PHILIP S. SHAW, ESQUIRE
99 Hancock Street
Cambridge, Massachusetts 02139

March 19, 1971

Mayor Alfred Vellucci
City Councillors
Cambridge City Hall
Cambridge, Massachusetts

Sir:

As you will recall I have communicated with the Council several times in the past concerning rent control in Cambridge, and I am again requesting time in which to speak. Most recently I appeared before the Council concerning the formula for fair net operating income. At that time I and other spokesmen for tenants' interests conclusively demonstrated that the formula was so inadequate that it was not justifiable. It was so clearly wrong, I felt, that the Interim Adminstrator and his successor would disavow it. Instead, however, the formula has been and is being applied with predictable results in rent adjustment cases.

Rent increases of between 25% and 50% have been granted, and these increases were far in excess of the increases needed to cover the increase in costs. The increases can only be attributable to the Administrator's guidelines and cannot be justified in any other fashion.

In one building that I know about the landlord asked for, and received, a rent increase of $25.00 per apartment over the March level of rent. Since this was what his rents were before rollback, and since the hearing was held in February, the tenants never saw much of the benefits of rent control.

As far as I know the tenants are all old people on low or fixed incomes. None of them had attended the hearing and none of them had rolled back their rents. (The landlord seems not to have told them about rollback). They could not afford this increase and yet it was granted.

From my knowledge of the situation, I would estimate that costs could have risen a maximum of $3,000.00; (including a tax increase of $1,138.00) this can in no way justify a rental increase of $6,300.00 per year. This formula and the Administrator's timidity in changing it are responsible for this harsh and outlandish result.

Since tenants are just beginning to suffer from Mr. Corkery's administration of the law, an investigation would be timely. If this council, either through a committee of two of its members or some other mechanism, were to obtain the facts in the present cases, they would be able to stop the abuses mentioned above.

You would need to know the amounts of increases granted, the increases in actual costs and the landlord's rate of return before and after rent control in order to get a clear idea of what has happened.

I hope that you will take steps to remedy this already deteriorating situation.

Very truly yours,

Philip S. Shaw

Philip S. Shaw

PSS/mw

March 9, 1971

Effect of Cambridge's "Fair Return" Formula on Rents

The following table shows the effect of Cambridge's current fair return formula on rents in 14 Cambridge buildings. Each of these buildings is presently under consideration for a rent increase, although no final determinations have been made to our knowledge.

The buildings vary in size from 2 to 100 units and contain a total of 436 apartments. The sample appears to reflect considerable variety in terms of geographic location, housing type, rent levels, and quality.

The data used in this analysis is based on income and expense figures supplied in landlords' supporting financial statements, which accompany their petitions for rent increase. These figures were revised as necessary, according to the best estimates of actual costs and income on the part of those familiar with the buildings.

The fair return formula under consideration is based on the following principles, as defined by the Cambridge Rent Control Administrator:

1. Fair net operating income should range within 10-15% of market value
2. Market value should equal between 5x and 7x gross annual income
3. Market value should equal 3x assessed value, as a rule of thumb.

The current regulations also state that the actual rates of return and gross rent multiplier used in each case will depend on housing conditions. Since we did not have adequate information to account for building quality in this analysis, we have applied the upper and lower limits of the formula to obtain a range of possible rent increases in each case.

Column III shows the rate of return (net operating income in relation to market value) the owners of these buildings were earning in March 1970. The figures are based on an estimated market value of 5x gross rents, using the lower limit of the city's formula. (A higher multiplier would yield a lower rate of return.) The average rate of return is about 9.8%. It should be emphasized that this rate of return was presumably satisfactory to most landlords--and probably more than satisfactory--since there were no controls on the housing market at that time.

Column IV shows how much of a rent increase over the March 1970 level would be required in order to maintain each owner at the rate of return he was making then. Under this approach, the landlord would be entitled to pass his entire cost increase since March 1970 on to his tenants, dollar for dollar. The average increase allowed by this method is about 7%. (Note that under this approach, the many landlords who were earning <u>more</u> than a fair return in March 1970 would continue to do so.)

Columns V-IX show what could happen to rents in these buildings under the city's fair return formula:

Columns V and VI show the range of increases that would be allowed if market value were defined as 5x gross rents--the lower limit of the city's formula. Under this standard, rent increases for the buildings studied would range from 9-33% on the average, depending on whether the owner was allowed a

10 or 15% return on the market value.

Column VII shows how much present rents would increase if market value were defined as 7x gross rents and the landlord were allowed a 15% return on the market value--the upper limit of the city's formula. Under this standard rents in the buildings studied would increase 63%, on the average.

Columns VIII and IX show the range of increases that would occur if market value were defined as 3x assessed value. Under this standard, rents in the buildings studied would increase from 20% - 50% on the average, depending on whether the owner was allowed to earn 10-15% on market value.

In summary, it is clear that the city's fair return formula would permit substantial--if not outrageous--increases in rent controlled buildings. Even the lower limits of the formula would allow rent increases which are greater than those required to maintain landlords at the rate of return they were making in March 1970, before rent control went into effect. In short, this means that the fair return formula would allow many landlords to earn a rate of return under rent control which is considerably higher than the rate they were satisfied with in the "free market." A formula that achieves this purpose can hardly be justified as consistent with the intent of the rent control act.

Urban Planning Aid
407 Highland Avenue
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EFFECT OF CAMBRIDGE'S FAIR RETURN FORMULA ON RENTS

I. Bldg	II. Units	III. Rate of Return 3/70 (FMV=5x)	IV. % Increase Needed to Maintain R of R 3/70	V.	VI.	VII.	VIII.	IX.
				Percentage Increases Allowed Under City Formula, if:				
				FMV=5x R=10%	FMV=5x R=15%	FMV=7x R=15%	FMV=3AV R=10%	FMV=3AV R=15%
A	92	9.4%	0%	3%	28%	58%	29%	68%
B	29	9.4%	12%	12%	36%	68%	40%	79%
C	100	12.9%	4%	5%	26%	56%	19%	54%
D	6	7.8%	3%	14%	38%	70%	17%	43%
E	25	9.8%	3%	5%	30%	60%	2%	25%
F	100	NA	NA	10%	35%	64%	NA	NA
G	6	8.3%	13%	20%	46%	73%	35%	67%
H	3	9.5%	1%	3%	28%	54%	7%	34%
I	23	11.2%	9%	3%	28%	58%	NA	NA
J	3	10.4%	2%	-2%	22%	54%	-1%	21%
K	3	8.7%	20%	25%	50%	80%	60%	100%
L	18	10.0%	3%	2%	27%	57%	4%	27%
M	7	7.9%	8%	14%	38%	68%	17%	44%
N	22	12.0%	20%	11%	36%	66%	24%	54%
Avg.	436	9.8%	7%	9%	33%	63%	21%	51%

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Communication from Philip S.Shaw,Esquire
regarding rent control

March 22, 1971

In City Council March 22, 1971

PLACED ON FILE

Paul E. Healy City Clerk