

As Chicago Transfer Tax Vote Looms, Similar Policies In LA And NYC Hint At What Could Come Next

The stage is set and the actors are warming up backstage as Chicago's commercial real estate industry awaits the imminent opening of the curtain on a decision that could reshape how business is done for the foreseeable future.

The battle over Chicago's proposed [real estate transfer tax](#) has been escalating for months. Key adversaries on both sides of the issue have been [pouring money into](#) trying to sway the city's voters by the time they head to the ballot box in March. But with much of CRE focused on the struggle for voters' hearts and minds, fewer are asking the question: What will happen to deal volume in an already struggling market if voters do approve the measure?

While it's impossible to predict the future, the impact of similar tax measures in Chicago's metropolitan counterparts of Los Angeles and New York City may offer insight into what could be coming down the pike. Los Angeles passed [Measure ULA](#) in November of 2022 and New York State updated its transfer tax law in 2019.

Those who witnessed the fallout of similar taxes in other metros say the Windy City could see a swift, sharp uptick in deals as key players race to get transactions done in the period between the passage of the measure and its implementation. That's what happened in both New York [and LA](#).

In the long term, though, the market will likely adapt to changed conditions, as New York's five-year experience with such a tax suggests.

"I understand the knee-jerk reaction of Chicagoans and the 'sky is falling mentality' that occurs any time the government imposes a new regulation, but I am confident that the CRE industry will adapt," said New York-based Adler & Stachenfeld partner YuhTyng Patka. "If there are any palpable effects on deal volume, it will be short-lived."

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Chicago's proposed tax would create a tiered system that reduces the burden on property sales below \$1M to 0.6% and ups the rate on sales larger than \$1M. The transfer tax on property sales between \$1M and \$1.5M would be 2%, while the transfer tax on property sales over \$1.5M would increase to 3%, quadrupling the current rate. The revenue the tax generates will go toward fighting homelessness.

Sales of nonresidential properties would account for about 75% of the increased tax revenue, about \$120M of the \$160M the tax would generate per year on average, [according to a University of Chicago analysis](#).

If voters approve the new system it would likely go into effect in January 2025, giving at least a nine-month window for dealmakers to execute transactions before the city implements the tax.

The Chicago market would likely see an increase in deals despite a sluggish capital environment, but that would simply reflect deals being pushed to complete earlier than they would have without the tax, said [Christopher Berry](#), a professor at [the University of Chicago](#)'s Harris School of Public Policy and faculty director of the Mansueto Institute for Urban Innovation.

“We should expect an uptick in deals between when it passes and when it's enacted,” Berry said. “I don't think we should read too much into it in terms of its signals about the health of the market.”

The most impacted deals would be those on the margins, Berry said.

“There's a deal that someone might have been on the fence about doing,” Berry said. “Those are the deals that you would expect to get pushed forward in time to get done before the tax goes into place.”

‘Running To Get Transactions Done’ In LA

If the Chicago market follows similar trends to Los Angeles, there could be an onslaught of deals in the period between passage and implementation. Voters in the City of Angels approved Measure ULA in November 2022, which adds a 4% tax on transactions of more than \$5M and a 5.5% tax on transactions over \$10M, to create a consistent revenue stream for affordable housing.

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In the first quarter of 2023, before the tax went into effect on April 1, commercial real estate sales on properties valued at over \$5M hit \$2.4B, [according to the San Fernando Valley Business Journal](#). In Q2, after the implementation of the tax, sales plunged to \$260M, the outlet reported.

There was a massive rush to close deals in the window between the approval of the Los Angeles tax and its implementation, said [Damon Juha](#), a real estate attorney at [Saul Ewing](#) in Los Angeles.

“You had people just running to get transactions done as quickly as possible knowing that they're going to be hitting this tax very, very soon,” Juha said. “We literally saw sellers trying to incentivize brokers, buyers [by] giving away cars, giving discounts or doing anything and everything to market their property as opposed to another one. “

Juha said he's seeing a smaller amount of deals in the wake of the tax, and the deals he is completing are larger because the increased cost can “make or break” the underwriting in a smaller deal.

The drop-off in completed deals after the implementation of the tax led to Los Angeles' city government missing its projections by a sizable margin.

Los Angeles' revenue estimate for the tax in its first year was \$672M. In its first month, it [netted just \\$3.6M](#), far below the roughly \$56M per month it needed to generate to hit its annual goal. By the end of 2023, the projected revenue from the tax was only \$150M, according to a [University of Southern California study](#) published in December.

The passage of LA's tax spurred some owner-users to pull the trigger on purchases they had been mulling for a while to avoid the additional cost post-implementation, Juha said. Other property owners tried to incentivize tenants to sign long-term leases to make transactions easier to underwrite, he said.

The national transaction environment across CRE is different in 2024 due to high interest rates, difficulty securing financing and slow sales throughout the country. Yet, the window between approval and implementation in Chicago could serve as an opportunity for investors that have been waiting in the wings to make their moves, Juha said.

“There's a lot of dry gunpowder sitting on the sidelines right now,” he said. “Now you have this sunset period if all this dry capital decides, ‘Hey, we've been sitting. We'd rather deploy the capital now than wait and have our underwriting affected because of this.’”

New Yorkers Adapted: 'Sometimes The Goalposts Move'

In 2019, New York legislators updated the state's 1% transfer tax law, which had been on the books since 1989, with a sliding scale of supplemental rates for any property purchases over \$2M. The scale charges buyers [up to 3.9%](#) of the cost of any property purchased for over \$25M.

The initial results mirrored Los Angeles — deal volume increased, then decreased precipitously. Overall sales for Q3 2019, after the tax was implemented, fell by 11.5% compared with Q3 2018, while sales for \$2M or more dropped by 31.5% to the lowest level since 2011, [The Wall Street Journal reported](#).

But a few years later, market activity had stabilized and even increased.

The city's real estate transfer tax netted about \$700M in 2019 and 2020, [according to the Illinois Answers Project](#). The proceeds fell to less than \$445M in 2021 before shooting up to almost \$982M in 2022.

While new regulations impact sales pricing, the longer-term impact indicates that, like New Yorkers, those in other cities might just learn to roll with the punches, adopting the tax as another cost of playing.

“Rules are constantly changing, sometimes the goalposts move in the middle of the game,” Patka said. “When you are doing business in New York City you have to be accustomed to adaptability in order to survive.”

In Chicago, the fight over the transfer tax has gotten more intense over the past month, with an industry group opposing the tax [filing a lawsuit](#) in early January aimed at knocking the measure off the March ballot. Both sides are out in full force with ground support and mailers, like one touting that the measure would force the wealthiest to “pay their fair share.”

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A mailer opposing the tax, created by the trade group [Illinois Realtors](#), blames the city for mismanaging federal funds allocated for housing and decries the measure as a “new property tax on homes, apartments, and even small businesses,” [according to Crain’s Chicago Business](#).

But the academic who has studied the issue extensively believes that, despite a possible short-lived flurry of sales and a lot of grumbling, the CRE professionals of 20 years from now will most likely just look at a passed tax as part of the price of operating in Chicago.

“In the long run, it will probably just become a cost of doing business as it has in New York, effectively,” Berry said. “It’s just in the short run, it can be very disruptive and particularly harmful to the people who are the current owners.”