Bloomberg

November 4, 2019

Pied-a-Terre Tax Revival Is Latest Threat to NYC's Luxury Market

State lawmakers to try again for levy on $5 million-plus deals, Developers argue additional costs would further dent demand

New York skyline from Central Park. Photographer: George Rose/Getty Images North America

New York's pied-a-terre tax, left for dead earlier this year, is back on the table and the real industry is gearing up for a fight.

Fresh off imposing an increased "mansion tax" and eliminating privacy protections favored by well-heeled buyers, state lawmakers are reviving efforts to tax second-home purchases of $5 million or more.

There's a growing desire among Democrats to address wealth inequality, and for them, the idea of slapping a annual tax on the uber rich who scoop up Manhattan apartments is long overdue. But for William Zeckendorf, whose firm built some of the city's most expensive condo towers, the proposal is the wrong idea at the wrong time.

He and other developers -- and the lawyers, appraisers and brokers who cater to millionaire clients -- argue that going after pied-a-terre buyers would further dent demand in the already struggling luxury real estate market. Thousands of new high-end condos are on their way, adding to a glut, and takers for them have all but disappeared. New rules that promote a political environment where buyers feel targeted would push even more of them away, Zeckendorf said.

"It's a sin tax," said Zeckendorf, whose projects include 520 Park Ave. and 15 Central Park West. "It's a tax meant to discourage economic behavior. And does the city really want to discourage pied-a-terre owners from coming to New York?"

Public coffers

New mansion and transfer tax surcharges, which took effect July 1, will raise an estimated $365 million annually, dedicated to shoring up the city's crumbling transportation system. But there are more public-spending needs, and it makes sense for people who can afford the most expensive apartments to help foot the tab, said State Senator Brad Hoylman, a Manhattan Democrat.

Hoylman has been trying to pass a pied-a-terre tax since the heady condo boom days of 2014, when high-end buyers from other countries thought nothing of sheltering their millions in the safe harbor of Manhattan apartments.

"They use our system of laws to protect their international investment in real estate, and I think there should be a premium on that," said Hoylman, who hasn't yet released a revised version of the bill. "This is a way to capture that purchasing power and use it for some common good."

'Class warfare'

New York's powerful real estate interests succeeded in derailing the pied-a-terre proposal in March, calling it "class warfare on the rich" and singling out the yearly levy, which had verbal support from Governor Andrew Cuomo, as one that would disembowel the property market.

The compromise was to raise closing costs: increasing the one-time "mansion tax" to as much as 3.9% on purchases of $2 million or more, and a separate transfer tax of 0.65% on $3 million-plus deals.

"People can get over a one-time thing," said Donna Olshan, president of luxury brokerage Olshan Realty Inc. "But the effect of annually raising your real estate taxes by a stratospheric amount will significantly devalue the property. It will kill the market."

The market is already moribund, pressured by the basic laws of supply and demand. The post-recession construction boom that flooded Manhattan with costly condos is still going strong, but the haven-seeking investors who just a few years ago plunked down record-shattering sums for lavish new penthouses are gone.

Supply Flood

New buildings with a combined 1,737 condos are expected to reach the market next year, according to an estimate by brokerage Core. Projects debuting in 2021 will have an additional 3,066 apartments.

With so much inventory chasing a very exclusive purchasing pool, wealthy buyers are in no rush to buy and are demanding discounts. So far this year, contracts for homes priced at $4 million or more -- including resales and co-ops -- are down 18%, Olshan Realty data show. Deals in that price range at new developments have plunged 36%.

In a robust market, where values are increasing, investors might be willing to accept an annual tax as a price to pay for the promise of fatter returns in the future, said Martin Jajan, an attorney who represents high-end Manhattan buyers, including many from overseas. But even the wealthy aren't going to throw away cash by paying a premium for a depreciating asset.

"The notion that they're just going to spend money because they want something and not consider the consequences or the risk is ridiculous," Olshan said.

Economist’s view

A levy targeting just the smallest and most well-off sliver of property owners won’t deter those who want the status of owning a place in Manhattan, according to James Parrott, the economist who wrote the 2014 report that spurred Hoylman’s legislative push for the pied-a-terre tax. And if sales do slip, he said, that’s not a catastrophe.

“The way a market economy adjusts to something like this is that the prices come down, and in the future, high-end developers will be more circumspect in what they build,” Parrott said.

For developers, the proposal is just another in a stream of attacks by politicians against their business. The new mansion and transfer taxes came after the federal government capped deductions for state and local levies to $10,000, increasing carrying costs for many homeowners in the region. And a new law makes publicly available the names of people who buy property under the guise of a shell company -- a change that may discourage purchases by celebrities or others concerned about their security, according to Jajan.

Sensing the political mood, and a populist spirit that’s not going to let up, Zeckendorf and other developers commissioned studies that suggest an annual pied-a-terre levy would be counterproductive. A decline in second-home purchases would mean fewer transfer-tax payments, fewer service jobs for people who cater to luxury buyers, and lower sales tax revenue. Details of the studies will be released later this month.

“We will demonstrate that this tax is a net loser,” Zeckendorf said. “It will cost them more revenue than it could ever generate.”