting to offset unavoidable increases in taxes and utilities with reductions elsewhere.

This line of argument is reinforced by looking at the Pre '47 and Post '46 segments separately. Although overall costs rose by about the same percent in both sectors (6.8% for post-war buildings and 7.3% for pre-war), increases in taxes and utilities in the Pre '47 buildings were greater (12.6% and 16.4% respectively, vs. 5.6% and 12.7% in the Post '46 stock). Perhaps as a result, administration costs in Pre '47 buildings were cut more (-1.7%) and maintenance expenses hardly increased (+1.7%).

It is impossible to make EXACT comparisons between changes in the I&E figures and cost increases measured by the PIOC. Many of the price index components are measured on an April-to-April basis while most landlords (although not all) file expense statements for the calendar year. There are also obvious dissimilarities in how the O&M components are measured. The PIOC, for the most part, uses proxies to measure actual cost changes while the I&E data consists of expenditures. Finally, the PIOC data is "lumpy." We know only the increase over the course of one year, but not changes or variations in the rate of increase throughout the year. Since we must combine two PIOC's to make a comparison with the I&E data, this "lumpiness" forces us to make somewhat simplistic assumptions.

Despite all of these disclaimers, it IS extremely useful to compare this I&E data with

### Comparison of the Percentage Change in O&M Costs: Price Index of Operating Costs vs. Longitudinal Income and Expense Study



Source: 1990 and 1991 Price Index; NYC Department of Finance, 1990 and 1991 Income and Expense Filings.

the PIOC. Looking at data from a single year may not tell us too much, given the inexact nature of the comparisons, but over the next three to five years we should find out a great deal about the accuracy of the PIOC.

The chart above shows changes in the PIOC and I&E cost components. The PIOC increase was 9.6% while expenses reported to Finance increased 7.1%. Given the standard error of the PIOC and the aforementioned difficulties in making direct comparisons between the PIOC and I&E data, one cannot say with any

degree of certainty that this difference is statistically significant.

As expected, the increases vary more by component. Even so, the similarities are greater than the differences (see chart). The three components with the fastest rate of increase in the PIOC (Taxes, utilities, and fuel) also show the greatest rate of increase in the I&E data. Similarly, three of the four components with the smallest increases in the PIOC (Insurance, Administration and Maintenance) were also low in the I&E (see chart above).

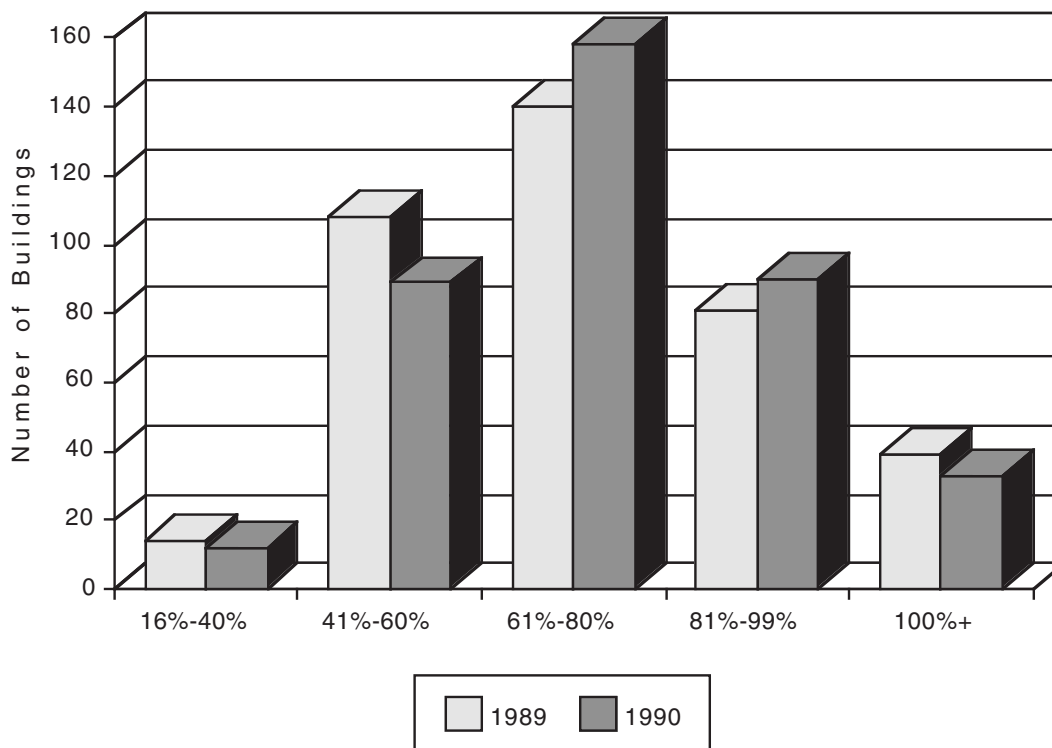
## O&M to Income Ratios

Given an increase in expenses of 7.1% and a mere 3.7% increase in income, one would expect the average O&M to income ratio to

increase. In fact, the proportion of income spent on O&M rose sharply, from 65% to 67%.

The number of buildings with an O&M to income ratio in excess of 100% declined slightly, from 39 to 34. However, the decrease is actually a statistical artifact, since the number of buildings with a ratio of 96% or more rose from 43 to 47. In short, conditions among the “worst off” buildings did not change much. The O&M to rent ratio worsened most among buildings which

**Distribution of O&M-to-Gross Income Ratios,  
Longitudinal Income and Expense Study**



Source: NYC Department of Finance, 1990 and 1991 Income & Expense Filings.



# INCOME AND EXPENSE AUDITS

## Sample Size and Selection

The specific purpose of this audit study was to gauge the accuracy of income and expense statements filed with the Department of Finance. These I&E statements have been used by the Board for the past three years to measure the operating cost profiles of rent stabilized buildings. It certainly would have been useful to audit all of the 500 buildings in last year's I&E sample so that we could adjust our estimates of rent and operating costs with some precision. However, the Department of Finance did not have the resources to undertake such an extensive project. A sample size of 50 was agreed upon as a compromise; it was sufficiently large to evaluate the soundness of the I&E data yet not impossibly burdensome and expensive for Finance.

The pool from which the sample of fifty buildings was drawn consisted of buildings from last year's I&E sample frame which registered with DHCR. Defining the sample in this way had some practical advantages. Constraining the sample to registered buildings allows us to compare registered (DHCR) rents with rental income reported to the Finance Department.

The sample size limitation made it impossible to use a complicated cluster sampling scheme as in prior studies. However, we did wish to make sure the sample included a representative mix of building types and sizes. Accordingly, a fairly simple cluster sampling strategy was devised (see box).

### Income and Expense Audit, Sample Size and Selection

Number of Buildings

|                   |    |
|-------------------|----|
| 11-19 units ..... | 15 |
| 20-99 units ..... | 25 |
| 100+ units .....  | 10 |
| TOTAL .....       | 50 |

A random selection was made within these parameters. The number of buildings in each category roughly mirrors the actual distribution of rent stabilized buildings.

The tax block and lot numbers of buildings selected for audits were transmitted to the Finance Department. RGB staff met with Finance personnel to discuss auditing procedures before the fieldwork began. After the audits had commenced, RGB staff looked at DHCR rent rolls for each of the buildings. In the course of scrutinizing the rent data it became apparent that one of the buildings in the sample was rent stabilized in name only. This building was eliminated from the sample and the RGB supplied Finance with two randomly selected replacements.

Five owners refused to cooperate with the auditors. Four of these buildings were in the 100+ category and one was in the mid-size (20-99 units) group. The refusals shrank our original fifty building sample to 46. The final sample included 15 small buildings, 24 medium-size buildings and only 7 large buildings.

It is difficult to say how the non-participation of large buildings affected the results of the study. As we will see, the auditors' operating cost reductions were much less extensive for large than for smaller buildings. However, large buildings also contain a relatively small portion

of the stabilized housing stock (less than 25%).

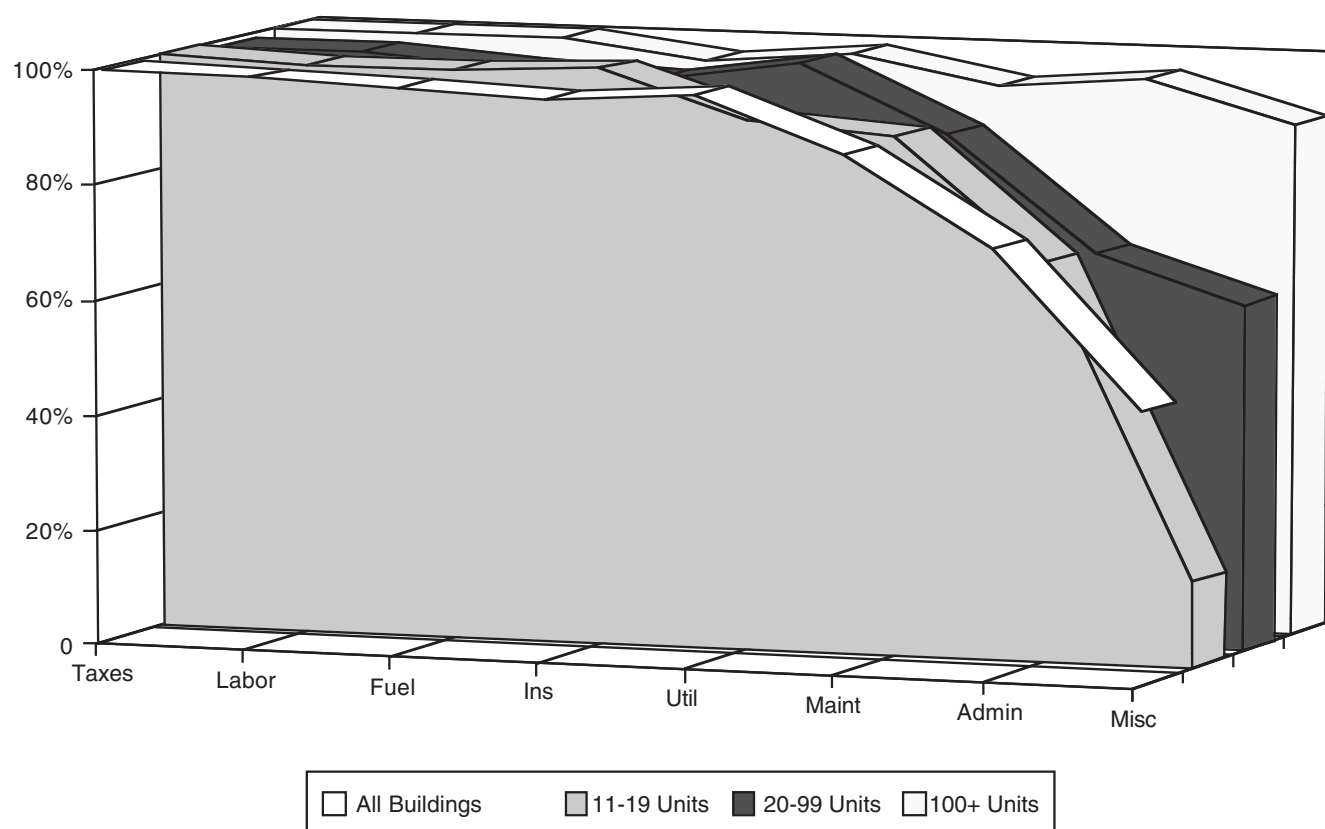
The auditors examined owners' 1990 Income and Expense filings, most of which contained calendar year 1989 information. Although the RGB would have preferred an audit of the 1991 I&E filings, logistical problems made this impractical. At the time the audits began, many of the 1991 filings were still being used "in the field" or were not yet filed at the Finance Department's borough offices. In any case, the 1990 filings were perfectly adequate for the purposes of this study, which was primarily to examine the reliability of the I&E statements, NOT to provide precise estimates of rent and operating costs.

## O&M Costs

In all of the I&E studies to date, we have "weighted" the data to reflect the proportion of rent stabilized UNITS in the housing stock. A simple weighting procedure is also used in this study. The three weights reflect the percentage of units accounted for by each of the building types: 11-19 units (12%), 20-99 units (65%) and 100+ units (23%). Mid-size buildings account for nearly two-thirds of all stabilized units and thus have by far the largest weight.

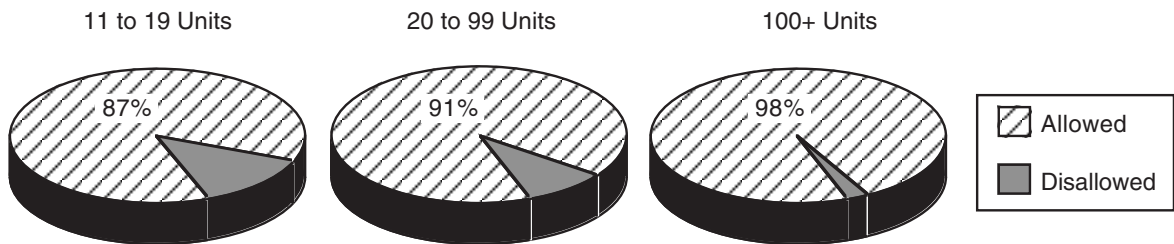
The chart on this page illustrates the adjustments made by the auditors. Overall

**Allowable Expenses by Building Size and O&M Category**  
(Unaudited Expenses Equal 100%)



Source: Audited Income and Expense Filings, NYC Department of Finance.

### Allowed Expenses as a Proportion of Reported Expenses by Building Size



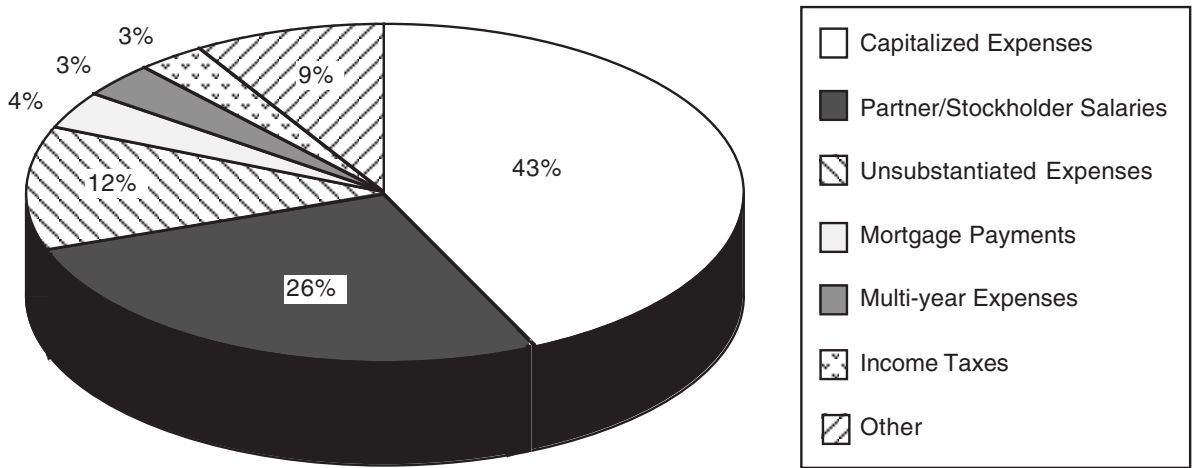
Source: Audited Income and Expense Filings, NYC Department of Finance.

Note: This chart is presented only to illustrate a possible link between building size and disallowed expenses. Due to the small sample sizes, no great degree of statistical confidence should be attached to these figures.

(weighted) O&M expenses were reduced about 8%. Many of the categories were scarcely affected by the auditors' detective work. Adjusted taxes, labor, fuel, utilities, and insurance are 97% or more of the unadjusted figures. The three categories which account for nearly all of the auditors' expense reduction are maintenance, administration, and the "miscellaneous" category.

The auditors provided the RGB with some additional detail on the types and amounts of expense reductions (see "pie" chart below). The largest category was "capitalized expenses;" it accounted for about 43% of all disallowed expenses. Salaries paid to partners or stockholders were also substantial, constituting 26% of the total.<sup>1</sup> Other categories documented

### Disallowed Expenses by Expense Type



Source: Audited Income and Expense Filings, NYC Department of Finance.

## Number and Proportion of Sample with Disallowed Expenses

|                                      | # of<br><u>Buildings</u> | % of All<br><u>Buildings</u> |
|--------------------------------------|--------------------------|------------------------------|
| Capitalized Expenses .....           | 24                       | 52%                          |
| Unsubstantiated Expenses .....       | 20                       | 43%                          |
| Partner or Stockholder Salaries..... | 11                       | 24%                          |
| Multi-year Expenses .....            | 3                        | 7%                           |
| Income Tax.....                      | 2                        | 4%                           |
| Mortgage Payments .....              | 1                        | 2%                           |

Source: Audited Income and Expense Filings.

by the auditors include unsubstantiated expenses (i.e. no supporting documentation was provided by the owner), mortgage payments, multi-year expenses (e.g. a three-year insurance policy which is expensed in a single year), and income taxes.

The table above shows the number and percentage of buildings with each type of expense reduction. The practice of including capital expenses in O&M was quite widespread; over half of all the buildings in our sample expensed capital items. Unsubstantiated expenses (20 cases) and partner/stockholder salaries (11 cases) were the next most common types of expense reduction. The other kinds of disallowed expenses were relatively rare, occurring in only a few buildings.

The amount of expense disallowed by the auditors was inversely correlated with building size. Expenses were adjusted downward by only 2% for the largest buildings, 9% for mid-size

buildings and by 13% for the smallest structures. The effect of building size is particularly apparent in two of the expense categories, administration and miscellaneous expenses. Administration expenses were reduced by about 30% for the small and mid-size buildings, but only 4% in the large buildings. The miscellaneous category was adjusted downward by 85% for the smallest buildings but only 11% for the largest.

Lack of management skills may account for the large reduction in

administration expenses in smaller buildings. The very low level of disallowed expenses in the largest buildings may be due partly to superior record keeping. We know, for example, that unsubstantiated expenses were very low in the largest buildings. **Unfortunately, it is impossible to separate the effects of bookkeeping from the bias introduced into the sample by the refusal of five owners to cooperate with the auditors.** Disallowed expenses might have been much higher had the five non-cooperating buildings been audited. We can only conclude that the data from the largest buildings are inadequate to assess the accuracy of the I&E statements for this class.

## Income

In addition to reviewing expenses, the auditors also examined the amount of rent and income collected by landlords. Using the owners' rent rolls as a guide, the auditors made slight

<sup>1</sup> If these salaries were not disallowed the total reduction in expenses would be 6% rather than the 8% cited previously.

revisions, resulting in an upward adjustment in rents of approximately one-half percent. More substantial revisions were made in gross income, which includes rent from apartments, stores, and offices, as well as other sources of income. Gross income was elevated 1.1%.

Adjustments to income were greatest for the smallest (11-19 unit) buildings. Income was revised upward by about 4%; nearly half of the buildings had adjustments. Medium and large buildings were little changed, with revisions of .7% and .4% respectively.

With access to DHCR's rent registration records, RGB staff was able to cross check I&E rent data with 1990 registered rents. Staff entered the DHCR rent rolls into spreadsheets and summed all the rent information by building type. Several adjustments were made to make this information comparable with the I&E data.<sup>2</sup>

One would expect the adjusted DHCR rent data to exceed the adjusted amount on I&E forms, since the I&E figures include vacancy and collection losses and the DHCR data does not. In fact, this was the case. Dividing the adjusted DHCR rent by the adjusted I&E rent, we found the following differences by building size:

#### DHCR Rent as a Proportion of I&E Rent

|                  |      |
|------------------|------|
| 11-19 units..... | 124% |
| 20-99 units..... | 111% |
| 100+ units ..... | 114% |

In the case of the mid-size and large buildings the difference is not great. The excess of DHCR rent over I&E rent is 11 to 14%, a gap which can probably be closed by taking into

account vacancy and collection losses and slight discrepancies in apartment counts. It is harder to explain away the difference among the smaller buildings (nearly 25%) which persists even AFTER the adjustments made by the auditors.

The two most likely reasons for the large discrepancy in the small building category are 1) Apartments which are being used for commercial purposes and/or apartment rent mistakenly placed on the commercial income line of the I&E form and, 2) Cash rent and/or owner-occupied apartments not discovered by the auditors or reported on the I&E form.

## O&M to Rent Ratio

The unadjusted O&M to rent ratio for the fifty buildings is .68. Since this figure was computed using 1990 submissions, the appropriate figure for comparison is the .72 ratio computed for last year's I&E study. The difference between the two ratios is not surprising given the disparate sample sizes, weighting methods, and sample variation.

This year's estimate of the O&M to rent ratio was .75 based on 1991 submissions. If we assume that an audit of the 1991 I&E filings would have resulted in the same findings as in this study (all other things being equal), we can revise the O&M to rent ratio based on the adjustments made by the auditors. Doing so would result in an O&M to rent ratio of .69 (.71 if salaries to stockholders and partners are considered a legitimate expense). While we do not suggest that this is necessarily a precise estimate of the O&M to rent ratio, the audited data strongly suggest that the .75 figure from this year's I&E study is too high. ○

<sup>2</sup> The DHCR data was from 1990 while the I&E statements largely cover calendar 1989. To compensate for the temporal differences the DHCR rents were adjusted downward by the RGB rent index. In most cases landlords did not register all of the units in their buildings. To account for these missing units (i.e. to make the DHCR and I&E rent rolls comparable), staff assumed that the rents for unregistered units were equal to registered rents. These were added to the DHCR rent rolls.

---

# Mortgage Financing

Pursuant to section 26-510(b)(iii) of the Rent Stabilization Law, the Rent Guidelines Board is required to examine, among other things, the

## INTRODUCTION

c u r r e n t  
“costs and  
availability

of financing (including effective rates of interest)” prior to establishing annual guidelines. To fulfill this mandate the RGB staff undertakes this annual survey of lending institutions.

In recognition of the number of lending institutions leaving the multi-family market indicated by last year’s survey results, the survey pool has been modified to eliminate lenders who have not provided multi-family loans for several years. Additional financial institutions which advertised in newspaper and telephone directories as multi-family loan providers have been added to this year’s sample. As a result of these efforts, the survey was sent to 57 financial institutions (including 12 institutions not previously surveyed) as compared with 56 institutions in last year’s mortgage survey.

The questionnaire was revised this year to probe bankers on the performance of their multi-family loan programs. In addition to the usual questions on financing availability and lending criteria, financial institutions were asked to comment on the volume of multi-family applications, loan approval rates, and the change in loan approval rates. Moreover, banks were asked to quantify the proportion of non-performing loans and compare it to last year’s level.

## RGB MORTGAGE SURVEY

### Summary

The Federal Reserve Board's aggressive interest rate reductions in the past year had some positive impacts on the multi-family loan market. However, this year's survey results indicate that lenders are financing fewer multi-family properties and fewer owners are applying for loans. Since these two activities are interrelated, it is difficult to determine whose behavior is precursory. For instance, given the economic climate and soft real estate market, some lenders have suffered financial losses in their real estate and commercial loans already. They have become less willing to finance multi-family properties as well as other commercial properties. Concurrently, landlords may feel discouraged since it is much more likely that they will have to face a more thorough application process which is almost guaranteed to be followed by more stringent reporting requirements if the loan is approved. Moreover, the survey results show that the decrease in interest rates for 30-year conventional home mortgages in the past year is much more substantial than the decrease in the rate for multi-family loans.

### Response to the Survey

Unlike last year, federal regulatory intervention has not been as common (see charts), but many financial institutions have been forced to take painful measures such as dividend cuts, employee dismissals, increased fees and earlier recognition of losses to stay

afloat. These restructuring measures may have contributed to this year's low response rate. In fact, 15 of the surveys had to be remailed due to changes in personnel and/or corporate locations.

The 22 surveys which were returned this year represent a reduction of 13 from last year's survey (see charts). Six lenders did not complete the entire survey due to temporary or permanent suspension of their multi-family loan programs. The reasons cited by these lenders included internal reorganizations, changes in lending policies due to recent mergers, and the suspension of the Freddie Mac multi-family loan program.

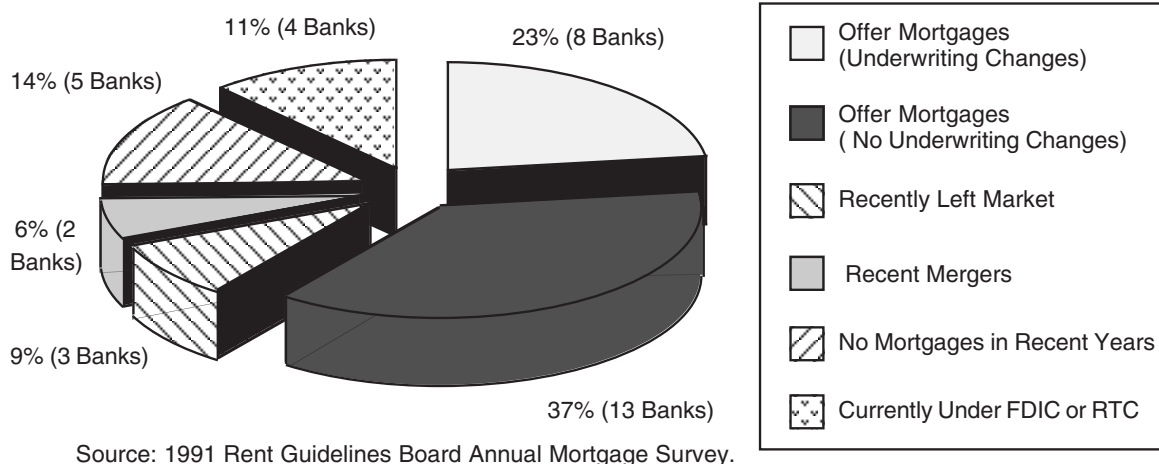
In 1991, there were 21 usable responses including 16 savings banks, two commercial banks, and three savings and loan associations. This year, there are only 16 usable responses. The respondents consist of eight savings banks, four commercial banks and four savings and loan associations. Thirteen of these respondents also completed the survey in 1991. They provide valuable information for point-to-point comparisons.

Since several lenders indicated that they could no longer issue multi-family loans because of the shut-down of Freddie Mac's multi-family operation, staff contacted Freddie Mac to inquire about its multi-family loan program. We were told that the shut-down is not permanent and Freddie Mac plans to re-enter the multi-family market pending the creation of a new loan program and a new refinancing program. However, no official date has been set to begin either of these programs.

The Freddie Mac multi-family loan program was first suspended in October 1990. During that month, Freddie Mac issued a letter to its shareholders regarding its third quarter performance and its multi-family portfolio. Since \$3.7 billion of its \$11 billion multi-family portfolio (largely in certain parts of the New York metropolitan area and the Southeast) were considered distressed assets, Freddie Mac



## 1991 Mortgage Survey Respondents



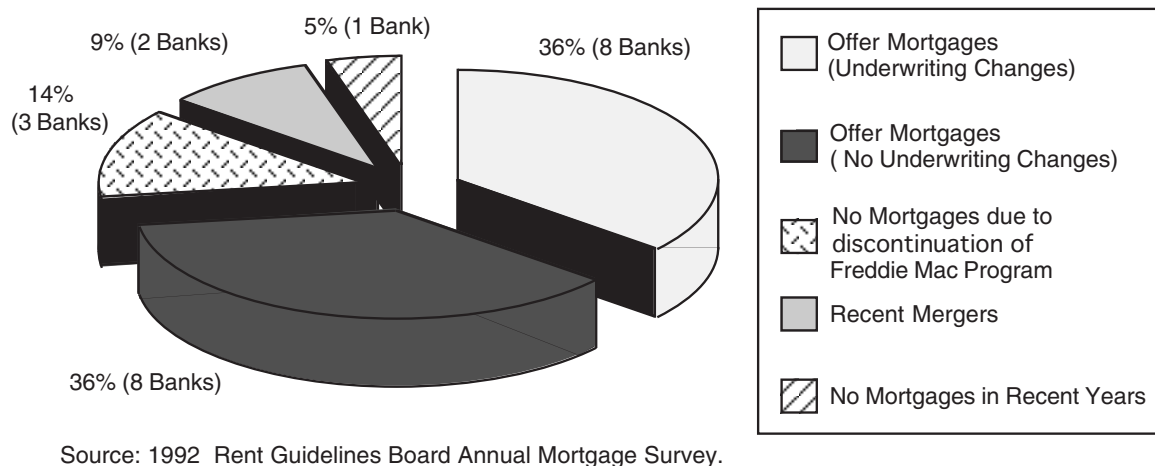
informed its shareholders that it would shut down its multi-family program and focus on minimizing its losses. Since October 1990, Freddie Mac has been conducting a property-by-property revaluation of these distressed properties as well as a loan-by-loan review of its performing portfolio. Moreover, it has accelerated its loan work-out program for

delinquent loans and potential foreclosures.

## Changes in Underwriting Practices

Last year, the average proportion of multi-family loans in the bank's portfolios was 44 percent, which also represents this year's average. However, the nine banks which

## 1992 Mortgage Survey Respondents



completed both years' surveys have reduced the proportion of their multi-family loan portfolio significantly. The average among these banks has declined from 56 percent to 36 percent.

Two questions in the survey dealt with the volume of multi-family loan applications and the proportion of application approvals. As for the volume of multi-family loan applications, 13 out of 16 banks which responded experienced either a decrease or no change in the volume of applications. Among the lenders who responded to the question on the volume of loan approvals, with one exception, all 15 banks responded that there was either no change or a decrease in loan approvals. Even though the Federal Reserve Board reduced its discount rate several times over the past year to stimulate the credit market, none of these lenders indicated a strong demand for multi-family loans.

The next portion of the survey dealt with specific changes in lending practices as well as the identification of the causes leading to these changes. Of the 16 banks which responded to these two questions, 50 percent (eight lenders) indicated that more stringent lending practices were implemented, and none relaxed lending standards. The most common changes involve the use of more stringent appraisals and the reduction of the loan-to-value ratio.

As for the causes leading to the changes in lending practices, eight of the 16 banks which still provide multi-family loans identified increased delinquencies and defaults by landlords as the primary reasons for changes in lending practices. Three of these eight banks stated that they became more conservative to accommodate the higher level of water and sewer charges. A number of lenders tied the causes to the recession and soft job market.

Lenders were also asked to comment on the level of non-performing loans and to identify causes for any increase. There are wide differences among the 13 lenders who identified

the proportion of non-performing loans. Although the average proportion is about 5 percent, some lenders cited a figure as high as 25 percent while others estimated it as low as 1 percent. Moreover, these differences were also reflected in the percent change over time. While the average increase in non-performing loans over January 1991 among these banks is 40 percent, some lenders reported an increase greater than 50 percent while others reported it as low as 1 percent. It appears that some banks' multi-family loan portfolios are more financially sound than others. Banks were once again asked to identify factors that contribute to the changing level of non-performing loans. Six of the 10 banks identified higher water and sewer charges as a factor for the increase.

Lenders were not asked how their institutions handled the increase in non-performing loans. However, a recent trend has been identified among large commercial banks indicating a greater willingness to initiate foreclosure proceedings because of heavy losses. According to an article in the *Wall Street Journal* in May 1991, many lenders' patient efforts to restructure real estate loans scarcely improved loan performance. As a result, large commercial banks such as Chase Manhattan, Citicorp and Chemical Bank have conducted some foreclosures and have become temporary building managers.<sup>1</sup>

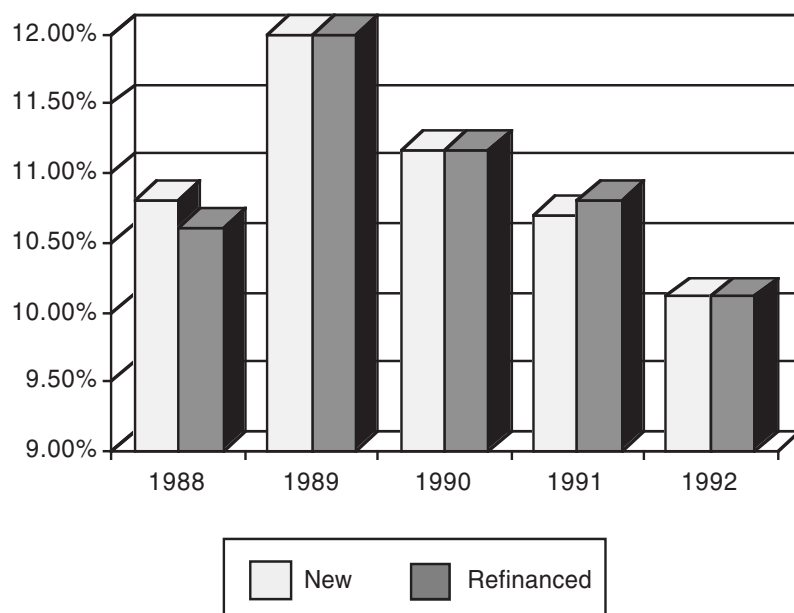
## Financial Availability and Terms

As in the previous survey, lenders were asked to provide information on interest rates, points charged, lending periods, types of loans, and any additional requirements for new

---

<sup>1</sup> Neil Barsky, "Lowering the Boom - Tired of Endless Talk With Big Developers, Banks Try Foreclosures," *Wall Street Journal*, May 8, 1991.

### Average Interest Rates for New and Refinanced Permanent Mortgages, 1988-1992



Source: Rent Guidelines Board Annual Mortgage Survey, 1988-92.

financing and refinancing of multi-family loans.

The average interest rate among this year's respondents reflects current market trends. Compared to last year, the interest rates for both new and refinanced mortgages fell about one-half percent (see chart), which continues a three-year downward trend in multi-family loan rates. Moreover, eight of the nine banks who responded to both surveys lowered their interest rates by at least half a point.

There is basically no change in points charged for multi-family loans. The average points charged was 1.37, which is slightly higher than 1.28 points in January 1991. Among the nine lenders who completed both years' survey, the points charged were identical at 1.31 points.

While the average loan duration

increased from 8.1 years in January 1991 to 10.2 years this year, the increase in the loan period may indicate lenders' willingness to provide greater flexibility rather than simply offering longer loan periods. In fact, two of the 13 banks which completed this section of the survey provided loans of 5 to 20 years and 5 to 25 years respectively. Nine of the 13 banks who responded to both years' surveys answered this portion of the survey. Their average loan duration increased from 8.8 to 10.3 years. Excluding three banks, the others stated the same loan period as in January 1991.

Comparing changes in interest rates for multi-family loans and 30-year conventional home mortgages in the past year, consumers of single family loans appeared to receive a greater benefit from the Federal Reserve Board's aggressive reduction of interest rates. According to data compiled by HSH Associates, a publisher of mortgage information, the average rate offered on 30-year conventional home mortgages in the New York area dropped by 15 percent (from 9.9 percent to 8.4 percent) from mid-January 1991 to mid-January 1992.<sup>2</sup> The record low conventional mortgage rates of this past January reflected the

<sup>2</sup> "Mortgage Interest Rates," Real Estate Section, *New York Times*, January 19, 1992.

last major interest-rate reduction by the Federal Reserve Board in December 1991. The multi-family loan market has not been as responsive, since rates fell from 10.7 percent to 10.1 percent.

There are mixed views among housing experts and economists on whether interest rates will continue to fall, but they all seem to agree that the stability of interest rates is tied to the speed and strength of an economic recovery. Alan Greenspan, chairman of the Federal Reserve Board, is among those economists who hold a more optimistic view on the national economy. Appearing before the Senate Banking Committee on February 26, 1992, Mr. Greenspan insisted that there will be definite signs of economic recovery within weeks, while admitting that there is no compelling evidence that the economy has

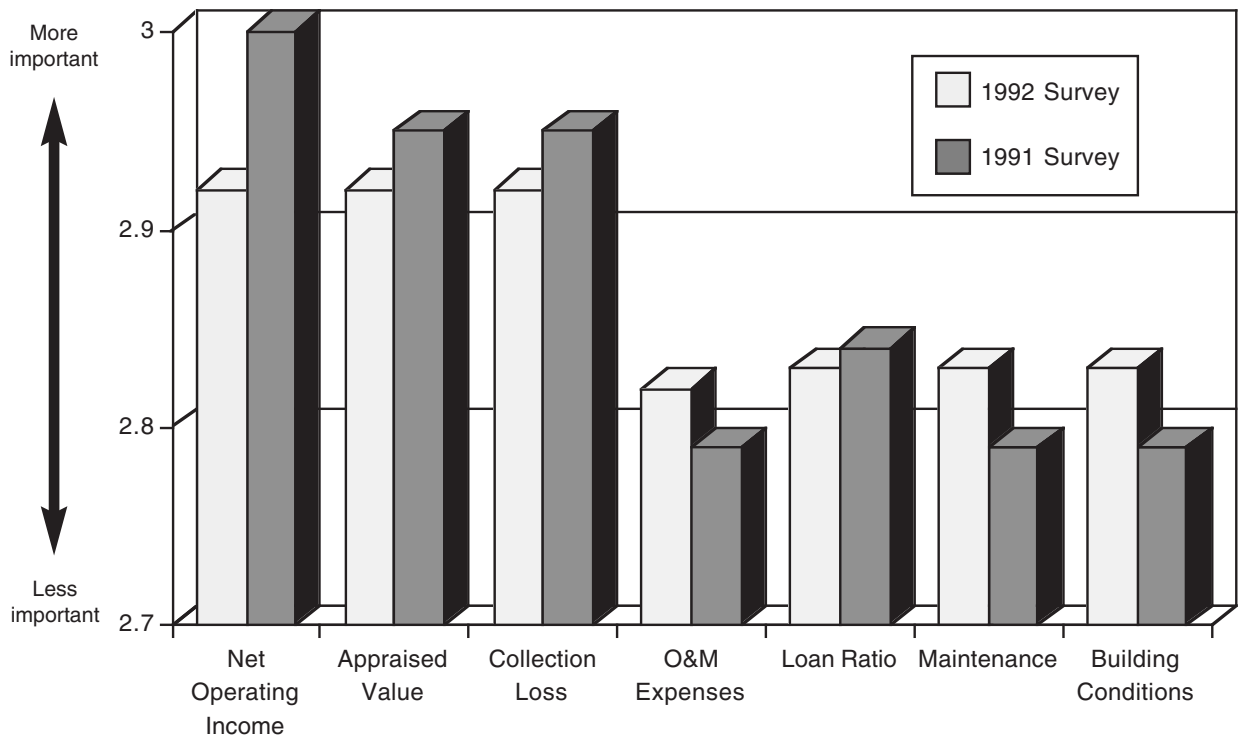
actually bottomed out. Furthermore, Mr. Greenspan did not rule out the possibility of another round of rate reductions.<sup>3</sup>

## Lending Criteria

The responses to this portion of the survey have been very consistent over time. In 1992, lenders showed slightly greater interest in bottomline monetary and physical indicators such as the O&M ratio, building maintenance, and building conditions, although the main emphasis is still placed on net operating income, appraised

<sup>3</sup> Wartzman, Rick, "Greenspan Expects Good Economic Data in 'Weeks,' Hints at Rate Cut Otherwise," *Wall Street Journal*, February 26, 1992.

### Comparison of Lending Criteria



Source: Rent Guidelines Board Annual Mortgage Surveys, 1991-92.

Note: Higher scores indicate lenders attach more importance to the criteria.

---

# The Vacancy Allowance

The broad legislative goal of the Rent Stabilization system is the establishment of “fair” rent levels. Fairness, of course, is a normative matter which is open to

## INTRODUCTION

interpretation. Given the overall legal framework supporting the establishment of rent guidelines the term appears to connote a process which attempts to balance three objectives: One objective is the establishment of rent levels which are generally humane<sup>1</sup> - in the sense that owners are not permitted to fully exploit demand for housing accommodations driven by situational scarcity. A related objective is setting rents which reasonably support the reliance and expectation interests of good faith (non-speculative) investors. While the Board cannot guarantee a profit for every owner, the Board should attempt to preserve the kind of returns that a competitive market with a vacancy rate in excess of 5% might generate - given all the various and changing factors of supply and demand such as tenant incomes and costs of operation. Finally, fairness requires that the overall rent burden be allocated among tenants in an even handed way - or that differentials in rent adjustments among similarly situated tenants bear some reasonable relationship to legitimate public policy.<sup>2</sup>

The goal of fairness serves both a limiting and a supportive function when it comes to vacancy allowances. Preservation of “humane” rent levels takes on a different meaning when it comes to newcomers. Vacancy allowances

cannot force someone out of an established residence. Yet, high vacancy allowances in periods of scarcity may allow for excessive demand driven increases. Then too, market pressures change and demand patterns in submarkets may vary. Thus, in periods (or in submarkets) with more modest demand the capacity to exploit the shortage will diminish. In much of the present market it is clear that the ability to exploit excessive demand through vacancy allowances is less than it was before the recession.

Achievement of the second objective (attempting to honor reasonable investment backed expectations) rests upon whether the rental incomes of stabilized buildings are at or about where one might expect to find them in a competitive market. This requires some rather abstract and general speculation about the long term effects of changes in the local housing supply as well as in effective demand. The vacancy rate as of the last official count was 3.8%. Assuming that the 1.2% gap is closed with the sudden infusion of some 12,000 new units and that mobility within the rental market allows the establishment of a new competitive equilibrium, would landlords be better or worse

---

<sup>2</sup> It is important to note that while the policy goals described here may sound like legal standards, strictly speaking they are not. They are simply attempts to untangle and identify the key considerations incorporated in to the general notion of fair rents. While the discussion is informed by statutory and constitutional concepts, it is by no means an attempt to define legal parameters. The severity of the public emergency involved along with the nature and scope of public intervention varies with changing economic conditions and regulatory responses. The discretion afforded public authorities to respond is broad but not unlimited. With the exception of two state court decisions concerning Board procedures, no rent adjustment established by the Board in its twenty two year history has been found to be unlawful in any respect.

---

<sup>1</sup> Here the term “humane” is simply used to describe rent limits which effectively protect public health, safety and welfare.

off then they are in the present regulated environment? Certainly owners who have a number of units well below market might realize some gains, and owners without such units would lose ground to the tenant's new found bargaining power. But what about the typical owner? Unfortunately, the question is too abstract and speculative for the answer to command a broad consensus. It calls upon Board members to make an honest judgment after reflecting upon virtually all of the information presented about the current state of the industry. If rent stabilization has accomplished its broadest legislative goal, it will have generally neutralized the impact of the shortage on rent levels.

If past guidelines have satisfied the first two objectives (that is that they have generally been humane for tenants and reasonable for good faith investors) the relevance of these policy goals to the vacancy allowance issue is eliminated. Larger vacancy increases designed to "make up" for lost ground become as irrelevant as efforts designed to eliminate the allowance because of "excessive" past increases. Some members may argue that the Board has not accomplished one or the other of these objectives so that the expansion or elimination of the vacancy allowance may be an appropriate remedial tool.

The third objective - fairly allocating the rent burden - is less a matter of historical perspective. Here the question appears to be whether vacancy allowances over the long term unfairly benefit tenants in place at the expense of newcomers. The preservation of neighborhood and household stability along with recognition of the hardship imposed when households are forced to move may justify special protection for tenants in place. How much additional protection should long term tenants receive? Even though some rent skewing is inevitable, unusually high rents from frequent turnover or exceptionally low rents from long term tenancies

are equally at odds with general fairness.

## VACANCY ALLOWANCE STUDY

### History of the Vacancy Allowance

For most of its history the RGB has enacted some type of vacancy allowance in its orders (see Appendix G for a complete history of vacancy allowance provisions). During the past 23 years, only two orders have lacked provisions for rent increases on a vacancy (#6 and #14)<sup>3</sup>. Order six followed the brief experiment with vacancy decontrol (1971 to 1974) and was evidently a reaction against the effects of this policy. Order 14 came after a 15% vacancy allowance, the highest in the Board's history.

The type of vacancy allowance enacted by the RGB has varied somewhat over the years. During most of the 70's the allowance tended to be a simple 5% addition to the rent. In the early 80's (Order #12) the Board enacted its first "tiered" vacancy allowance - a 10% allowance was granted if no change in tenancy occurred since 1975, otherwise the increase was limited to 5%. The "tiered" approach was abandoned the following year but revived in an even more elaborate format in 1983 (Order #15).

Perhaps because the vacancy provisions of Order #15 were so complicated, the Board adopted a simpler version of the tiered approach in 1984.<sup>4</sup> Landlords were allowed a vacancy allowance if no vacancy increase was received the

<sup>3</sup> The Board's "orders" describe allowable rent increases, including lease renewal increases and vacancy increases. The "guideline period" is the one year period these increases are in effect.

<sup>4</sup> DHCR officials have objected to tiered Vacancy Allowances on the grounds that they are difficult to administer.

preceding year. This approach was used for orders 16 through 19. In 1988 (Order #20) the Board came full circle and returned to the policy of the 70's - a straight percentage increase that could be taken once during the guideline period.

Historically, the vacancy allowance has not necessarily been regarded as a means of accomplishing special policy objectives. Rather, the chief purpose seems to have been to raise additional revenue for landlords without imposing on existing tenants.<sup>5</sup> Consider, for example, the rationale for the vacancy allowance as stated in the explanatory statement for Order #7 in 1975:

"Tenants renewing leases will be receiving increases which already account for predictable cost increases. Asking them to pay an extra amount because of this cash flow problem could well be placing an unfair and difficult burden upon them. New tenants however know what an apartment will cost them when they rent it. Theoretically at least they can choose... An extra vacancy increase allowance may force them to choose a slightly less desirable apartment but it would not cause severe financial hardship. The Board decided therefore that the best way to deal with narrowing operating margins is the reinstitution of a special allowance

of 5% for vacancy leases."

The "explanation" for the vacancy allowance is almost apologetic. Vacancy leases were not viewed as accomplishing any specific public purpose, but simply as a means of raising revenues for landlords without unduly raising the rents of "tenants remaining in place."

Over the years the extra revenue generated by the vacancy allowance was targeted toward a number of purposes:

| <b>Order #</b> | <b>Stated Purpose for Vacancy Allowance</b> |
|----------------|---|
|----------------|---|

|              |  |
|--------------|--|
| 7.....(1975) | "... deal with narrowing operating margins..." |
|--------------|--|

|              |  |
|--------------|--|
| 12....(1980) | "... make up for the lack of total compensation on fuel... and to compensate owners for various cost factors..." |
|--------------|--|

|              |  |
|--------------|--|
| 13....(1981) | "... as a means of compensating for the drastic rise in mortgage financing costs... the decline of housing as a competitive investment, and the under-projection of operating cost increases in the last three years..." |
|--------------|--|

|              |   |
|--------------|---|
| 15....(1983) | "... to compensate for the ... eroding effect of inflation on the value of return on equity." |
|--------------|---|

|              |  |
|--------------|--|
| 17....(1985) | "The vacancy allowance was also intended to assist property owners in recouping the major costs of refurbishing individual apartments for new tenants, costs for which compensation may not be available through other means." |
|--------------|--|

|              |  |
|--------------|--|
| 19....(1987) | "... recouping the increase in the operating and maintenance expense to rent ratio..." |
|--------------|--|

In general, the explanatory statements offer few remarks other than those quoted here.

<sup>5</sup> While the Findings and Declaration of Emergency in the Rent Stabilization Law note the "special hardship to persons and families occupying rental housing" (NYC Administrative Code 26-501), protection of tenants in place is clearly not an exclusive legislative objective. The same law established a 5% vacancy allowance for two year leases and a 10% allowance for three year leases in the first year of rent stabilization. The law provides that thereafter, the "guidelines board shall determine what the rental for a vacancy shall be." (NYC Administrative Code 26-510(d)). Prior to the adoption of the Omnibus Housing Act of 1983, hotel owners were permitted, upon vacancy, to charge rents "At any price notwithstanding any permissible established rent level" [Former RSL 26-510(e)]. After 1983, hotel owners may charge new permanent tenants "the guideline level for vacancies established by the Rent Guidelines Board" [RSL 26-510(e), current].



They also contain little criticism of the vacancy allowance with the exception of a relatively lengthy statement in 1975 (Order #6):

“A vacancy bonus is a special increase allowance for an apartment rented by a new tenant... There is no present justification for... a vacancy bonus. Its purpose supposedly is to reimburse the owner for the costs of redecorating, advertising, and renting a vacant apartment. However, these costs are a part of normal maintenance and are considered as such by the Bureau of Labor Statistics... Because the costs of renting a vacant apartment are normal operating and maintenance costs, they should be borne by all the tenants in a building not just those newly renting a vacant apartment. The vacancy bonus granted in the past has resulted in unequal rents for similar apartments... Rent skewing is a major problem in the controlled stock and it would be a mistake for the Guidelines Board to encourage it in the stabilized stock.”

This excerpt contains a number of the most commonly used arguments for and against the vacancy allowance. In the next sections of this paper we will examine some of these arguments.

## Arguments For and Against the Vacancy Allowance

### *Rent “Skewing”*

One of the most commonly raised arguments against the vacancy allowance is that it encourages “rent skewing,” that is, different

rents for identical apartments. The argument goes something like this: If two identical apartments begin with the same rent but one becomes vacant after a number of years, the vacant apartment will reach a higher rent level with the vacancy allowance. Given this higher rent, the apartment which became vacant is more likely than the other apartment to become vacant once again and reach an even higher rent, thereby further widening the rent disparity between the two apartments. Eventually, a wide gap in rent for identical apartments is created as some tenants remain in place for long periods of time while others move in and out of apartments with higher rents.

This argument does have some appeal. However, it is a bit too simplistic. One of the implicit assumptions of this line of reasoning is that identical units in the private sector would rent for the same amount. In an Arthur D. Little report entitled *Housing Gridlock in New York* (1987), the authors examined rent levels in cities with and without rent regulation. They found that

“**In all** [emphasis added] cities, tenants benefit from staying in a rental unit for long periods of time. All other things being equal, rents decrease with each year of additional occupancy.”<sup>6</sup>

In short, some of the rent “skewing” which now exists in the regulated sector is likely to have predated the imposition of rent stabilization and would have continued in an unregulated market. However, most skewing is undoubtedly an undesirable byproduct of rent regulation. In a small scale study of the 50 buildings the RGB submitted to the Department of Finance for audits, we found that the average difference between the lowest rent apartment in

<sup>6</sup> *Housing Gridlock in New York*, Report to the Rent Stabilization Association of New York City, Inc., May 1987, page 2.

an apartment “line” and the highest rent apartment was 60%.<sup>7</sup> Although we have no comparable data for unregulated apartments, one would not expect the difference to be nearly as high.

Apart from the vacancy allowance, there are many other factors which also create rent skewing. The lease terms chosen by tenants, the vacant apartment improvement program, and the MCI program may all increase the rent differential between identical rent stabilized units to an equal or greater extent than the vacancy allowance. In *Rent Stabilized Housing in New York City: A Summary of Rent Guidelines Board Research, 1990*<sup>8</sup> it was shown that the differential between two tenants with identical rents of \$190 in September 1983 would increase to \$31.23 by 1989 if one tenant consistently chose a one year lease and another consistently chose a two year lease, or a difference of 10.6%. The individual apartment improvement program can create even greater disparities in rent. DHCR has estimated that the mean increase in apartment rent for units with improvements due to the individual apartment program in 1989 was 25.3%. By contrast, the vacancy allowance in that year was 12%.

It should not simply be assumed that a vacancy allowance skews rents. “Skewing” is, after all, a measure analogous to the standard deviation in statistics - that is, the extent to which values differ from the mean. As noted previously, rents for equivalent apartments tend to be lower for each additional year of occupancy. Since this is so, a vacancy allowance restricted to units which have been occupied for a substantial period of time could actually REDUCE the

amount of rent skewing by moving the rents for these units closer to the mean.

The effect of a vacancy allowance NOT restricted to units occupied for a lengthy period of time is ambiguous. On the one hand, the allowance would certainly move low rent units closer to the mean. However, if the vacancy allowance is taken more often on higher rent units, the net effect could be to skew rents further. The overall effect of an untargeted vacancy allowance is an empirical question which we cannot answer at this time.

As a postscript to this discussion it might be questioned whether the reduction or elimination of “skewing” is in fact an important public purpose. As previously noted, the practice is accepted in the private market. Some might argue that long-term residents should be rewarded with lower rents since they contribute to neighborhood stability and may save landlords the expense of vacancy improvements and collection losses. Finally, if a tenant chooses a two year lease rather than a one year lease, and realizes a long term benefit, the benefit is similar to that generated by foresighted tenants in the private market who subject themselves to an element of risk in choosing lease terms.<sup>9</sup>

The question of rent skewing is at least in part a rather backhanded way of examining who benefits most (or pays the least) given the current system of regulations. In the next section we will examine this question directly.

### *Who benefits from the vacancy allowance*

As noted earlier, the vacancy allowance

<sup>7</sup> The data was obtained from DHCR’s “on line” rent registration system. Only the 37 buildings with clear apartment “lines” (e.g. 1A, 2A, 3A) were used. Our assumption was that the apartments in the line were identical; in fact there may be some differences between apartments. The 60% figure cited in the text is the median difference. The mean is somewhat higher - 71%.

<sup>8</sup> See page 46.

<sup>9</sup> The one area where the vacancy allowance may unduly add to rent skewing is in apartments with frequent turnover due to a cycle of high rents or some other form of undesirability. Here the market will eventually cap the rents. This, however, may be an objectionable approach to some [see discussion of preferential rents].

was enacted largely to provide landlords with additional revenue, rather than to accomplish any targeted objective. Since this is the case, one might ask which renters benefit and which lose from the vacancy allowance policy. One might expect that recent movers would be the chief losers; they pay the higher rents associated with policies which allow rents to rise on vacancy.

There are two ways in which the “disbenefit” of being a recent mover can be measured. The first is to compare median stabilized contract rents for occupied units with asking rents for vacant units. As the table below shows, the rent “premium” associated with a vacant unit rose throughout most of the 80’s.

In 1981 a vacant stabilized unit rented for slightly less than an occupied unit. However, during the 80’s asking rents increased much faster than rents for tenants in occupancy. By 1987 the median asking rent for a vacant unit

was 19% over the median rent for occupied units in the Pre ‘47 stock and 30% more in the Post ‘46 stock. In short, the explosion of demand for housing in the 80’s meant that although rents for occupied units rose by the guideline amounts, increases for vacant units reflected the additional market pressures by rising substantially more.<sup>10</sup> Most likely, this reflects a rise in new luxury units and individual apartment improvement increases, along with the vacancy allowances permitted by the Board.

Looking at the issue from a somewhat different perspective, the 1987 Housing and Vacancy Report found that although the number of vacant for rent units increased between 1984 and 1987, the median asking rent rose approximately 43%, compared to a 22% increase for occupied units. The effect of these rent increases was borne by so-called “recent movers” - those who moved between 1984 and 1987. At that time, recent movers within the city paid a mean average contract rent of \$456 compared to \$350 for non-movers, a premium of 30%.

The 1987 Housing and Vacancy Report found that recent movers were slightly more affluent than city residents as a whole. A smaller proportion had incomes in the bottom two income deciles and a somewhat larger proportion had earnings in the upper fifth of the income distribution. The racial distribution of households was similar to the city’s.

The real difference between recent movers and non-moving households is in terms of age. Only 4.9% of recent movers were elderly, although these households represent about 21% of all households in New York City. All other household types, including single parents with children, were overrepresented in the recent mover group relative to the city’s population. While other types of increases (e.g. renewal

|   | <u>1981</u> | <u>1984</u> | <u>1987</u> |
|---|-------------|-------------|-------------|
| <b>Median Contract Rent for<br/>Rent Stabilized Units</b> |             |             |             |
| <b>Occupied units</b>                                     |             |             |             |
| Pre ‘47 .....   | \$223 ..... | \$276 ..... | \$345       |
| Post ‘46 .....  | \$325 ..... | \$385 ..... | \$450       |
| <b>Vacant units</b>                                       |             |             |             |
| Pre ‘47 .....   | \$218 ..... | \$304 ..... | \$412       |
| Post ‘46 .....  | \$309 ..... | \$406 ..... | \$584       |
| <b>Vacant rent as a percentage of occupied</b>            |             |             |             |
| Pre ‘47 .....   | 98% .....   | 110% .....  | 119%        |
| Post ‘46 .....  | 95% .....   | 105% .....  | 130%        |

Source: *Housing and Vacancy Survey, 1981-87*

<sup>10</sup> It would be interesting to see if the growth of preferential rents has moderated this gap. This comparison must await data from the 1991 Housing and Vacancy Survey.

leases, MCIs) are paid by all types of households, the brunt of the vacancy allowance largely falls on younger households. If one accepts the argument that the cost of renovating a vacant apartment should be borne by all renters, the vacancy allowance might be viewed as an unjust redistribution from the younger households to older households.

### *Tenant Mobility*

One of the most common arguments made against rent regulation is that it restricts tenant mobility. By creating “bargains” for many renters, housing is “overconsumed,” thereby reducing the vacancy rate. As a result, some tenants find no reason to move while others find appropriate housing hard to find. The mobility rate is reduced and tenants cannot necessarily find units suitable to their needs.

In *Housing Gridlock in New York*, the authors found that the turnover rate in New York was much lower than in other cities, including other cities with rent regulations. Specifically, they noted that

“Relatively few New York apartments ‘turn over’ from one household to another every year. Out of the total rental housing inventory of 1.9 million, about 200,000, or 11 percent, turn over annually. Relative to the size of their respective rental housing inventories, this is about one-third the number of units which turn over in Chicago and Los Angeles annually.”

The authors of the report surmise that rent regulations are responsible for most of the difference in mobility rates. However, in comparing different cities it is not easy to isolate the impact of rent regulations. A host of other factors also influence turnover, including tenure (i.e. the percent of households which rent), the

average age of household heads, the amount of new construction, employment opportunities, and other peculiarities of the individual housing market. It is likely that rent regulation accounts for some, but certainly not all, of the differences between cities.

In cities with rent regulations and market rents on vacancy or high vacancy allowances (e.g. Los Angeles) the mobility rate is quite high. In general, one would expect mobility in the rental market as a whole to increase as the percentage of units approaching market rates increases. In areas with long established regulations, such as New York, a high vacancy allowance policy might increase mobility within the rental market as a whole (i.e. the market including unregulated units) but could actually decrease mobility within the stabilized sector if rents within this sector become more “skewed.” In any case, the level of mobility is probably determined more by the overall rent level than by the vacancy allowance in particular.

Tenant mobility is, of course, only one concern of policymakers. The benefits of greater mobility must be weighed against other objectives, such as establishing fair rents, evaluating the impact of the allowance on different socioeconomic groups, and considering some of the possible benefits of LESS mobility (e.g. stability of neighborhoods).

### *The Revenue Impacts of the Vacancy Allowance*

The impact of the vacancy allowance on owners’ income depends on the following factors: 1) The level of the vacancy allowance, 2) The turnover rate, 3) The types of units which turn over, and 4) The collectibility of the allowance. Over the years staff has attempted to measure the impact of the allowance as a subcomponent of the RGB rent index.<sup>11</sup> In these computations

## Financial Impact of the Vacancy Allowance, 1985-1992

| <u>Allowance</u> | <u>Period</u> | <u>Aggregate<br/>Rent Increase</u> | <u>% Guideline Inc. due<br/>to Vac. Allowance</u> |
|------------------|---------------|------------------------------------|---|
| 7.5% .....       | 85/86 .....   | 0.77% .....                        | 12%   |
| 7.5% .....       | 86/87 .....   | 0.79% .....                        | 13%   |
| 10% .....        | 87/88 .....   | 0.99% .....                        | 17%   |
| 12% .....        | 88/89 .....   | 0.86% .....                        | 13%   |
| 12% .....        | 89/90 .....   | 0.86% .....                        | 14%   |
| 5% .....         | 90/91 .....   | 0.36% .....                        | 9%  |
| 5% .....         | 91/92 .....   | 0.46% .....                        | 12%   |

Source: Rent Guideline Board orders, 1985 - 1992.

we considered only the level of the allowance and the average turnover rate. Information on the other factors (i.e. types of units and collectibility) was unavailable.

The table on this page illustrates the estimated revenue impacts of the allowance for the past seven years. The first two columns of the table show the amount of the vacancy allowance increase and the guideline period. The fourth column shows the percentage of the guideline increase which can be attributed to the vacancy allowance. For instance, in 1991/92 the 5% vacancy allowance was projected to increase owners' aggregate rents by about one-half percent (.46%). Given that the guideline as a whole would raise landlord rental income by 3.93% (according to calculations from the RGB rent index), the proportion of the rent increase due to the vacancy allowance is 12% (third column of table). In short, about one-eighth of the additional rent authorized by the Board last

year was due to the vacancy allowance.<sup>12</sup>

The impact of the vacancy allowance has varied over the years, but not tremendously. The peak guideline year for the allowance was 1987/88. In this guideline the vacancy allowance boosted landlords' rents by nearly a full percentage point and constituted about one-sixth of increased revenue.

## Policy Options

In this study we have discussed five major impacts of the vacancy allowance. These impacts include "rent skewing" (different rents for identical apartments), the rent burden distribution (how much of the rent burden is shifted to recent movers who tend to be younger),

<sup>11</sup>The RGB rent index is a component of "Table 14" of the Board's explanatory statements. Table 14 also includes an operating and maintenance cost index. Historically, staff has compared the ratio of the rent index and the O&M index to arrive at an estimate of the O&M to rent ratio.

<sup>12</sup>The one-eighth figure is our best approximation, based on an average turnover rate and the average rent. In some cases the vacancy allowance may not be collectible, as in the case of very high rent units and units in low-income neighborhoods. In addition, if the vacancy allowance is collected more often on a particular type of unit, this may throw off the calculations somewhat. Note that some of the variation in the table is due to changing turnover rates rather than to changes in the level of the vacancy allowance.

owners finances (how much additional rent revenue the option would raise), mobility (whether the option would help expand the pool of available apartments) and administrative feasibility (the feasibility of equitably administering the regulations).

The plans which have the greatest impact on rent skewing in the long run are those which tie rent increases to other rents in the apartment building. These plans allow rents to converge toward the mean or the highest rent in the line. It must be noted, however, that in the short run a plan which allows rents to go to the highest in the line would probably increase skewing.

As we noted earlier, rents tend to decrease with each additional year of occupancy. As a result, units with very long term occupants have the lowest rents. If no vacancy allowance were in effect, the net impact over time would be to increase rent skewing since rent for units with multiple long term renters would diverge further and further from the average.

The effects of a vacancy allowance plan on the distribution of the rent burden depend primarily on the level of the vacancy allowance rather than how the plan is structured. Obviously, a plan which distributes the rent burden equally (i.e. through renewal increases) is most advantageous to younger, mobile renters. A high vacancy allowance or one which allows rents to rise to the highest level in the building is the least advantageous.

The impact on owner's finances is in some cases easy to evaluate (e.g. no vacancy allowance) and in some cases very difficult to judge (rent tied to highest in line). To evaluate the impact of alternatives based on the highest rent in the line staff would have to undertake some type of empirical study.

Mobility depends on the overall level of rents as well as the extent to which rents are skewed. A private market presumably encourages the highest level of mobility since

rents are at their maximum and competition discourages the skewing of rents. In a regulated market, given the general level of rents, mobility is greatly influenced by rent skewing. Thus, vacancy allowance policies which reduce skewing will also encourage mobility to a limited extent.

The administrative feasibility/enforceability of the allowance varies considerably depending on the alternative. No vacancy allowance, an allowance based on a fixed percentage, or an allowance based on a fixed amount are easily enforced AND easily understood by renters. An allowance which is tied to the highest rent in the line may be difficult to enforce. In addition, the alternative is also more difficult for tenants - information on other apartment rents is not as easily obtained as the past rent for a particular unit. Note that Westchester county's Vacancy Allowance is tied to "highest rents in the line" and requires notice of comparable rents to new tenants.

## Regulatory Responses to Preferential Rents

Compounding the issue of vacancy allowances is the matter of preferential rents - that is rents established by owners which are below the maximum rents allowed by law. This year the Board has received much testimony with regard to the growing presence of preferential rents. Clearly much of the "upper end" of the market no longer commands the additional increases authorized by the Board's vacancy allowances. If a vacancy allowance is largely uncollectible because of market conditions, what harm can it do to new tenants? What benefit will it provide to owners? Only in submarkets or in individual units where the allowance is collectible are the questions of fairly allocating the rent burden and improvement of building revenues



relevant - that is unless the market changes. While perhaps not a likely scenario, if the market tightens up in the next few years, the issue of whether owners will be permitted to fully recapture foregone vacancy and renewal increases will become critical. This brings us back to the question of how to deal with preferential rents - a matter perhaps as complex as the vacancy allowance itself.

There appears to be a split of legal opinion over how preferential rents will affect future rents once the preferred tenant has vacated. The Rent Stabilization Code explicitly permits owners to charge preferential rents. Once this is done the tenant receiving the lower rent is entitled to renewal leases subject to the RGB guideline increases (plus MCI, new appliance or other administrative increases). Section 2521.2(b) of the Code provides that when the benefitted tenant vacates:

... the legal regulated rent previously

established plus the most recent applicable guideline increases [plus administrative increases] may be charged a new tenant.

DHCR's interpretation of the Code is simply that only the vacancy allowance and renewal increase authorized by the most recent RGB order may be added to the legal maximum rent as it existed at the time of commencement of the preferential tenancy. Disputing DHCR's interpretation of the Code, Martin Heistein, Counsel to the Rent Stabilization Association, and Blaine Schwadel of Rosenberg & Estis have publicly taken the position that owners should be able to increase maximum legal rents by the full guideline amounts each time the unit is registered with the DHCR. While this has no effect on the tenant receiving the preferred rent, it would permit a substantial increase for any subsequent tenant. The example in the table of two alternative preferred rents illustrates the

### Alternative Preferred Rents

| <u>Date</u>   | <u>Preferred Rent I</u> | <u>Alt. Preferred Rent II</u> | <u>DHCR's view Legal M.R.</u> | <u>Schwadel view Legal M.R.</u> |
|---|-------------------------|-------------------------------|-------------------------------|---------------------------------|
| 11/1/84 (2 yr lease) .....                                | \$350 .....             | \$150 .....                   | \$400 .....                   | \$400 .....                     |
| 11/1/86 (2 yr lease) .....                                | \$381.50 .....          | \$173.50 .....                | \$400 .....                   | \$436 .....                     |
| 7/1/87 (6% MCI) .....                                     | \$404.39 .....          | \$183.91 .....                | \$424 .....                   | \$475.24 .....                  |
| 11/1/88 (2 yr lease) .....                                | \$440.79 .....          | \$205.46 .....                | \$424 .....                   | \$518.01 .....                  |
| 7/1/89 (1/40th*) .....                                    | \$450.79 .....          | \$215.46 .....                | \$434 .....                   | \$528.01 .....                  |
| 11/1/90 (1 yr lease) .....                                | <b>\$471.08**</b> ..... | <b>\$225.16**</b> .....       | \$434 .....                   | \$564.97 .....                  |
| <b>New Tenant, 11/1/91 (1 yr lease 4% + 5% vac) .....</b> |                         |                               | <b>\$473.01 .....</b>         | <b>\$615.82 .....</b>           |

\*assumes \$10 per month increase for new appliance.

\*\* rent charged and paid on 9/30/91



difference of approaches. The current DHCR rule would allow the owner to charge a new tenant \$473.01 no matter what the preferred rent had been. Notably, in the example given by alternative one, this permits a legal maximum rent only a few dollars above the preferred rent of \$471.08. The Heistein/Schwadel approach also disregards the amount of the preferred rent. They would permit a rent of \$615.82 - a complete restoration of the regulated status quo. This position appears to make sense in a tight market where the bulk of preferred tenancies result from "sweetheart deals" to employees, relatives etc... It is the rent that would probably have been charged if the preferred tenancy had not occurred. The logic of this approach is less clear, however, where preferred tenancies result from arms length deals in a loosening market.

Are legal rents above market "fair rents?" A case might be made that market rents which dip below legal maximums establish a new standard for fairness. If one adopts this view it appears that three different results may be justified - depending on the circumstances.

First, in a tight market where rents below legal maximums result only from sweetheart leases the Heistein/Schwadel approach appears most consistent with the purpose and policies which underlie the stabilization system. If an owner wants to give a break to a friend, relative or employee s/he should be free to do so without suffering the loss of future rent increases.

Second, in a looser market where rents below the legal maximums are established and tighter market conditions eventually follow, an increase based upon the rent charged and paid by the preceding tenant plus the most recent vacancy and renewal adjustments appears to make the most sense. This would conform to the other increases offered by the Board in that vacancy allowances and renewal adjustments are calculated from the rent charged and paid on

September 30th immediately preceding the guideline season.

Third, where the rents established by the second method are particularly low because of the exceptional case where a sweetheart lease was granted even when loose market conditions prevailed (e.g. a rent of \$150 when the market commanded \$400 and the RGB orders allowed \$450) some fair minimum is needed. By calculating RGB rent increases over the rent previously charged and paid the new tenant would gain an extraordinary and unintended windfall. Here it appears that the DHCR approach might be used to establish an absolute minimum.

If the market tightens and preferential tenancies are once again isolated to sweetheart lease situations consideration should be given to the establishment of the Heistein/Schwadel approach. The central point is simply that the nature of the market should determine the regulatory response to preferential rents.

Of course, if one believes that the full application of RGB orders are presumptively fair - even when they allow legal rents to rise above market - application of the Heistein/Schwadel approach in any market is logical.

The current DHCR approach takes what might be described as a middle ground which attempts to accommodate two very different situations: the sweetheart deal and the bargained for preferential rent.

Any initiative to develop a new approach to preferential rents would require consultations with DHCR. It is not clear that the RGB has authority to modify rent adjustments addressed by the Rent Stabilization Code. In any event, the issue deserves a full public airing before any change in course is recommended. The DHCR has considered revisiting the Code in the near future. We, therefore, advise against any assumption that the current treatment of preferential rents will remain unchanged. ○



# INCOME AND AFFORDABILITY REPORT

## Income and Job Growth

During the last decade of economic growth New York City grew as a center for sophisticated jobs, high employment and rising incomes. The 1990 Census showed that in 1989, the median household income was nearly \$30,000; a 26 percent (inflation adjusted) increase from 1979. The percentage change in the city's median household income was well above New York State average change in income for the same period.<sup>1</sup>

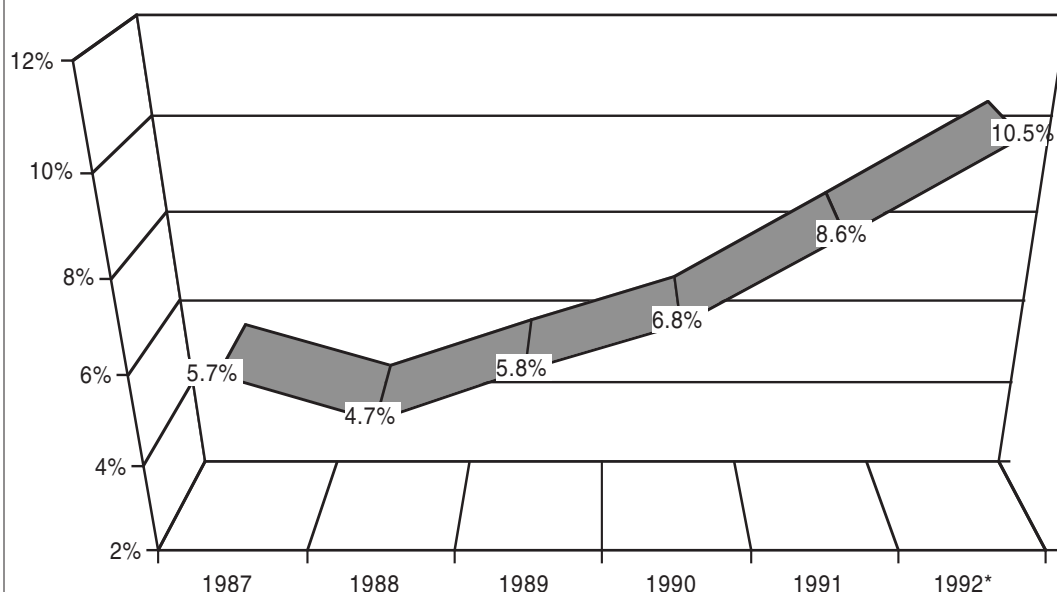
But the census was taken two years ago when most of the city's bad news was still to come. That is, the census caught the end of the economic boom and did not capture the weaknesses in the city's economy which have become apparent since 1989.

From 1987 to 1989 high employment in the service and government sectors sustained the city's economy. These two sectors added 56,000 jobs to their payroll, while 58,000 jobs were lost in the other sectors. As the recession took deeper hold, the government and service sectors could not maintain employment growth to compensate for the losses in other areas, and the city's employment slid downward. Hence, since 1989 job creation and earnings have deteriorated and the unemployment rate has risen.

As the graph shows, nonagricultural payroll employment declined substantially in the last two years. From December 1989 to December 1990 NYC lost more than 100,000

jobs. Total payroll employment worsened further in 1991. An additional 213,000 jobs were lost, particularly in the trade and service industries. Both of these sectors combined accounted for almost 50 percent

**New York City Average Unemployment Rate, 1987-1992**



Source: NYS Department of Labor.

\*The unemployment rate is an average of January, February and March 1992.

<sup>1</sup> An article in the New York Times on April 16, 1992, p. B4 published the following census data: The 1979 median household income, in 1989 dollars, in New York State was \$28,433 and the 1989 median income was \$32,965; a percentage change of 16 percent. In New York City the 1979 median income, in 1989 dollars, was \$23,663 and \$29,823 in 1989.

of the total job loss in that year.

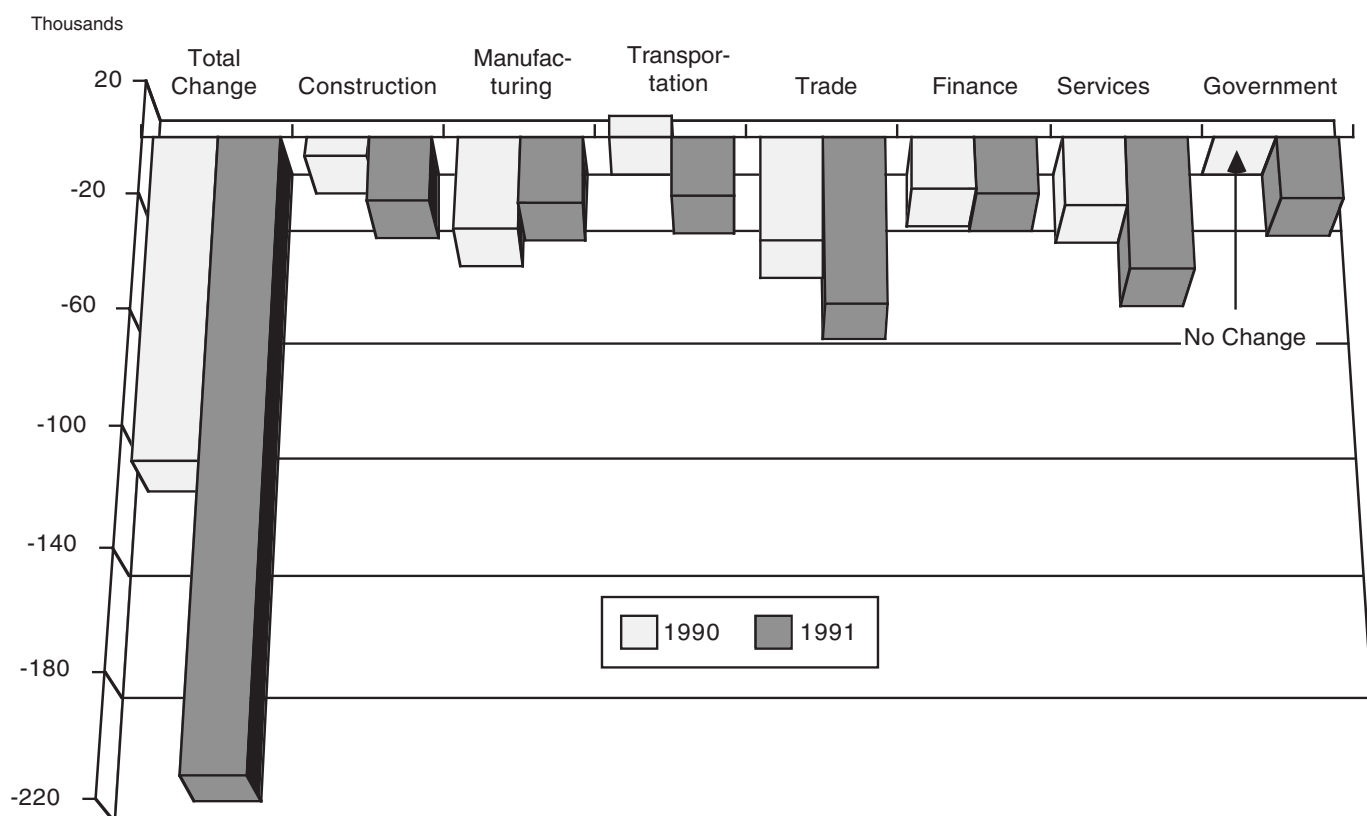
Unlike prior years, the public sector was unable to expand its payroll to compensate for the losses in the private sector. Last year, 10 percent of the employment lost was from the public sector. The inevitable net result of this worsening market was an increasing unemployment rate. The city's average unemployment rate in 1991 was 8.6 percent, the highest rate since 1984. Thus far 1992 has not shown any signs that the recession has eased its grip on the region's economy. For the first three months of 1992, the city's average unemployment rate was 10.5 percent.

Those who remain employed have also been hit by the recession. According to data

gathered by the U.S. Bureau of Economic Analysis, in 1988 the change in current and real per capita income for NYC residents was quite impressive, rising by 8.8 percent and 3.8 percent respectively. In 1989, however, real per capita income rose by only 1.5 percent.

Average gross earnings, as measured by the NYS Department of Labor for workers employed in NYC, increased 17 percent from 1986 to 1988. Real earnings for those two years was up 5.9 percent. In 1989 earnings no longer kept pace with inflation (-1.8%). The percentage change in earnings for those employed in NYC was negative, after adjustments for inflation. The most recent available data for 1990 showed a mere 0.3 percent increase in real earnings.

### Changes in NYC Payroll Employment by Industry, 1990 and 1991



Source: U.S. Bureau of Labor Statistics.

Note: The change in employment is computed as of December of the previous year.

## Rents

One byproduct of the 1980s economic prosperity was the rising cost of housing. The census data showed that median gross rent more than doubled from 1980 to 1990. Median rents were highest in Queens and Staten Island, and lowest in Bronx and Brooklyn. However, in terms of percentage increases the order was different. From 1980 to 1990 rents rose the most in Staten Island (123%) followed by Brooklyn and Queens (116%); the lowest increase in rent was in Manhattan (99%). (See chart).

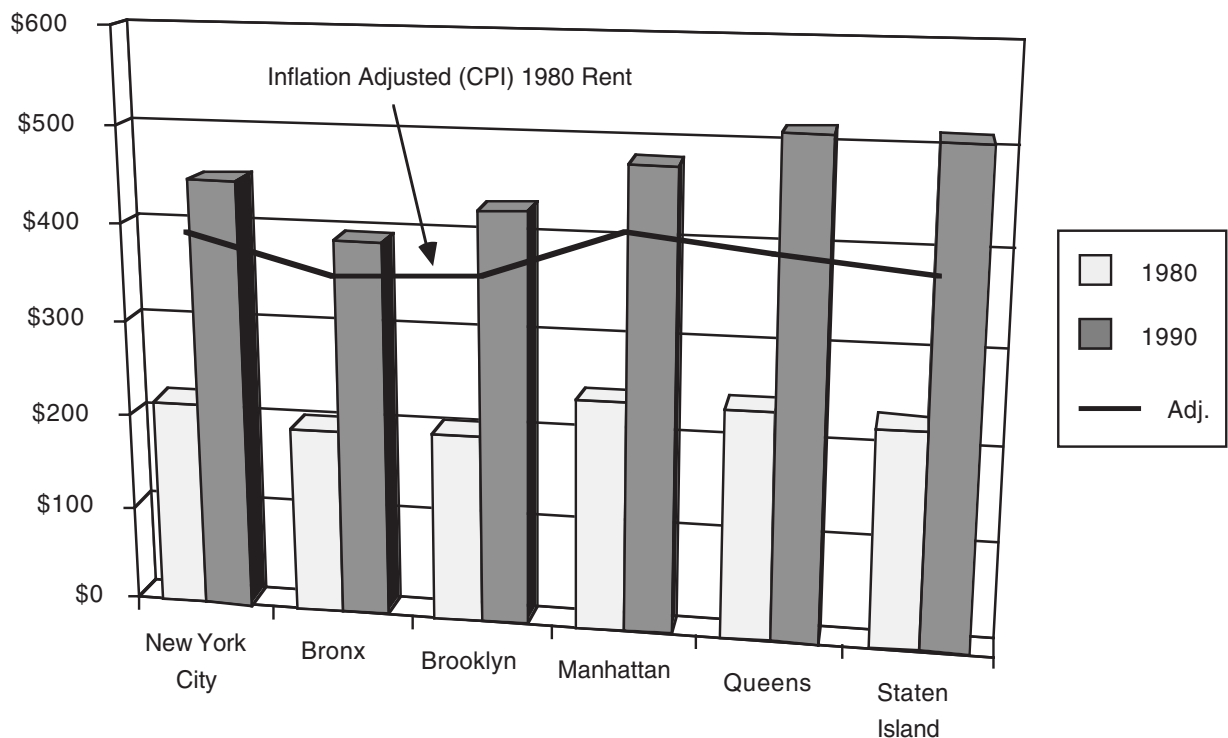
The increase in the Consumer Price Index from 1980 to 1990 was 68.7 percent, whereas the

PIOC increased 85.3 percent from April, 1980 to April, 1990. When adjusted by the CPI, rents in New York City grew 23 percent from 1980 to 1990. As a result, rents outpaced inflation.

As costs and rents increased, household income data showed a percentage change of 26 percent (in constant dollars) for the period of 1979 to 1989 according to the U.S. Census. Based on this estimate, it appears that on average income has grown proportionately with rent. Given the time period examined, however, these figures do not reflect the full effect of the present recession.

There was a substantial change in higher rent units. In 1980 only 4 percent of the respondents reported a rent of \$500 or higher.

**1980 and 1990 Median Contract Rent by Borough**



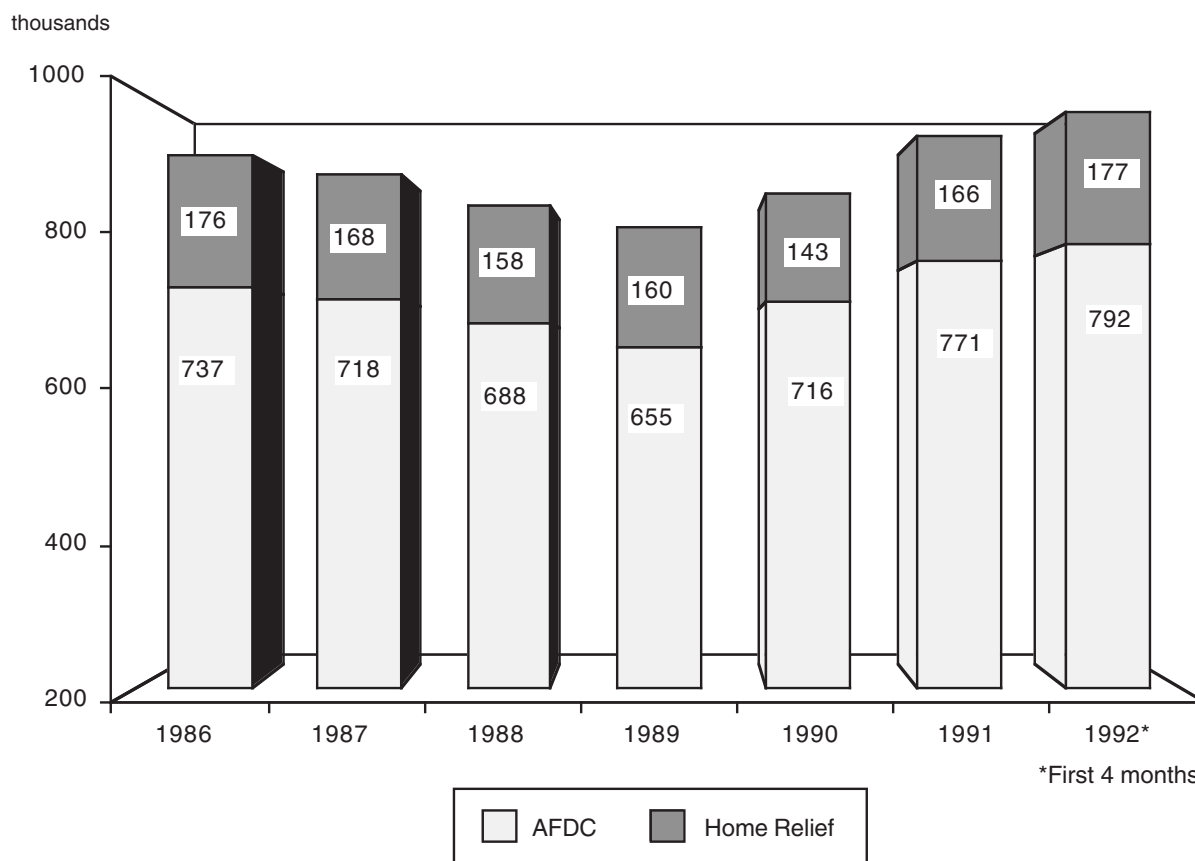
Source: NYC Department of City Planning, Population Division, U.S. Bureau of the Census.

However, in 1990 40.9 percent of the rental housing units in the city reported a contract rent of at least \$500. This is an increase of over 700 percent in ten years. The percentage changes for each of the boroughs were well over 1,000 percent, except for Manhattan whose percentage change was 224 percent. This is not unexpected, since 1980 reported rents in Manhattan were already somewhat higher than the other boroughs. Also, as previously discussed, median rents in Manhattan grew at a slower pace from 1980 to 1990. It appears that \$500 plus rents may no longer be regarded as unusually high.

## Public Assistance and Homelessness

There is little doubt that the rapidly expanding economy in the mid-80's drew people out of the city's welfare system. During fiscal years 1985 to 1988 persons receiving public assistance fell 9 percent while the unemployment rate dropped 40 percent. However, it took only three years for the city's economy to lose over 300,000 jobs and for the unemployment rate to skyrocket. During those three years recipients of

### Public Assistance Recipients - AFDC and Home Relief Grants, Fiscal Years 1986-1992



Source: *Mayor's Management Report*.

Note: The category AFDC also includes Predetermination Grant (PD-ADC) recipients.

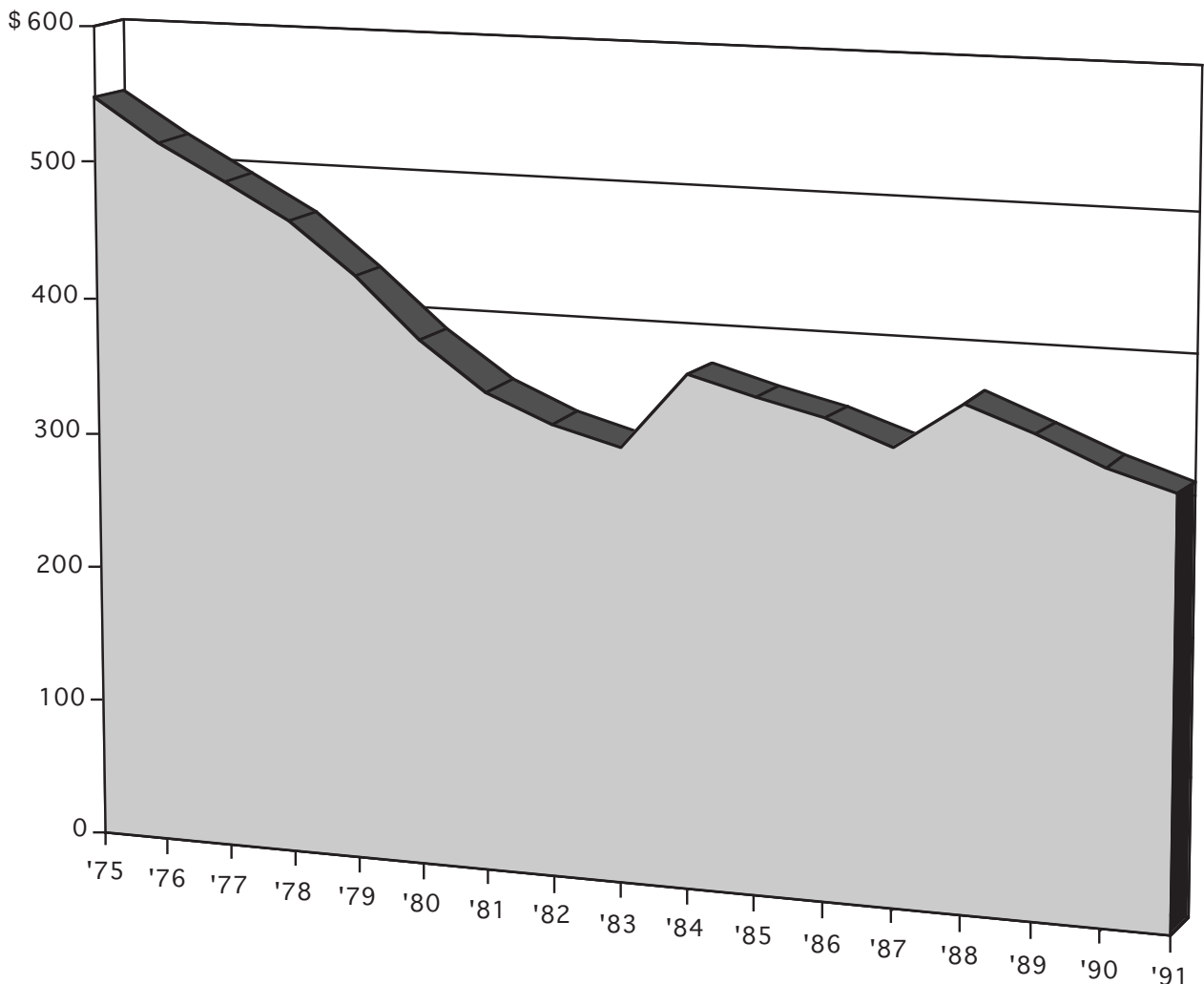
AFDC and Home Relief grants increased 15 percent. The forces of economic recession have brought low income households back into the public assistance sphere at a faster rate than they were taken out by economic prosperity.

For many of these households housing prices may be out of their reach. Using the example for a household size of four, the shelter allowance has not kept pace with inflation and

rising rents (see chart below). Since 1975 the shelter ceiling has been adjusted twice, in January 1984 and January 1988. The shelter allowance of \$312 for a family of four is 44 percent below the 1989 median rent reported by the Census Bureau.

Previous staff reports have noted the difficulty of estimating the homeless population. The Census Bureau did attempt to count the

### Shelter Allowance for a Four Person Household in Constant 1991 Dollars, 1975-1991



Source: HRA, Office of Policy and Program Development, and U.S. Bureau of Labor Statistics

Note: The current dollar value of the shelter allowance in 1975, 1984 and 1988 was \$218, \$270, and \$312 respectively.



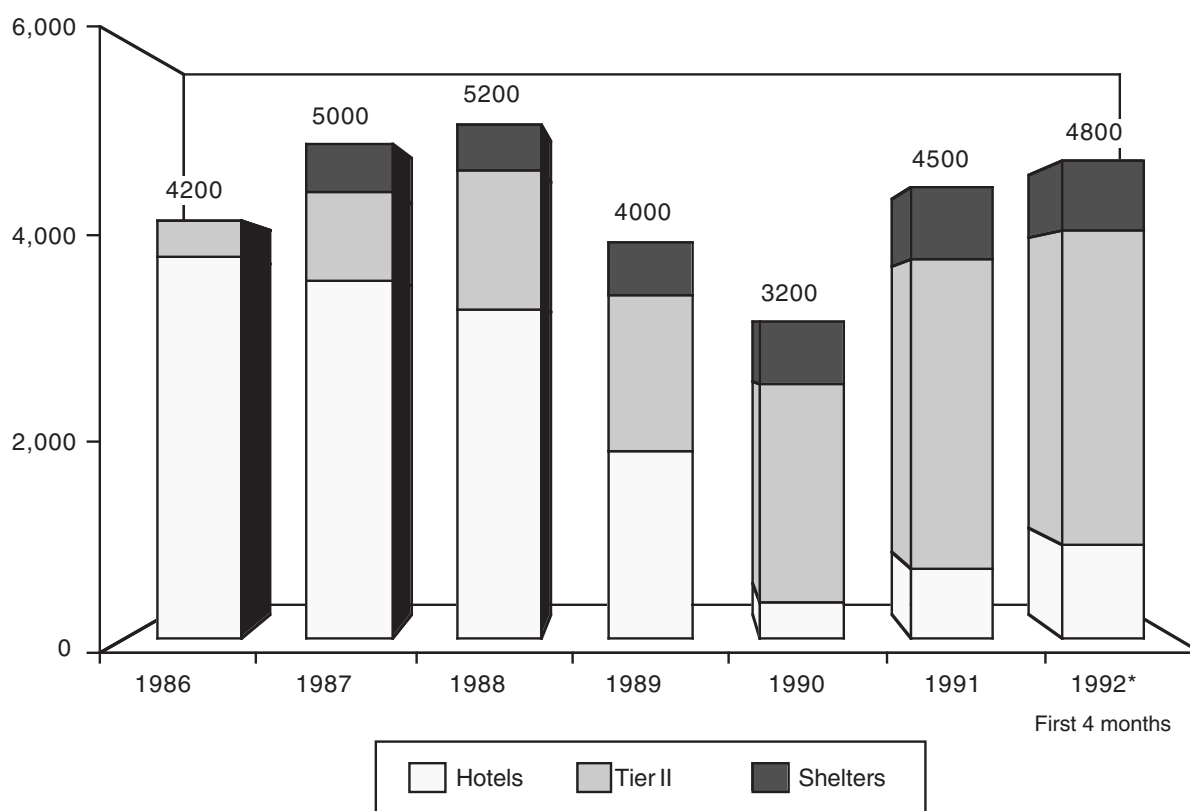
number of homeless people during the last census. Their effort may provide the best estimate. However, this data has not yet been made available. The information which is accessible reflects, for the most part, the desirability of lodging in city shelters and the city's ability and/or willingness to provide monetary assistance and permanent housing for those in shelters.

At the end of the decade, the city had been successful in reducing the number of homeless families in temporary housing. The

population of families dropped from over 5,200 in FY 1988 to 3,200 in FY 1990. But in FY 1991 homeless families seeking public shelter rose 42 percent. In the first four months of the current fiscal year, the city reported 4,800 families lodged in city shelters.

To a certain degree this data may reflect diminishing opportunities for affordable rental housing and the pressure of in-migration. According to data released from the 1990 Census on population and housing, 7 percent of all renter-occupied units were severely overcrowded

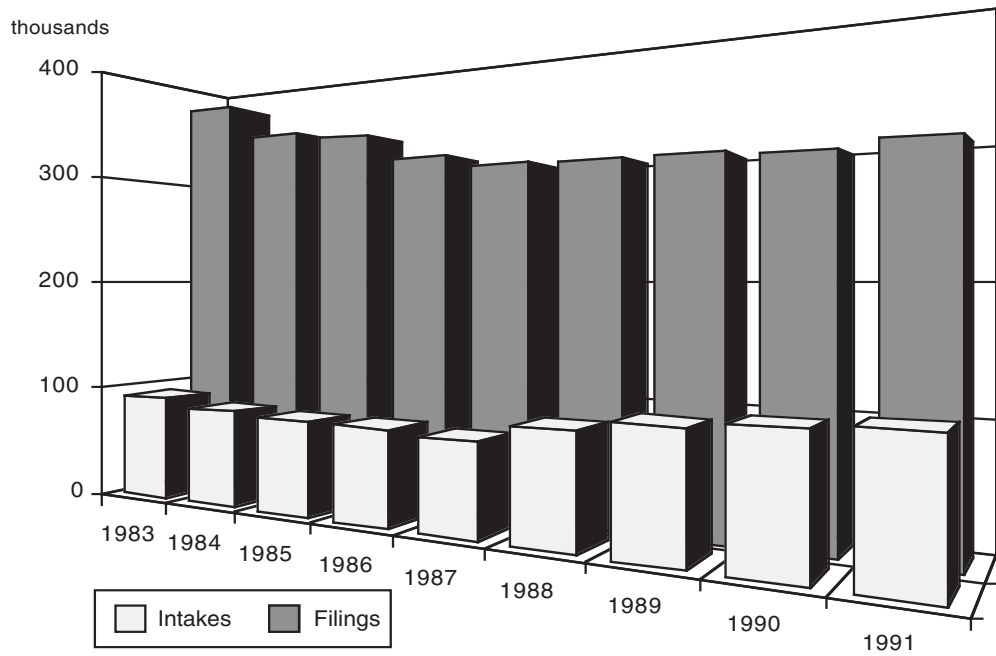
### Number of Families in Temporary Housing, Fiscal Years 1986-1992



Source: *Mayor's Management Report*.

Note: In FY '86, the number of families housed in public shelters were included in the hotel category.  
Numbers rounded to the nearest hundred.

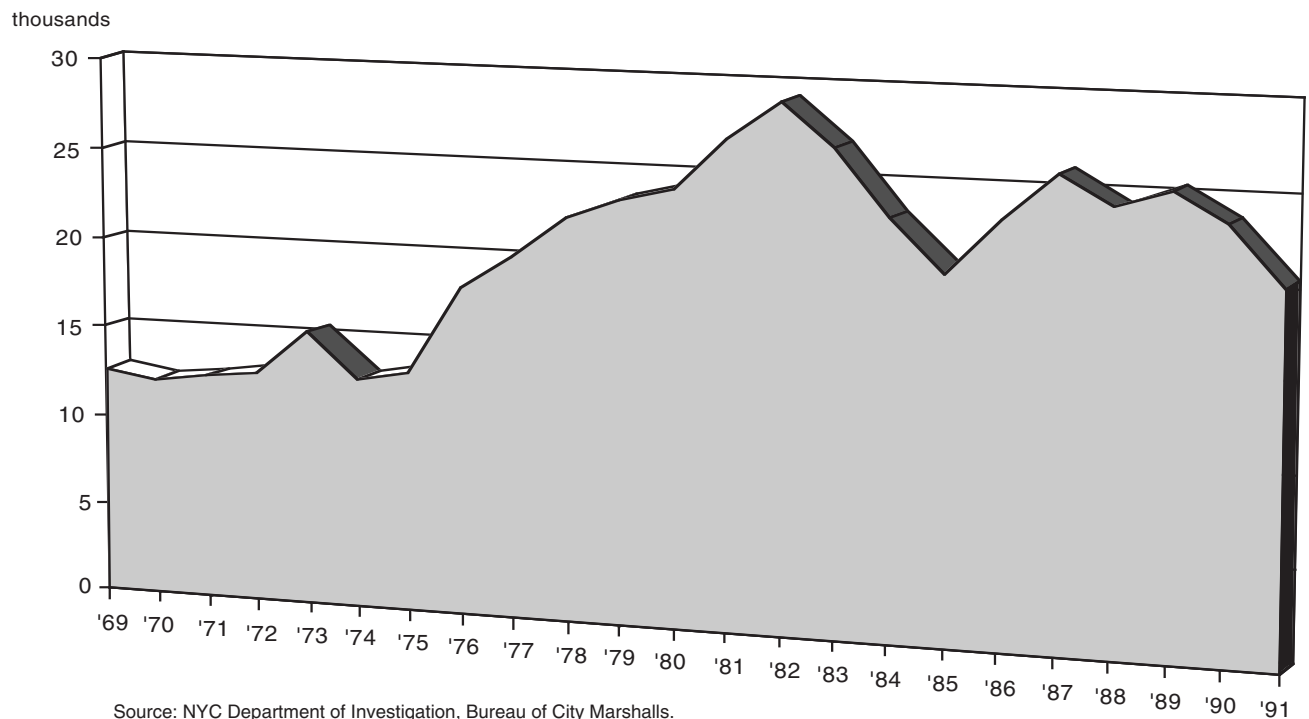
### Non-Payment Petition Filings and Case Intakes in NYC Housing Courts, 1983-1991



Source: New York City Civil Court.

Note: These figures do not reflect case restorations.

### Possessions and Evictions Performed by City Marshalls, 1969-1991



Source: NYC Department of Investigation, Bureau of City Marshalls.

in 1989.<sup>2</sup> This is more than double what was reported from the previous census.

## Housing Court Actions and Evictions

Long term trends in housing court actions and evictions reflect a variety of economic and institutional forces. Court proceedings are costly and time consuming. In a loosening market where the benefit of a vacancy is declining, the incentive for owners to work out resolutions with late paying tenants is heightened. At the same time, new housing opportunities for those who can afford them may reduce the number of tenants forced to hang on until an eviction is secured. Whatever the explanation, the effect of this recession on non-payment and eviction proceedings has not paralleled the sharp rise witnessed during the last recession.

Non-payment petitions have remained flat for several years, increasing only slightly to 302,000 in 1991 from 297,000 in 1990. The number of case intakes, reflecting non-payment actions added to the court calendar (less restorations), has been rising for the past 4 years, from a low of 77,000 in 1987, to 108,000 in 1991. We have no present explanation for this rise in the proportion of non-payment petitions which remain unresolved and end up on the housing court calendar. The number of evictions fell to 20,000 in 1991, from 24,000 in 1990.

---

<sup>2</sup> Crowding is defined as more than 1.01 persons per room; severe crowding is defined as more than 1.51 persons per room. The large increase in overcrowding may be partly an artifact of the immense pressure on the Census Bureau in 1990 to improve enumeration techniques.

# THE EFFECTS OF RENT REGULATION ON ECONOMIC AND RACIAL INTEGRATION

## Introduction

Although not a central objective of rent regulation, the possibility that economic and racial integration might be counted among its incidental benefits has been raised on occasion. Not all observers would agree - even if greater economic and racial integration could be achieved through rent regulation - that this social benefit would outweigh other benefits achieved through market allocation. Be that as it may, no direct study of the premise - that rent regulation actually promotes such integration - has been uncovered by staff research. Consequently, a survey of literature on neighborhood segregation along with an analysis of the racial and economic composition of New York City neighborhoods, comparing these with the density of rent stabilized households, has been undertaken. As will be shown, there is no statistical evidence of a relationship between rent regulation and economic or racial integration. At the same time, this report does not conclusively negate the possibility that, under some circumstances, rent regulation may promote or facilitate greater economic and racial integration.

The first portion of this study presents a brief survey of relevant research and summarizes two recent studies. It also includes a brief discussion of the applicability of these works to racial integration in New York City. In an effort to measure the impact of stabilization on the economic and ethnic diversity in New York City

neighborhoods, staff conducted three statistical analyses using the residential income and ethnicity data from the 1987 Housing and Vacancy Survey. These statistical results will be discussed in the second portion of the study.

## Selected Literature on Racial and Economic Integration

Much of the early sociological research on residential racial succession focused on different facets of neighborhood transformation in the presence of other ethnic groups. The early “invasion-succession” model which first appeared in sociological journals in the thirties assumed the process was driven by economic forces.<sup>1</sup> The withdrawal of an established homogeneous population that could afford better accommodations elsewhere provided the opportunity for relocation of some upwardly mobile minority families. However, since integrated neighborhoods were accepted only as unstable and transitional, long-term racial integration was not believed to be achievable.

More recent studies have challenged the accuracy of this “invasion-succession” model and the inevitability of residential racial succession. Based on their numerous studies of racial change in large cities over more than two decades, Peter Wood and Barrett Lee concluded that there is “a moderating trend in all regions of the country toward less inevitable succession and greater stability in mixed neighborhoods.”<sup>2</sup>

In place of the “invasion-succession” model, Wood and Lee suggested future research

in racial integration should be done on a “multilevel perspective, simultaneously evaluating a variety of demographic, economic, and institutional factors that might shape changes in neighborhood racial composition.”<sup>3</sup> These factors may include a city’s housing supply, housing age, manufacturing activity, and the presence of other races. Other contemporary sociologists called for examination of tract characteristics such as the percentage of Hispanic households, extent of crowding, and proximity to heavily minority areas.<sup>4</sup>

In a recent study of neighborhood racial integration, Douglas S. Massey and Andrew Gross of the University of Chicago concluded that neighborhood racial integration is most likely to occur in metropolitan areas with relatively small proportions of African-American households and relatively large proportions of post-1970 housing, which is tied to the passage of the Fair Housing Act in 1968.<sup>5</sup> The authors documented a strong statistically significant relationship between the proportion of post-1970 housing stock and the degree of neighborhood racial integration.

Based on 1970 and 1980 census data, Massey and Gross developed three basic racial segregation indicators to analyze changes in racial segregation. These indicators were, the degree of segregation, the preferred probability of inter-racial contact, and the proportion of African-Americans required to relocate to achieve an even racial residential distribution. Massey and Gross defined “even racial residential” distribution for neighborhoods as the same racial composition as the city as a whole.

According to Massey and Gross, the New York Metropolitan Area became slightly more

<sup>1</sup> Aldrich, Howard; “Ecological Succession in Racially Changing Neighborhoods - A Review of the Literature,” *Urban Affairs Quarterly*, Vol. 10, No. 3, March 1975.

<sup>2</sup> Wood, Peter B. and Lee, Barrett A., “Is Neighborhood Racial Succession Inevitable? - Forty Years of Evidence,” *Urban Affairs Quarterly*, vol. 26, No. 4, June 1991, p. 618.

<sup>3</sup> Wood and Lee, p. 618.

<sup>4</sup> Wood and Lee, p. 619.

<sup>5</sup> Massey, Douglas S., Gross, Andrew B., “Explaining Trends in Racial Segregation, 1970-1980,” *Urban Affairs Quarterly*, Vol. 27, No. 1, September 1991.

segregated between 1970 and 1980. Its segregation index grew from .81 to .82. Comparing New York to the other nine largest metropolitan areas, its segregation index ranks third after Chicago (.88) and Detroit (.87). The average for the ten largest metropolitan areas is .78. If rent regulations had an ameliorating effect on segregation one might have expected New York's segregation index to be below average.

Among the three largest metropolitan areas with rent regulations, New York is the most segregated, followed by Los Angeles, and Washington DC. Since the three metropolitan areas which still have rent regulations encompass areas outside of the rent regulated areas, it is difficult to speculate whether the presence of rent regulation has made any impact on racial integration.

Massey and Gross also calculated the proportion of African-Americans who would have to relocate to achieve an even ethnic residential distribution. On average, 43 percent of African-Americans would have to relocate to achieve an even racial distribution in the 60 major metropolitan areas. In major metropolitan areas where rent regulation still exists, the proportion was higher than average, Washington DC at 82 percent, New York at 75 percent, Los Angeles at 60 percent.

If Massey and Gross were asked to evaluate racial dynamics in New York City, they would probably describe it as segregated and immobile. Like many other older major metropolitan areas, demographics and the age of housing stock in New York City do not appear favorable for a significant level of racial integration.

While sociologists have not investigated the impact of rent regulation on residential racial integration per se, some of the variables they have used in their studies are housing-related. As we have noted previously, Massey and Gross place a great deal of emphasis on the beneficial effects of new construction. The impact of rent

regulation on levels of new construction has been much debated. Economic theorists argue that rent regulation depresses construction levels, and would thus presumably hinder integration. However, several studies have shown that rent regulation has no adverse effect on the level of new housing supply. The Rent Stabilization Division of the Los Angeles Community Development Department studied the impact of rent regulation on new rental construction in 1985 and concluded that rent regulation may only affect production of new rental housing during the initial period of its existence.<sup>6</sup> John I. Gilderbloom and Richard P. Appelbaum in "Rethinking Rental Housing" cited other studies that produced similar findings.

One of the well documented impacts of rent regulation is its effect on tenant mobility. Since regulations depress rents below market levels, tenants consume more housing than they otherwise might. This "overconsumption" of housing by regulated tenants produces two important effects - the vacancy rate is suppressed and many tenants find it undesirable to move, since their current accommodations are a "bargain." In short, the turnover rate is much reduced.

If we assume for a moment that the existing income and racial characteristics of neighborhoods are based to a large extent on long established patterns of segregation, rent regulations could actually retard trends toward racial and economic integration. The lack of mobility within the rental market might make it difficult for new immigrant groups to move into established neighborhoods. In addition, since landlords may have many applicants for each apartment, the tendency would presumably be for the landlord to choose prospective tenants with the highest income and/or with ethnic

<sup>6</sup> Gilderbloom, John I., Appelbaum, Richard, "Rethinking Rental Housing," Philadelphia: Temple University Press, p. 135.

characteristics most like the other tenants in the building.

Of course there is a flip side to this process. While rent regulations may make it difficult for newcomers to move into established neighborhoods, they may also retard the process of gentrification. The legal protections afforded lower income households otherwise faced with displacement through gentrification will slow neighborhood change.<sup>7</sup> It appears that this may have occurred in certain neighborhoods in New York during the 80's, for instance in the Lower East Side of Manhattan,<sup>8</sup> now the most integrated neighborhood in the City. Presumably, lower income households would have been forced out of this area in the absence of tenant protections.

Rent regulation may also encourage affluent households to remain in some neighborhoods. The traditional pattern of "invasion-succession" in which integration exists for only a brief moment and then disappears (to be replaced by resegregation) may be moderated to some extent by regulations. The benefits of regulation may promote stability by slowing down patterns of "white flight" which have afflicted many residential areas.

Thus, in theory, the combined willingness and legal power of both affluent and lower income households to retain the benefits of rent regulation in the face of gentrification and other neighborhood changes may lead to greater levels of economic and racial integration.

These assumptions now call for a closer examination.

---

<sup>7</sup> See "Reassessing Rent Control: Its Economic Impact In a Gentrifying Housing Market," *Harvard Law Review*, Vol. 101:1835, 1988.

<sup>8</sup> For a discussion of gentrification in the Lower East Side, see DeGiovanni, Frank, "Displacement Pressures in the Lower East Side," (Issued by Department of Research, Policy and Program Development, Community Service Society of New York, 1987).

## Measuring the Effect of Rent Stabilization on Racial/Income Integration

In an attempt to assess whether stabilization is associated with the economic and ethnic diversity in New York City neighborhoods, staff conducted three statistical analyses using the residential income and ethnicity data from the 1987 Housing and Vacancy Survey. The HVS contains income and ethnicity data for 54 sub-borough areas, whose boundaries are largely equivalent to community boards. With the exception of one sub-borough area in Staten Island, all the other 53 sub-borough areas have a certain portion of their rental stock classified as stabilized. Hence, this study used economic and ethnicity data for 53 sub-borough areas.

The variables used in this study were: the percentage of stabilized units in the neighborhood, the percentage of households whose incomes are below poverty or near poverty, the percent of households with incomes greater than \$25,000, the mean and median income of households of each sub-borough, and the percentage of White, Black, Puerto Rican, and Asian households. Moreover, an integration variable called "Absolute" was created to measure the degree of integration within each sub-borough area. This variable is the absolute value of the difference between the percentage of white renters and renters of other ethnic backgrounds. In other words, in a well-integrated neighborhood, the variable "Absolute" is very close to zero.<sup>9</sup> A score of zero would indicate that

---

<sup>9</sup> According to the 1987 *Housing and Vacancy Report*, whites represent half of all households in the city as a whole. Thus, if half of the households in any given sub-borough are white and the remaining half non-white, the degree of integration is perfect. In this case the value of the variable "Absolute" should be zero. As the absolute value of percent of white minus percent of non-white increases, so does the degree of segregation.

the racial and economic composition of the selected sub-borough area is the same as the overall citywide composition.

A number of different correlations were executed and none of the coefficients were statistically significant at the 90 percent confidence interval. More importantly, there is no statistically significant correlation between the percentage of stabilized units and the degree of integration as measured by the variable "Absolute." It should be noted that no adjustment was made to accommodate the great variation in the proportion of rental vs. owner occupied housing among the 53 sub-boroughs in New York City. This is an important distinction. For instance, while on average 85 percent of the residents in Manhattan sub-boroughs are classified as renters, the average percentage of renters in other boroughs runs from 80 percent in the Bronx to 39 percent in Staten Island. Since the object of the exercise is to detect the influence of rent regulation on racial and economic integration, isolating neighborhoods with large rental housing stocks provides for a more straightforward comparison.

In order to refine this analysis, a smaller sample of 37 sub-borough areas was selected by excluding the sub-borough areas with less than 65 percent renters. At the 90 percent confidence interval, seven of ten correlations were statistically significant, although the strength of the correlations was relatively weak.<sup>10</sup> None of these indicated a link between rent regulation and racial or economic integration. The

"strongest" correlations were between percentage of stabilized units and the size of household mean and median incomes respectively. The next "strong" correlation was between the percentage of stabilized units and percentage of households with incomes greater than \$25,000. Moreover, a positive but less pronounced correlation was found between the percentage of rent stabilized units and the percentage of white population. These results suggest that in areas with a relatively high proportion of stabilized units, it is more probable to find white households and households with high incomes relative to other renter households.

The other three significant correlations seem to corroborate the initial results. These correlation coefficients seem to suggest that the higher the percentage of stabilized units, the smaller the proportion of African-American households or renters whose household incomes are near or below poverty.

The correlation between the percentage of stabilized units and the variable "Absolute" was not statistically significant. If stabilization had a measurable effect on racial integration in these 37 sub-boroughs, there would have been a significant correlation between these two variables.

The second statistical study was intended to measure the association between the extent of stabilization in sub-boroughs and the variation in renter household incomes. The two variables in this correlation were the percentage of stabilized units, and ratio between the standard deviation of renter household incomes and mean renter household incomes. If stabilization had a measurable effect on economic integration, there would have been a positive association between these two variables. However, with the sample size of 53 sub-boroughs, the correlation was not statistically significant. Using the same variables, two correlations were executed for the five sub-boroughs with the highest proportion of stabilized units

<sup>10</sup> There is positive association ( $r=.35$ ) between the percentage of rent stabilized units and the percentage of white population. The percentage of rent stabilized units is negatively correlated ( $r=-.33$ ) with the percentage of black renters. There are positive correlations ( $r=.48$  and  $r=.47$ ) between the percentage of stabilized units and household mean and median incomes respectively. In addition, there is positive correlation ( $r=.37$ ) between the percentage of stabilized units and the percentage of households with incomes greater than \$25,000. Additionally, there are negative correlations between the percentage of stabilized units and percentage of households with income below and near poverty ( $r=-.41$ ,  $r=-.43$ ).



and the five sub-boroughs with the lowest proportion of stabilized units. Again, both correlations were not statistically significant.

The last statistical study used a different statistical method to evaluate the effects of stabilization on economic integration. A simple regression was formed between two income variables. The dependent variable is the percentage of renter households with incomes below \$7,700, which is the lowest citywide income quartile in 1987. The independent variable is a sub-borough's renter household mean income. By examining the relationship between these two variables we were able to estimate the proportion of renter households with incomes below \$7,700 one would expect to find in any given sub-borough. This was our predicted value. The predicted percentage of renter households whose income fall in the lowest quartile were calculated for the five sub-boroughs with the highest proportion of stabilized units and the five sub-boroughs with the least number of stabilized units. Next, the actual percentage of renter households in this particular income quartile were calculated for both sets of sub-boroughs.

If rent regulation were positively associated with economic integration in the five sub-boroughs with the highest proportion of stabilized units, the actual percentage of households in the lowest income quartile would be significantly higher than the predicted percentage. In short, stabilization would allow more lower income households to live in the neighborhood. Conversely, the actual percentage of households in the other five sub-boroughs would be lower than the predicted value. However, the results did not strongly support this hypothesis. The regression predicted that 15 percent of the renters in the five most stabilized sub-boroughs should have incomes of less than \$7,700. The actual percentage was only slightly higher at 18 percent. In the five least stabilized areas, the calculated percentage and the actual

value were almost identical at 31 percent and 32 percent respectively.

[Editor's Note: Since the completion of this report, a Board member suggested that the correlation between income and the percentage of rent stabilized units might be higher if renters in the second lowest income quartile were used in the analysis. Staff undertook this additional analysis and the results were similar to those presented here - there was no significant relationship between the extent of rent stabilization and economic integration.]

## Conclusion

It is critical to keep in mind that by demonstrating little in the way of a statistical relationship between economic/racial integration and rent stabilization, nothing conclusive can be said about any causal relationship between them. It may well be that rent regulation promotes economic or racial integration in neighborhoods that would experience greater segregation in its absence. Given the many complex factors affecting integration levels, stabilization may have affected integration in ways imperceptible in any linear regression model. At present this data is simply inconclusive.

Last year staff suggested that "pressures affecting economic and racial integration occur during periods of market transition and rent regulation may have a critical impact at such times." While the present analysis has focused on the general experience of the City, no attempt was made to identify and examine neighborhoods in transition. More recent HVS data, decennial census data and other sources of information may permit staff to identify City neighborhoods in transition. A closer examination of the impact of rent regulation on economic and racial integration within these neighborhoods may provide further insight into this issue. ○

---

# *Population and Housing Supply*

---

## ANALYSIS OF THE 1980 AND 1990 CENSUS DATA

### Summary

The release of the 1990 Census data on population and housing allowed staff to analyze changes in housing conditions from 1980 to 1990. Since the census data does not make any distinction in the type of housing units, such as cooperatives/condominiums, stabilized units, etc. it is difficult to make a definitive conclusion in relation to the stabilized stock only. However, what this data showed is the general conditions of the housing market in New York City during a ten-year period:

- The city's population grew by 3.5 percent.
- The total number of renter-occupied units fell by 5.8 percent, whereas owner-occupied units rose by 23.8 percent.
- An additional 20,500 units were counted as vacant, a percentage change of 13 percent.
- For the city as a whole there was an increase of 1.6 percent in total housing units.
- The number of housing units available for rent rose, resulting in a higher rental vacancy rate.
- The combination of a growing population, a diminishing rental housing stock, and rising rents, resulted in a large increase in severely crowded households.

### The Housing Stock

New York City's housing stock increased by almost 46,000 units from 1980 to 1990, a net growth rate of 1.6 percent. The growth in housing units is a result of a 26 percent increase (+171,800) in the total number of owner units and a decrease of 5 percent (-111,500) in the total number of rental units.

Although the gain in the housing stock was not evenly distributed among the boroughs, the distribution of the housing stock did not change significantly. Manhattan accounted for more than 60 percent of the change in total units (30,400), followed by Staten Island (20,800) and Queens (12,600). However, the Bronx and Brooklyn showed a decline in their housing inventory. The Census Bureau reported a drop of 2.3 percent and 0.9 percent in housing units for the Bronx and Brooklyn, respectively.<sup>1</sup>

The number of vacant units in the city, which includes vacant for sale, vacant for rent and all other vacant units, grew 13 percent in the last ten years. This growth came entirely from additional units which were vacant for sale or for rent. The vacant units available for sale grew by almost 200 percent, and those units which were reported vacant for rent increased by 18 percent. The number of vacant units not available either for sale or rent decreased by 19 percent from 1980 to 1990.

The decline in vacant units unavailable for sale of rent is due mainly to a 69 percent drop in the number of boarded-up units. Even though the percentage change of vacant units for rent was somewhat more modest than those vacant units available for sale, rental vacancies still account for 50 percent of all vacant units in the city.

---

<sup>1</sup> It should be noted that the housing unit counts will not be subject to correction for undercount or overcount. For this reason, the data on housing units must be interpreted with care. Small changes in housing counts may not be significant.

## The Rental Market

In 1980, 77 percent of all occupied units were inhabited by renters. By 1990 the Census Bureau counted 71 percent of the housing units as renter-occupied units.

As renter-occupied units declined in number, available vacant units for rent increased in the city. The additional vacant units for rent translated to a rental vacancy rate of 4.1 percent. This is substantially higher than the 3.3 percent vacancy rate reported in 1980.

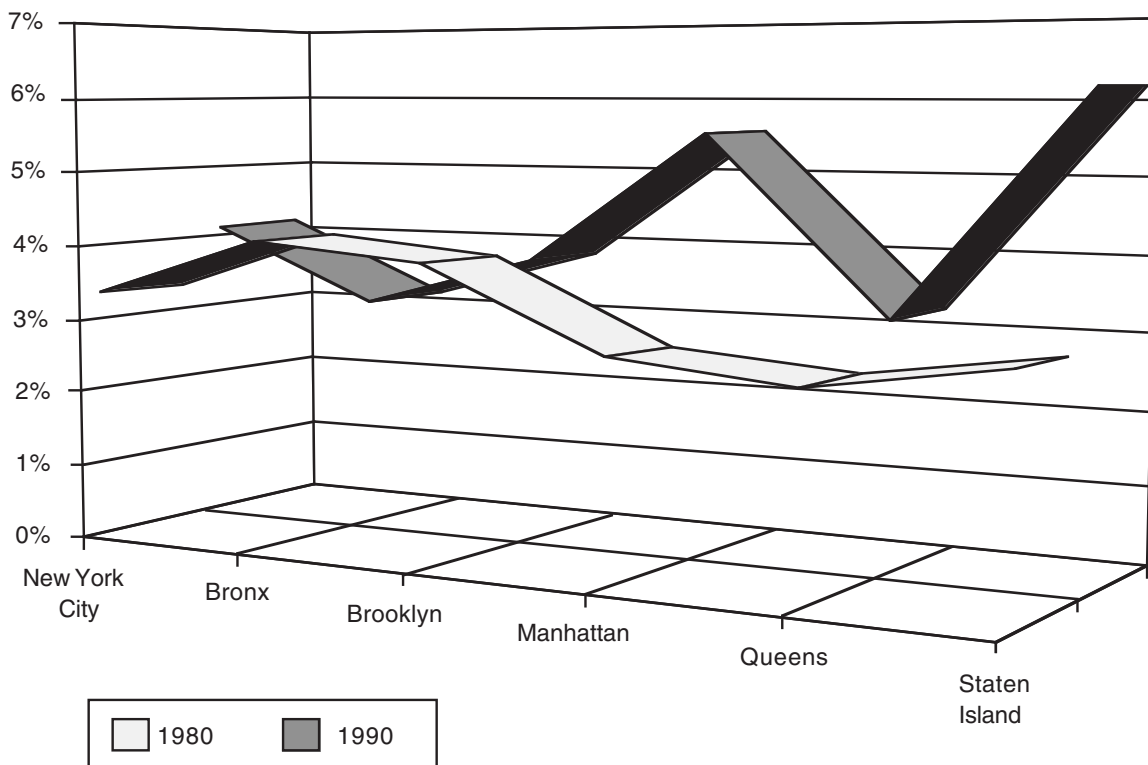
In 1990, the vacancy rate across the city ranged from a low of 3.1 percent in the Bronx to over 5 percent in Manhattan and 6.2 percent in

Staten Island. Relative to 1980, the census data showed a substantial tightening of the rental market in the Bronx and an increase in available rental housing in Staten Island and Manhattan (see chart below).

Although Staten Island experienced the highest vacancy rate increase of any borough, from 2.9 to 6.2 percent, the increase constituted only 9 percent of the additional vacant units. In contrast, there was a large number of additional vacant units in Manhattan, accounting for 81 percent of the additional citywide vacancies (an increase of 15,500 units).

Unfortunately, no data is yet available on asking rents for vacant units. However, since all of the additional vacancies were in the "high rent"

**Rental Vacancy Rate by Borough,  
1980 and 1990 Census**



Source: NYC Department of City Planning, Population Division, U.S. Bureau of the Census.

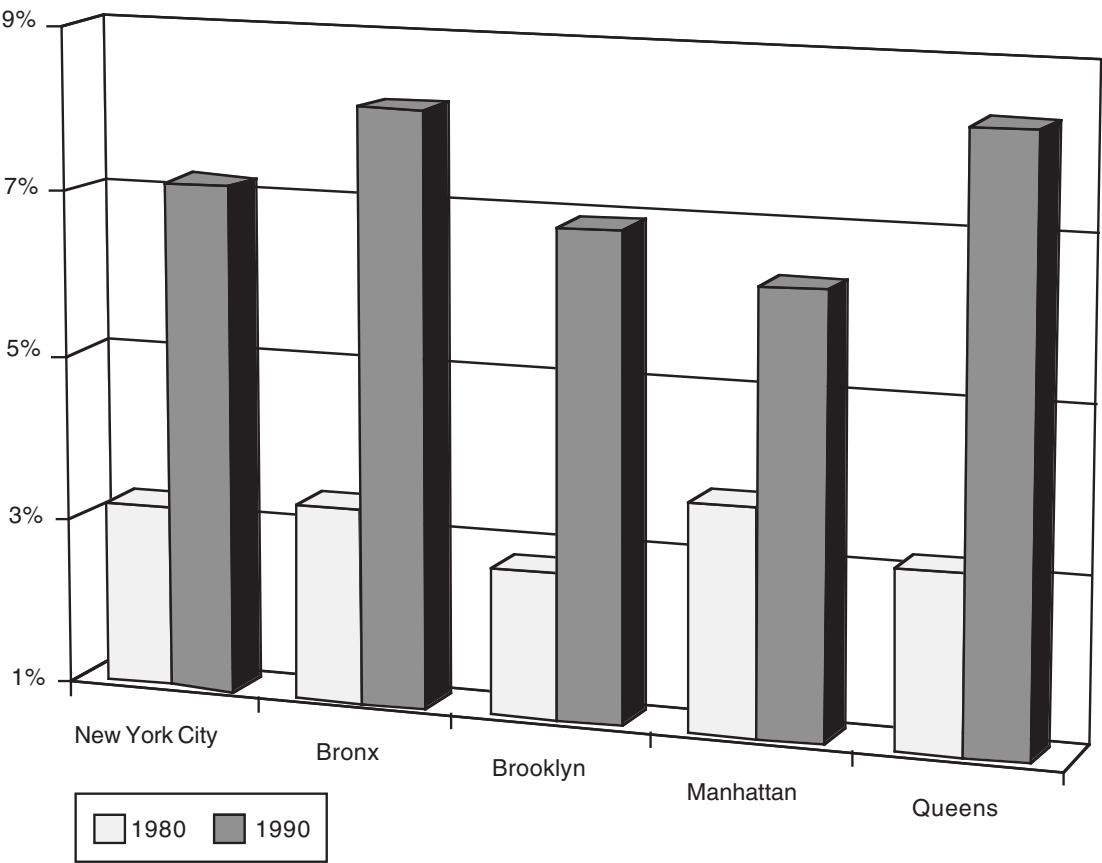
boroughs (i.e. not the Bronx or Brooklyn), one might assume that asking rents have risen more than rents for occupied apartments. In short, more units are available for rent but the asking rents for these units are probably quite high.

As a direct result of a diminishing rental housing stock and a growing population, overcrowded renter housing units have risen. There was a large increase in severe crowding. Using the definition of more than 1.5 persons per room as severe crowding, 7 percent of all renter-occupied units were severely crowded in 1990. This is more than double what was

reported ten years ago.

Severe crowding in renter-occupied units increased significantly in each of the boroughs. The most notable case was in Queens. In 1980 3.2 percent of the renter-occupied units in Queens showed severe crowding; ten years later this changed to 8.3 percent. This is an increase of nearly 150 percent. The other boroughs also showed a growth rate of over 100 percent in severe crowding. The sole exception was Manhattan. Relative to the other boroughs, the growth rate in Manhattan was slow, an increase of less than 54 percent (See chart).

Severe Crowding by Borough, Renter-Occupied Units



Source: NYC Department of City Planning, Population Division, U.S. Bureau of the Census.

Note: Crowding is defined as 1.01 persons per room or more, severe crowding is defined as 1.51 persons per room or more.

# HOUSING SUPPLY REPORT

## New Construction, Tax Abatements and In Rem Housing

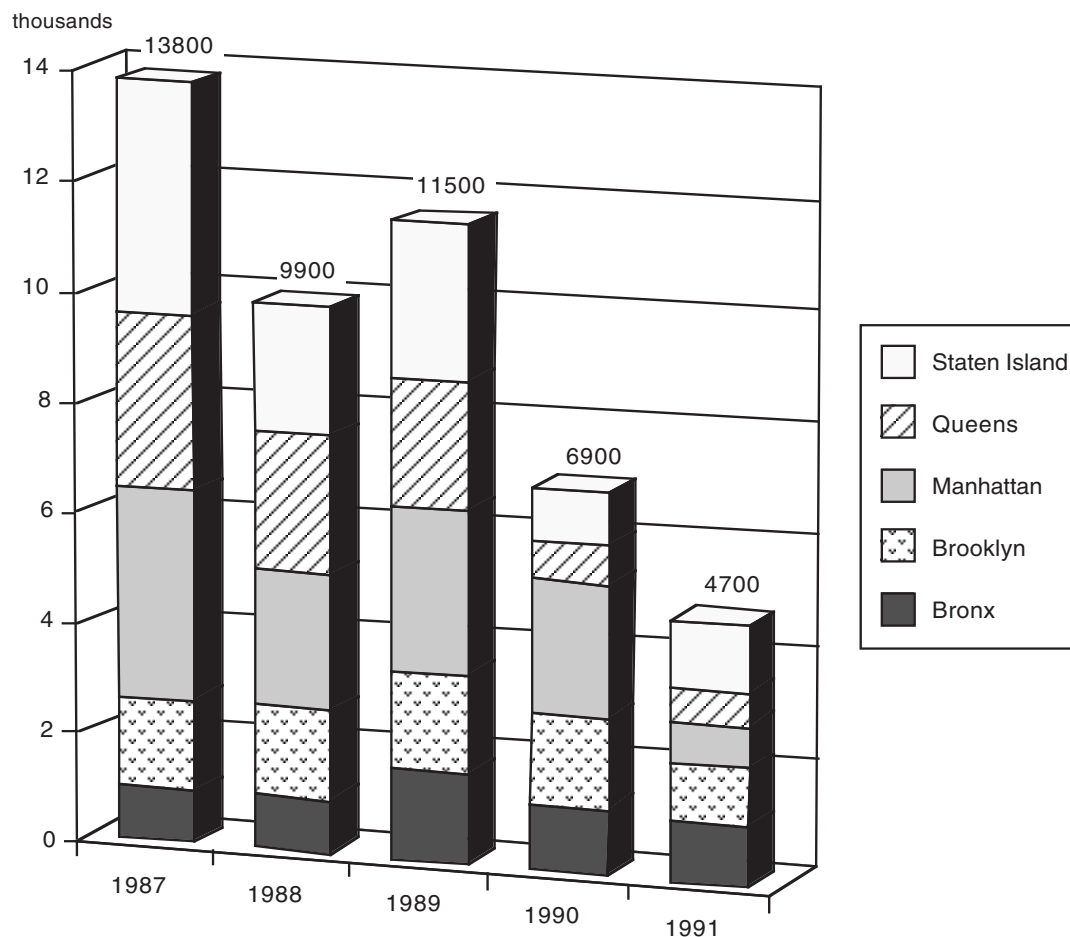
### *Housing Permits*

The number of housing permits issued for new construction fell by 32 percent in 1991

reflecting another year of sluggish growth in the housing market (see chart).

The share of permits issued in Manhattan and Queens continued to decline in 1991. In 1987 and 1988, permits from these two boroughs constituted over 50 percent of the citywide total. In 1991, permits from Manhattan and Queens made up less than 30 percent of the total. In fact, this is the first time in the past five years in which the number of housing permits issued in Manhattan did not constitute at least 25 percent of the total. The proportion of housing permits for the Bronx and Staten Island went up considerably, accounting for nearly half of the overall number of housing permits issued in 1991.

### Permits Issued for New Housing, by Borough, 1987-91

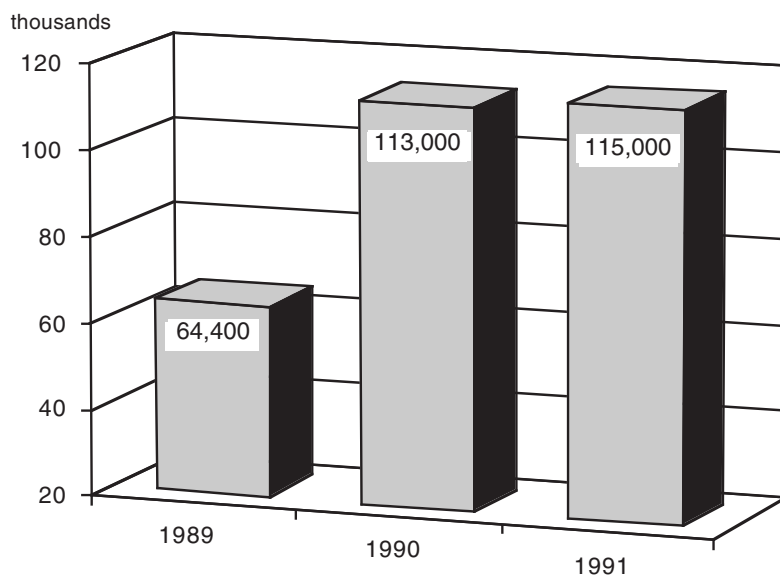


Source: Bureau of the Census, Construction Statistics Division, Building Permit Branch.

**J-51**

The J-51 tax abatement and exemption program indicates the level of rehabilitation activities in existing buildings. Tax abatements are issued for major capital improvements, moderate rehabilitation requiring the replacement of at least one building system, and gut rehabilitations. The number of units receiving J-51 tax abatement benefits has remained relatively constant in the two previous years, 113,000 units in 1990 and 115,000 units in 1991. However, the dollar amount of certified reasonable cost has

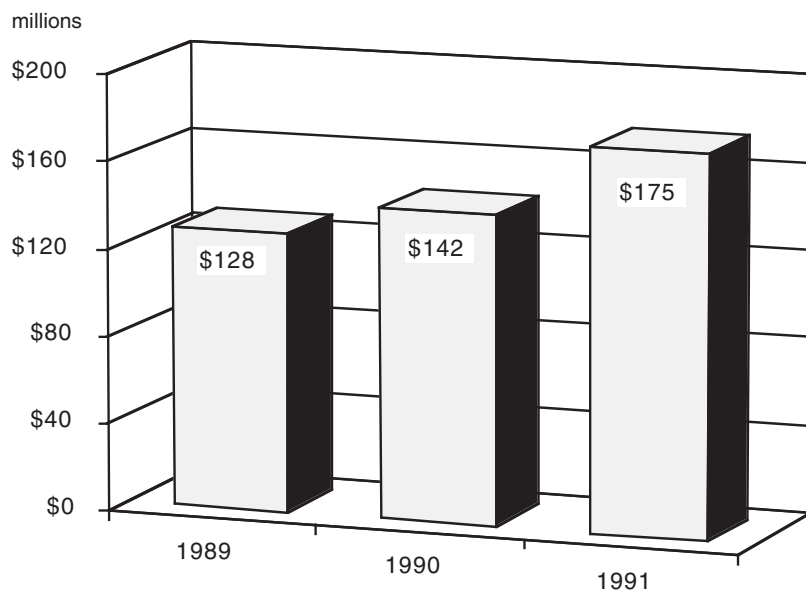
### Number of Units Receiving J-51 Tax Abatements and Exemptions, 1989-91



Source: NYC Department of Housing Preservation and Development, Office of Development.

Note: Figures rounded to nearest 100 units.

### Total Certified Reasonable Costs for J-51 Tax Abatement, 1989-91



Source: NYC Department of Housing Preservation and Development, Office of Development.

Note: Rounded to the nearest million.

increased from \$142 million in 1990 to \$175 million in 1991. The revised (January 1990) schedule of certified reasonable costs may have provided greater incentive for owners to file for J-51 tax benefits in the past two years. It should be noted that certified reasonable costs approved by HPD's Office of Development are not the same as actual tax abatements. The certified reasonable costs are approximations of the actual rehabilitation costs. HPD allows the actual rehabilitation costs or tax abatements to be as high as 150 percent or as low as 50 percent of the certified reasonable costs.



## 421-a

One indicator of new multi-family units entering the housing market is the number of preliminary 421-a certificates issued by HPD's Office of Development. In 1990, the number of units accounted for by 421-a certificates issued was at a record low, 980 units. In 1991, the number of units receiving 421-a certificates increased by more than 200 percent to 3,320. Over two-thirds of these multi-family units were in Manhattan and Brooklyn (1380 units in Manhattan and 820 units in Brooklyn). While the 1991 level represents a substantial increase from the previous year, the number of units receiving 421-a certificates remains the second lowest in recent years.

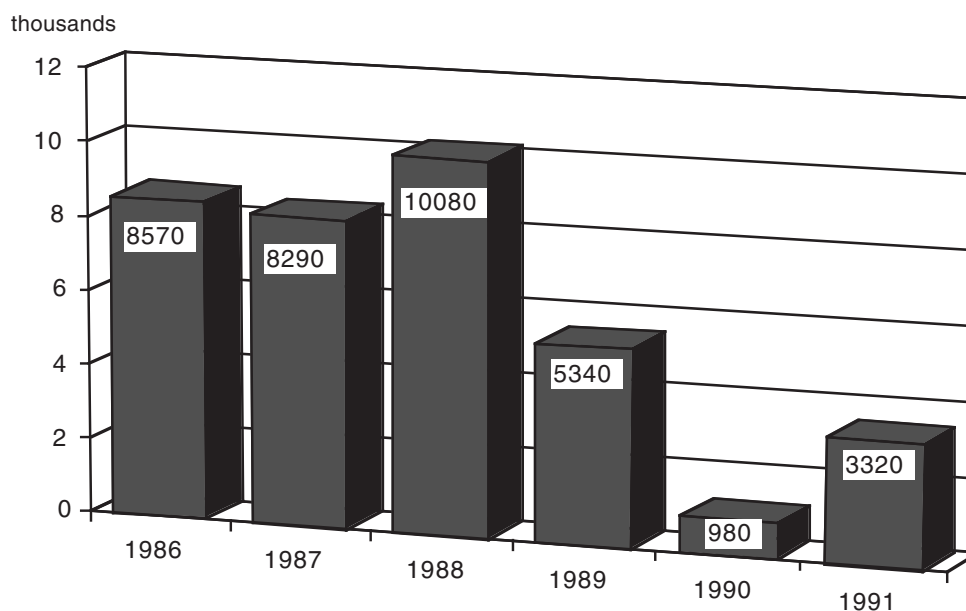
## Rental Vacancy Rates

According to the 1991 New York City Housing and Vacancy Survey, the citywide rental vacancy rate increased from 2.5% in 1987 to 3.8% in 1991. Other relevant information, such as the vacancy rate for rent stabilized apartments in 1991, has not yet been released by HPD.

[Editor's Note: Since the completion of this report, HPD has released additional data from the 1991 *Housing and Vacancy Survey* which shows that the vacancy rate for rent stabilized apartments is 3.9%.]

As noted earlier, the 1990 census data showed a citywide rental vacancy of 4.1 percent in 1990, compared with the 3.3 percent vacancy rate reported in 1980.

### Units in Buildings Receiving Preliminary Certificates for 421-a Tax Abatement, 1986-91



Source: NYC Department of Housing Preservation and Development, Office of Development.

Note: Figures rounded to nearest 10 units.

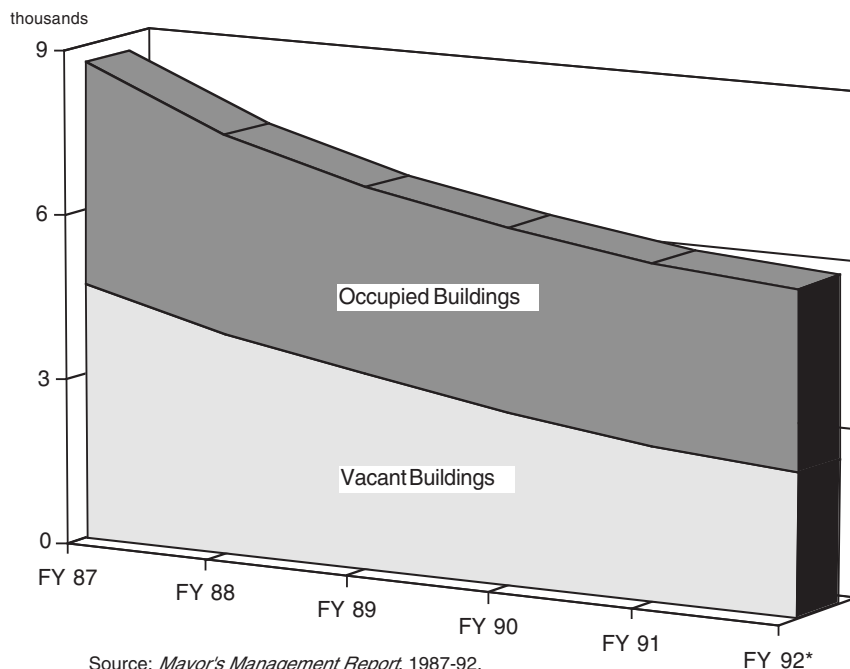
### *In Rem Housing*

The number of units in the City's in rem stock has continued to decline in FY'92. From FY'91 through the first quarter of FY'92, the number of in rem buildings has declined another 3% from 6,030 to 5,850 (see chart). Vacant buildings decreased another 7.5% from 2,800 to 2,590. However, there is little change in the number of occupied buildings.

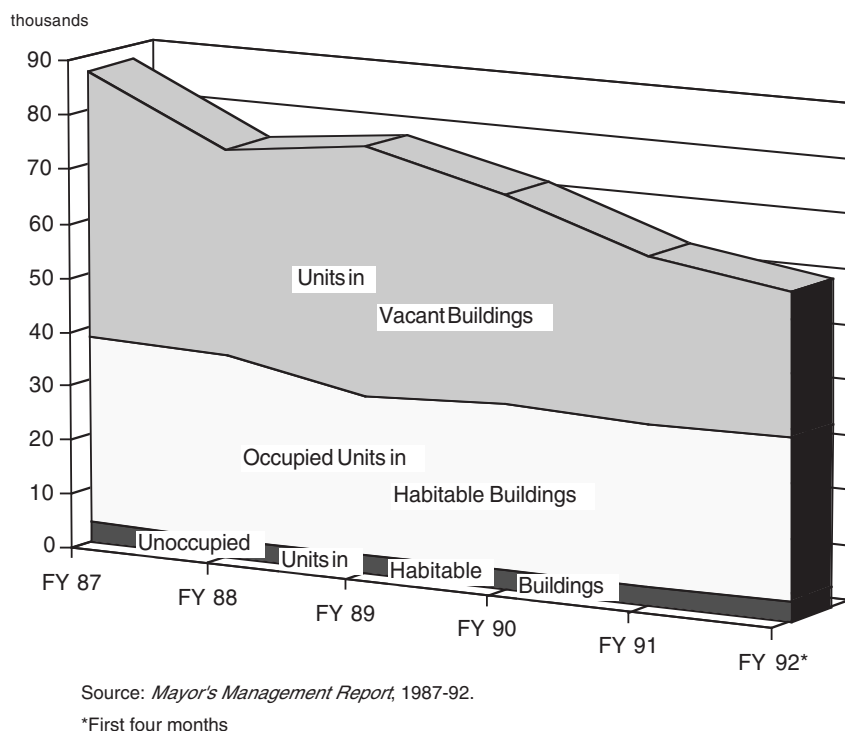
According to the Preliminary Mayor's Management Report (Feb. 1992), those remaining vacant are smaller buildings located in residential neighborhoods. The City is now focusing on creating programs to rehabilitate these smaller vacant buildings.

The total number of units has decreased by another 7% from FY'91 (see chart). While the number of units in habitable buildings, both occupied and unoccupied, has remained relatively constant during the first quarter of '92, the number of vacant units in buildings that are unoccupied has declined another 1%. It seems that much of HPD's effort has been focused on reducing the

### **In Rem Central Property Management, Buildings, Fiscal Years 1987-92**



### **In Rem Central Property Management, Units, Fiscal Years 1987-92**

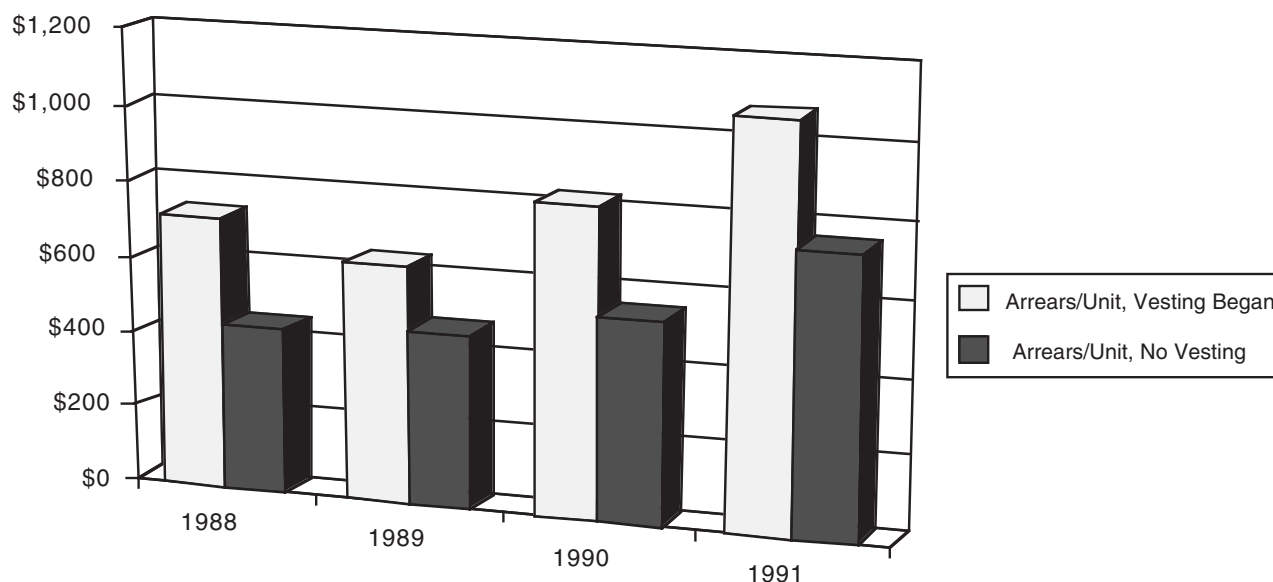


## Real Estate Tax Arrearage

Last year staff obtained tax arrearage data from the Department of City Planning for the years 1988 through 1990. This year's arrearage data includes 1991 as well. This information seems to confirm much of the testimony heard by the Rent Guidelines Board this year:

- The number of buildings with arrears (but not yet vested) declined between 1988 and 1990, but increased somewhat in 1991. The increase was from approximately 5900 buildings in 1990 to 6200 in 1991, or about 5%. The number of UNITS in buildings with arrears increased by 10% due to an increase in average building size.
- The City Planning data set was expanded this year to include information on buildings entering the vesting pipeline (but not yet vested). The figures confirm testimony that no significant increase in vesting has occurred. The number of buildings entering the vesting pipeline (but not yet vested) was 204 in 1990 and 209 in 1991.
- Although vesting has not increased in recent years, the number of buildings which are candidates for tax foreclosure has risen sharply. The median number of quarters in arrears (for buildings with arrears but without vesting actions) was 1.7 in 1988 and 1989, 1.9 in 1990 and 2.2 in 1991. More noteworthy may be the number of buildings in arrears for 4 or more quarters: Approximately 1900 buildings in 1988 and 1989, 2200 in 1990, and 2800 in 1991. The 1990 to 1991 increase was 31%.
- Among buildings not yet in the vesting pipeline, the average amount of arrears per unit rose sharply last year, from \$537

### Average Tax Arrears Per Unit, Stabilized Buildings, 1988 - 91



Source: Department of City Planning, Computer Information Services.

Note: Includes only rent stabilized buildings registered with the NYS Division of Housing and Community Renewal.

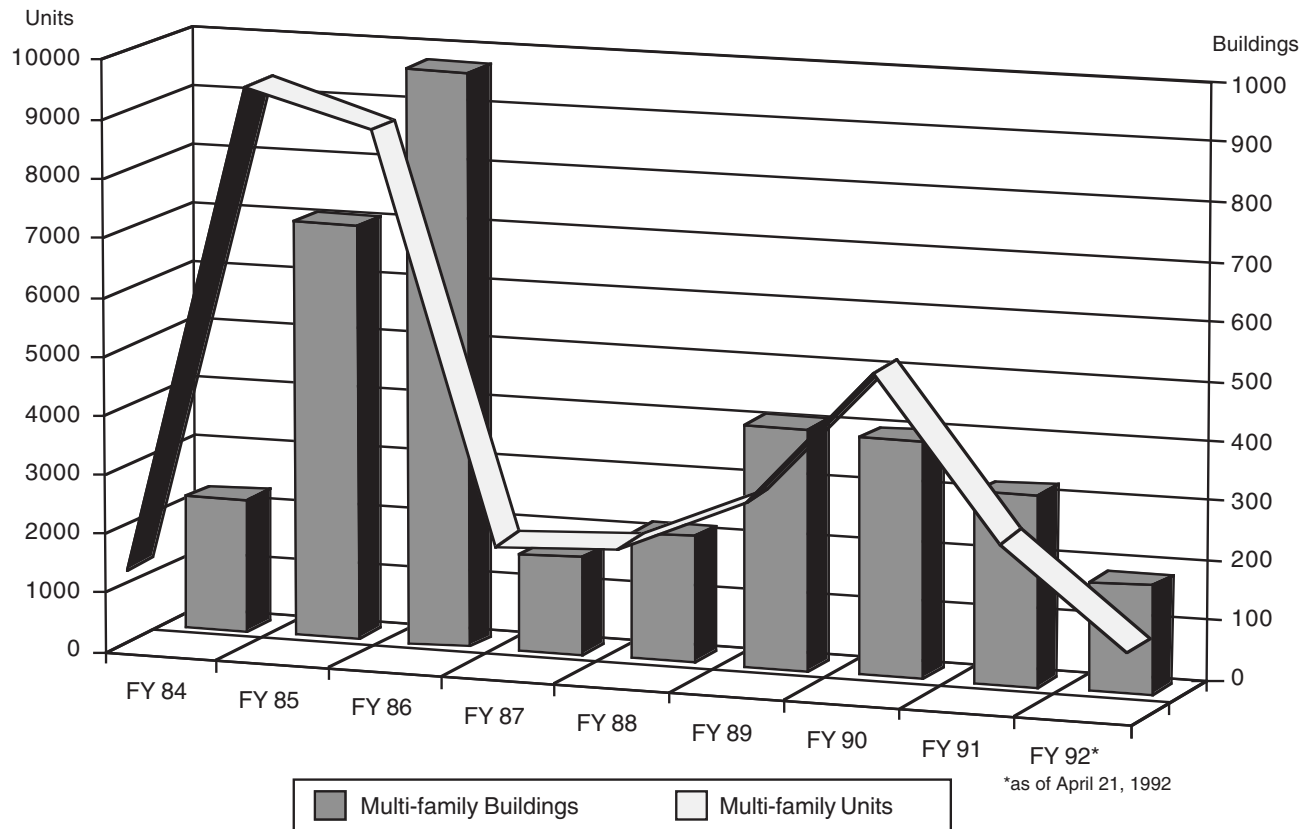
to \$745 per unit, an increase of 38%. The change was somewhat less dramatic for buildings beginning the vesting process in 1991 - an increase from \$817 to \$1067, or 31% (see chart previous page).

## Tax Foreclosure

While the redemption process has not changed, under the new city charter an In Rem Foreclosure Release Board was formed last year to approve redemption applications, a task formerly performed by the Board of Estimate.

According to Local Law 45, after a property falls in tax arrears for one year, the property owner is entitled to a two-year period to redeem the property. During the first four months of the redemption period, the property owner may work out some form of installment plan with the Finance Department to pay back taxes and penalties for the property. However, if the property owner wishes to redeem the property during the following 20 months, the owner has to apply for discretionary redemption with the new Foreclosure Release Board. The vesting statistics shown in the graph below are the actual number of buildings and units vested by the City.

**HPD Vestings of Occupied Multiple Dwellings,  
Fiscal Years 1984-92**



Source: Department of Housing Preservation and Development, Office of Property Management.

As we indicated in last year's report, HPD's Office of Property Management changed its vesting practice from a borough-by-borough basis to citywide annual vesting in fiscal 1989. Since then, the level of vesting activities has shown a steady downward trend although the size of these buildings tends to fluctuate from year to year. It seems that the recession has not yet had any measurable impact on the level of vestings.

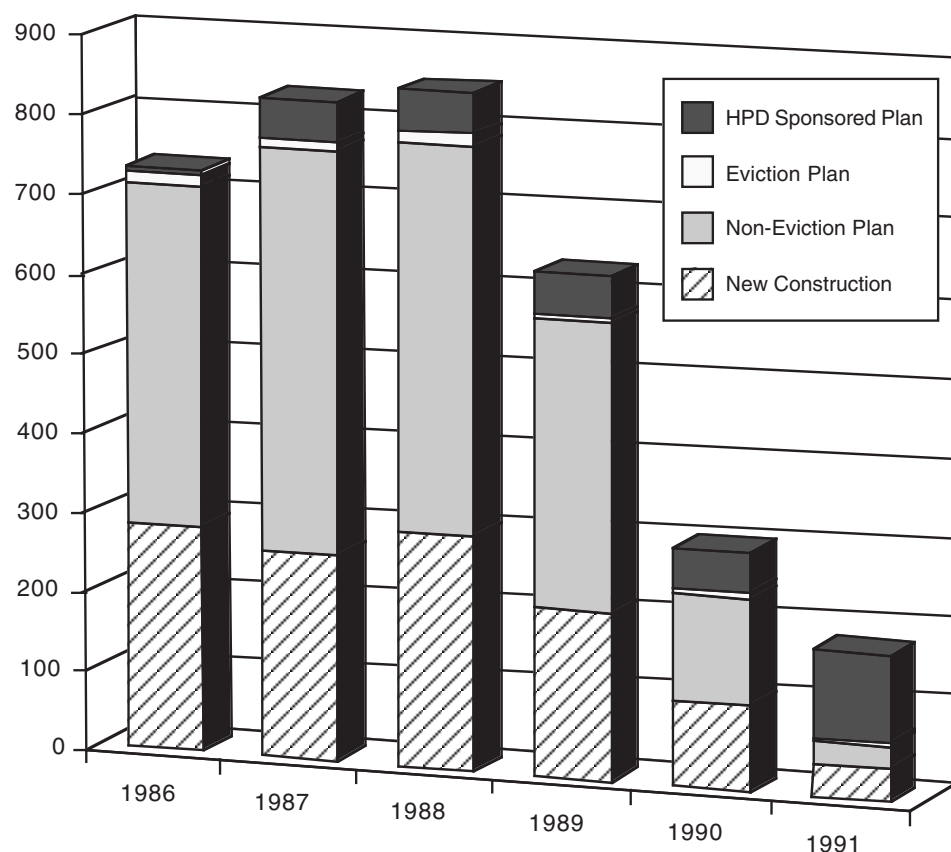
The number of occupied buildings vested has been declining since fiscal 1990. The number of occupied buildings vested in fiscal 1991 represented a 20 percent decline from the previous fiscal year. Additionally, because most of the occupied buildings vested in fiscal 1991 were smaller buildings, the number of units decreased by nearly 50 percent. In fiscal 1992, the Office of Property Management anticipates an additional decline in vestings. The numbers shown on the chart on the opposite page are the actual number of occupied buildings and units vested as of April 1992 (43 percent reduction in the number of buildings vested and 55 percent reduction in the number of units vested) The planned figures for fiscal 1993 have not been released by HPD

yet, but the Office of Property Management does not anticipate substantial increases in vestings.

## Residential Co-op and Condominium Activity

Both the number of plans and the number of units in plans accepted for filing by the Attorney General's Office in 1991 reflect the lowest level of co-op and condo construction and conversion activity since 1981.

**Number of Plans Accepted for Filing, 1986-91**



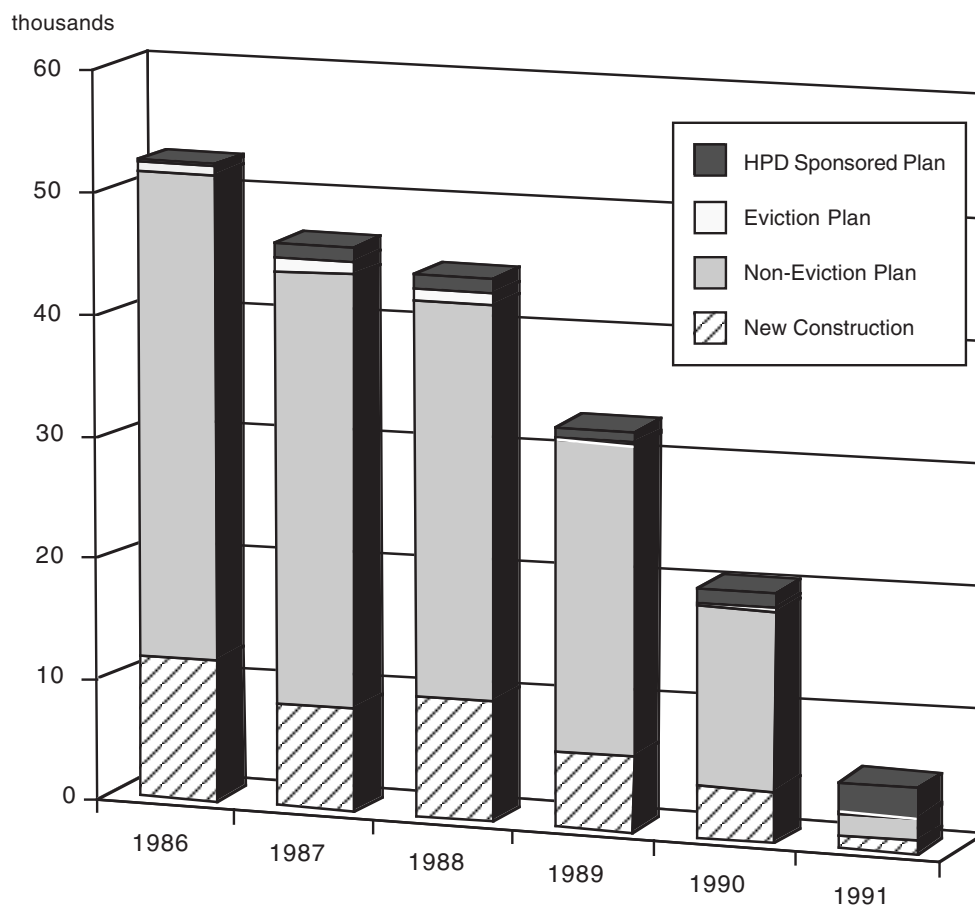
Source: New York State Attorney General's Office.

Before 1990, non-HPD plans constituted over 90 percent of the total number of co-op and condo plans accepted for filing. However, because of the extremely weak economy and widespread financial problems in the co-op and condo market in recent years, many banks became reluctant if not unwilling to provide co-op and condo loans to both sponsors and potential co-op and condo owners. In 1991, new co-op and condo construction accounted for only 23 percent (42 plans) of the plans accepted for filing while conversions accounted for 17 percent (32 plans) of the plans accepted for filing. Of these 74

plans, 31 were for Manhattan and 26 were for Brooklyn.

While private sector construction and conversion activities plummeted in 1991, the level of HPD sponsored co-op and condo conversions and rehabilitation continued to expand. In 1991, HPD sponsorship constituted 60 percent of all plans accepted for filing and 40 percent of the units. In terms of distribution by borough, most of the conversion activity sponsored by HPD was in Manhattan (40 plans and 1230 units), while the remainder was in the Bronx and Brooklyn. ○

### Number of Units in Plans Accepted for Filing, 1986-91



Source: New York State Attorney General's Office.

---

## *Rent Stabilized Hotels*

---



# PRICE INDEX OF OPERATING COSTS FOR RENT STABILIZED HOTELS

The hotel price index was developed by USR&E based on its findings in the *Report on the Analysis of Expenditure Data for the 1985 Price Index for Hotels*. It includes separate indices for each of the three categories of hotels (due to their dissimilar operating characteristics) and an index for all hotels. The overall increase in the hotel PIOC was 2.5% this year, somewhat below the rate of increase for apartments. Increases for the various building types were: Hotels 3.5%, Rooming Houses 2.5%, and SRO's 1.2%.

The tax relative was computed using a list of hotel buildings compiled by HPD for the 1991 HVS, as was the case last year. The overall increase in taxes was 12%. The increase was about the same for each of the hotel types.

The labor component for hotels consists of eleven separate subcomponents, including union wage and benefit increases, changes in social security and unemployment insurance, and wages for non-union supers, maids, desk clerks, maintenance workers and janitors. In previous years it has been extremely difficult to obtain wage quotes for non-union maids, desk clerks, and maintenance workers (Specs 211, 212, 213). Equipped with a better list of hotels and a substantially higher response rate to the owner survey, RGB survey staff thought it might be possible to obtain a reasonable number of responses this year.

Unfortunately, such was not the case. After a considerable amount of effort, the survey staff was able to obtain only 3 verified wage quotes for specs 211, 212 and 213. Three quotes were not sufficient to compute reliable price relatives, and forced us to question the appropriateness of the specs. After discussing this question with Speedwell, Inc., a joint decision was made to eliminate the specs from the hotel index and to reallocate the weight of these items to the other non-union wage components (i.e. Spec 211, Non-union supers and Spec 216, Non-union janitors). The increase in labor costs, using the new weights, was 4.0%, or somewhat less than the increase for apartments.

Fuel costs fell by 7.9%. The decrease was smaller than for apartments because more hotels use #2 fuel oil, which decreased in price less than the other grades.

## Change in the Components of the Price Index of Operating Costs for Rent Stabilized Hotels, April, 1991 to April, 1992

|                            |             |
|----------------------------|-------------|
| Taxes .....                | 12.0%       |
| Labor Costs .....          | 4.0%        |
| Fuel Costs .....           | -7.9%       |
| Utilities Costs .....      | -3.3%       |
| Contractor Services .....  | 3.8%        |
| Administrative Costs ..... | 3.2%        |
| Insurance Costs .....      | 2.3%        |
| Parts & Supplies .....     | unchanged   |
| Replacement Costs .....    | 2.9%        |
| <b>Overall .....</b>       | <b>2.5%</b> |

# TRANSIENT RENTALS IN SRO-TYPE BUILDINGS

## Summary

The purpose of this study is to determine the proportion of rent hotel owners derive from “transient” tenants. In this paper we compare data derived from Department of Finance I&E statements with DHCR rent rolls. For buildings which are registered with DHCR, it appears that hotel owners derive a considerable proportion of their revenue (40% or more) from transient rentals. Registered rooming houses and SROs, on the other hand, seem to have little or no transient income.

[Editor's Note: One of the major issues the Rent Guidelines Board has debated over the past several years is "transient income" in hotels. Tenant advocacy groups have argued that owners benefit greatly by short term rentals not subject to stabilization regulations. Hence, no rent increases for stabilized tenants are necessary. Owner groups contend that such a policy merely punishes the "good" owners who rent to long-term stabilized tenants (i.e. not to transients). This study contains the only concrete evidence presented to the Board regarding the extent of transient rentals.]

## Background

Last year's research consisted of two hotel studies. In the first of these, the so-called “Registration Study,” staff attempted to estimate the number of SRO-type buildings which should have registered with DHCR from 1984 to 1989,

and the percentage of buildings and units which actually did register. Using very conservative assumptions, it was estimated that almost half of all buildings and 40% of all units were not registered even once during the period. Based on this analysis we concluded that

“The data ... raises some troubling questions about the implementation of rent regulation in the hotel sector. Given the low rate of registration and the possibility that many owners may derive a small percentage of revenue from permanent tenants one might argue that the impact of the regulatory system on this vital housing resource is rapidly diminishing.”<sup>1</sup>

The second hotel study analyzed income and expenses in hotel buildings using the Finance Department's Local Law 63 filings. Although this study did allow us to compute averages for O&M expense, income, and the O&M to income ratio, it proved to be impossible to estimate how much income landlords derived from “transient” (i.e. non-stabilized) tenants.

In April the RGB gained access to DHCR's “on-line” rent registration records, thereby making it possible to compare the total amount of income reported by landlords to the Department of Finance with the aggregate amount of rent registered with DHCR. The difference between these two figures can be considered a rough estimate of income derived from non-registered units, some of which may be rented on a “transient” basis.<sup>2</sup>

<sup>1</sup> *Rent Stabilized Housing in New York City: A Summary of Rent Guidelines Board Research*, 1991, p.74.

<sup>2</sup> “Rental income” reported to the Department of Finance includes rent from all “apartment units” (SRO-type or regular) as well as rent from commercial units (e.g. stores, parking). It is a measure of rent collected rather than rent charged. Registered DHCR rents, on the other hand, are rents charged and account for vacancy losses (in our study) but they do not account for collection losses. If commercial rent constitutes 10% of total income (as in the apartment I&E study) and collection losses average 10%, these factors would more or less cancel out, making the two sources of data roughly comparable.

The income and expense study included data from 178 buildings, including 66 hotels, 67 SROs, and 45 Rooming Houses. After a comprehensive search of the DHCR registration records, we found that only 107 of these buildings registered between 1988 and 1991.<sup>3</sup> In short, 40% of the buildings were unregistered compared to 47% in the previously mentioned registration study. Registration rates ranged from 67% of SROs, to 58% of rooming houses, and 55% of hotels.

Addresses for the 107 registered buildings were transmitted to the Finance Department. Finance staff then “matched” these buildings with last year’s computer file to produce income and expense data for the registered buildings. RGB staff undertook the task of manually entering the DHCR data (comprising 107 rent rolls and about 7700 units) into spreadsheets and deriving estimates of rent.

<sup>3</sup> Last year’s I&E study was largely comprised of income and expense filings for calendar 1989. The most directly comparable DHCR rent information is from April 1989.

**Buildings Registered with DHCR  
Which Also Filed I&E Forms**

|                     | % Registered          |                                  |                                    |
|---------------------|-----------------------|----------------------------------|------------------------------------|
|                     | % Units<br>Registered | Units registered<br>“Stabilized” | % Income from<br>Registered units* |
| Rooming Houses..... | 95%                   | 87%                              | 112%                               |
| SROs .....          | 88%                   | 91%                              | 104%                               |
| Hotels .....        | 57%                   | 88%                              | 60%                                |

\* Defined as registered rent divided by rents reported to the Department of Finance.  
Source: NYS Division of Housing and Community Renewal, NYC Department of Finance.

**Findings**

The table below shows the characteristics of the buildings in our study. In order to allow direct comparisons between the amount of rent reported to DHCR and the amount of income reported to the Department of Finance, buildings with commercial units have been eliminated. This allows us to compare income reported to Finance (nearly all of which presumably comes from residential unit rents) with rents registered with DHCR.

Although all of these owners registered their buildings with DHCR, the percentage of units which were registered varies considerably.<sup>4</sup> In the rooming house and SRO sectors it appears that 95% and 88% of the units (respectively) were registered.<sup>5</sup> In the hotel sector, on the other hand only 57% of units were registered.

The table also indicates the percentage of registered units which are labelled “stabilized” in the DHCR files. Between 87% and 91% of all the units are registered as “stabilized” units. The other two categories are “exempt” (indicating that the unit is either temporarily or permanently exempt from rent stabilization) and “vacant.” Very few units are registered “exempt.” The vast majority of

<sup>4</sup> This percentage is the sum of all units registered with DHCR (whether “stabilized,” “exempt” or “vacant”) divided by the number of units reported on the Finance Department income and expense form. It should be kept in mind that ALL of these figures were reported by owners to the respective government departments.

<sup>5</sup> Some of the units are certainly owner-occupied and not required to register. As a result, the percentage of units which should have been registered and were actually registered is slightly higher than indicated by the table.

the registered units not registered as “stabilized” are in the “vacant” category. Vacant units account for about 10% of all registered units.

The fact that few units are registered as exempt does NOT mean that transient occupancy is a rare phenomenon. As we noted previously, 40% of the buildings in the I&E sample did not register at all and a large percentage of hotel units are unregistered. Some portion of these may be rented on a transient basis. In addition, according to testimony heard by the board this year some landlords also rent out units registered as “stabilized” on a transient basis.

The last column of the table is the amount of registered rent divided by the amount of income reported to the Department of Finance.<sup>6</sup> In the rooming house sector this figure is 112% - in other words, DHCR rents actually exceed income reported to Finance. Part of the difference between the DHCR and Finance figures is due to collection losses. If collection losses of 10% are included, the figure would approximate 100%. It is conceivable that some of the rent paid by tenants to small landlords is in cash and that not all is reported. Note from the table that the characteristics of SROs are similar to rooming houses.

Hotels derive approximately 60% of their income from registered units.<sup>7</sup> Since we have excluded buildings with commercial units from our sample, the remaining 40% of the income must be derived from the unregistered units (43% of all hotel units), some portion of which may be rented on a transient basis. **It seems clear that hotels have a very different income structure from rooming houses and SROs.**

**The figures cited here suggest that transient income is probably an important factor in the hotel industry.** Rooming houses, on the other hand, may derive little if any income from transient tenants. SROs are between the two extremes but appear to be more akin to rooming houses than hotels.

One final aspect of these figures is worth noting. The average monthly rent for non-registered hotel units is \$351, or less than the average for registered stabilized units (\$455). Since one might expect unregistered units to rent for more than the registered units, the only plausible explanation is that a large number of units are unoccupied - either through deliberate warehousing or because of inability to rent them to transients. ○

<sup>6</sup> DHCR rents are annualized to arrive at a figure comparable to the Department of Finance figures. Included in the DHCR figure are all unit rents classified as “stabilized” or “exempt” but NOT those classified as “vacant.” By excluding the vacant units we assume that this “snapshot” of the vacancy rate would hold true for the entire year.

<sup>7</sup> The figure may be somewhat less since collection losses are not considered.