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Op-Ed: Measure ULA Transfer Tax Misguided and Poorly Planned

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Many of you may be aware of the recent Measure ULA initiative that passed. The measure, referred to as a “mansion tax,” imposes a new 4% transfer tax on property sales in the city of Los Angeles valued between $5 million and $10 million, with the transfer tax rising to 5.5% for sales of $10 million or higher. This tax is for all residential and commercial properties, with some exclusions for churches and nonprofits.

Last year this would have affected approximately $20 billion in properties—727 homes or condos on the residential side and 270 apartment building sales, and 150 commercial sales.

From the face of it, 4% or 5.5% additional transfer tax may not seem like much. However, the tax would be added to the city’s existing 0.45% transfer tax for an overall city transfer tax of 4.45% on sales from $5 million to $10 million, nearly 6% on sales above $10 million. It would come in addition to the county’s 0.11% transfer tax.

Backers argue the measure will raise as much as $1 billion annually from the people who can most afford it to create housing for the Angelenos who most need it. On the face of it, helping people experiencing homelessness is an admirable thing. One of Amalfi Estate’s six charity partners is The People Concern, and we have been supporting them for years with its excellent work.

The issue is not raising money but fixing a broken system and bureaucratic red tape; in 2016, Los Angeles voters approved Measure HHH, a 10-year, $1.2 billion bond measure to address the homelessness crisis by building 10,000 new affordable and permanent supportive housing units. It has been a failure after six years, with only 1,000 HHH-funded units completed, at an average cost of more than $500,000 each (almost double the cost they had predicted).

UCLA Lewis Center for Regional Policy Studies put out an 18-page white paper in September 2022, written by several UCLA, Occidental and USC professors, which formed the basis for ULA. This white paper had multiple erroneous assumptions and biases.

“There is no evidence that the tax would impact rents for commercial or residential tenants,” they stated. “In most cases, transfer taxes are paid by the seller, who will have no legal avenues to pass on costs to tenants in a building which they no longer own.”

Additionally, this report cited multiple studies which show that rents are erroneously determined by the market, not taxes and fees: “Landlords already charge the most they can without losing tenants and facing vacant apartments/retail spaces—this will not change because of new transaction fees.”

The ULA white paper’s authors also stated the only people affected are large, wealthy corporations when the reality is most developers are small business owners. They will now find development projects outside the city of LA to avoid paying an additional 4 or 5.5%. This will mean substantial lost revenues for escrow officers, loan officers, title officers, Realtors, sub-contractors and many others.

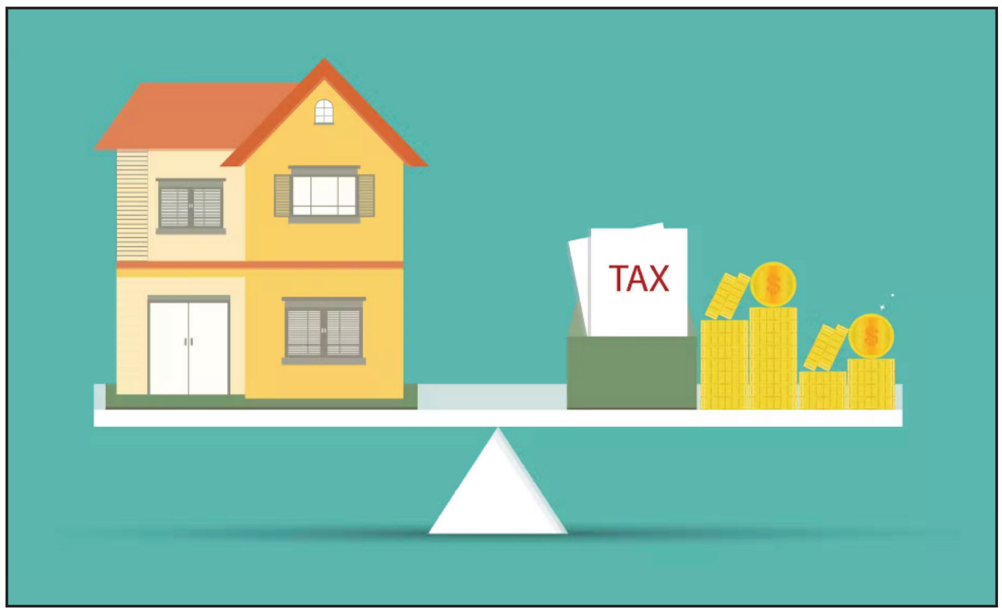

Photo courtesy of Amalfi Estates

“The ULA is a game changer for us,” one of our developer clients said. “We have been building and selling new SFRs in the Pacific Palisades/Brentwood area for many years ... We are selling houses in the $5 million to $6 million range. The new 4% tax on the selling price is equivalent to around 50% of our total project’s profit. Therefore, we stopped our tear down/lot purchases in the area and shifted our business to other directions.”

Another developer, Jeff Mironer with Province Town Estates, said, “As a small business owner, I develop high-end quality custom homes and apartment buildings. We employ up to 100 highly qualified professionals per project. ULA will hurt us tremendously. With the increased cost for permits (that was already implemented to help the homeless; over 500% increase in five years), high interest rates, materials, wages, insurance cost and shrinking supplies, ULA additional tax of 4 to 5% will cause losses for my company and small businesses like mine.”

The white paper authors stated that they found “minimal evidence that the tax would impact some for-profit new construction projects, but developers can adjust their business models to minimize the impact of the transfer tax, and revenues from Measure ULA will fund the construction of a much larger number of deed-restricted affordable homes. Real estate investors who buy to quickly resell—the harmful practice of ‘flipping’—may be more impacted, which we view as a bonus. However, the tax will significantly impact those with a short-term investment horizon who routinely ‘flip’ properties. This practice inflates housing prices and can cause evictions. If a side effect of this tax plan is to discourage flipping and speculation, that is a bonus.”

The single most significant source of campaign contributions to Measure ULA was construction unions because ULA mandates strict project labor agreements to only unionized workers and significantly inflates costs. And only existing affordable housing developers, many of whom are financial supporters of the measure. The *Los Angeles Daily News* called ULA a “special interest money grab.”

“Angelenos should ask themselves why these groups sponsored and paid to put Measure ULA on the ballot,” Jon Coupal, president of the Howard Jarvis Taxpayers Association, added. “The answer’s that affordable housing developers will benefit from the billions of taxpayer dollars.”

The college professors who wrote the white paper also reference San Francisco and Culver City passing similar measures with solid voter support. However, rather than using those cities, which spread the tax across all price ranges of properties, each having a different tax rate—San Francisco has six price ranges, each having a different tax rate, and Culver City has four price ranges of properties, each having a different tax rate—they chose the city of LA to only have only two price points and tax rates.

San Francisco passed Proposition W in the November 8, 2016, election and Proposition I in November 2020, establishing a marginal tax rate with six brackets:

- 0.6% for properties between $250,000 and $1 million
- 0.75% between $1 million and $5 million
- 2.25% between $5 million and $10 million
- 5.5% between $10 million and $25 million
- 6% for those over $25 million

So, the city of LA’s tax on $5 million to $10 million homes is 78% higher than San Francisco’s.

Similarly, Culver City passed Measure RE on November 3, 2020, establishing a marginal tax rate with four brackets:

- 0.45% on transactions under $1.5 million
- 1.5% between $1.5 million and $3 million
- 3% between $3 million and $10 million
- 4% for those $10 million and over

In addition to not equitably spreading the tax cost to all property’s price ranges, ULA targeted a couple of geographical areas substantially more.

For instance, Brentwood and the Palisades make up almost half—44%—of all the residential transactions sold over $5 million in the city of LA, with Bel Air being a distant third with 58 sales. In 2021 Brentwood had 118 homes sell from $5 million to $10 million, and 55 sell over $10 million, totaling 173 transactions worth $1,767,770,500.

The Palisades had the second most transactions with 105 sales from $5 million to $10 million and 38 over $10 million, totaling 143 transactions worth $1,345,472,226

The study also does not factor in the past five years; we have had the most significant appreciation rate in decades. We are currently going into a depreciating market, with home sales slowing considerably. As of mid-December 2022, Brentwood residential transactions are down 27% compared to last year and the Palisades is down 20%.

Santa Monica recently passed a similar measure of a 5.6% transfer tax on transactions over $8 million.

“It’s going to hold some sellers back, or at least cause them to think twice,” said Jordan Levine, an economist with the California Association of Realtors. “It undermines the broader growth in the housing market.”

Instead, the city—which over the last several years has received $1.2 billion in bonds for affordable housing from Proposition HHH—needs to spend the money it already has for affordable housing more wisely.

Additional concerns are the havoc this will have on comparable sales. Sales prices will be off, as sellers and buyers try and pay commissions or other closing costs directly or out of escrow. So a $6 million sale that would use a $5.5 million sale (that now sells for $4,999,000) will be affected. This, in turn, will lower future capital gains and property taxes collected. If the IRS can directly not collect the one-third that goes for capital gains on the difference of an average $5.5 million sale that sells for $5 million, they will lose $166,000 per transaction.

Additionally, the LA County Tax Assessor will miss out on the 1.25% tax on the $500,000 ($6,250) or $62,500 over 10 years.

I predict we will see a significant increase in homes selling for $4.95 million to $4,999,999 and $9.95 million to $9,999,999 compared to the previous year by sellers working to lower their transfer taxes.

The tax should be spread out over all price ranges and factored into what property values are doing. If someone buys a home for $6 million and a year later sells it for $5 million with this measure, they still need to pay a $200,000 tax on top of losing $1 million in equity.

With sales commission and other closing costs, a seller needs to sell for 10% more than they purchased to break even, which may work in an appreciating market, but we are going into a depreciating market.

While many predict an increase in properties coming on the market to try and sell by April 1, 2023, I don’t see that happening. Sellers typically do not want to come on before Christmas, and even if they have been able to come on the market in early January, it is doubtful they will be able to get into and close escrow by April 1, especially given the current slowing market. In addition, several sellers told me they were planning on selling their home, and now, due to this onerous tax, they have decided not to.

This poorly thought-out measure will have significant consequences on the economy that will be felt for years.

Anthony Marguleas is the founder of Amalfi Estates, and has sold $2 billion in properties and was selected by the Wall Street Journal *as one of the top 10 teams in the country out of two million agents. If you are thinking of buying a home or selling your own, contact Marguleas at 310-293-9280 or anthony@amalfiestates.com.*