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A Detailed Look at Los Angeles' New Mansion Tax, and Potential Ways to Avoid It if It Comes to Your City

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Los Angeles is known for being one of the most affluent areas in the country, but more recently, it has also struggled with its high rate of homelessness. To address concerns surrounding housing affordability and a widening wealth gap, the city proposed Measure "United to House LA" (ULA), which has become known as the "mansion tax." Voters approved this Measure in November of 2022; it went into effect on April 1, 2023.

The tax imposes a 4% tax on property sales above $5 million and a 5.5% tax on property sales above $10 million, to be paid by the property seller (for reference, the prior transfer tax was 0.45%). However, nonprofits, qualified affordable housing organizations, government agencies, and some others are exempt from the tax.

It is estimated the tax will impact about 4% of real estate sales and transfers in the city every year. According to the Los Angeles City Administrative Officer, it could generate between $600 million to $1.1 billion in revenue each year, depending on how many property transactions with values in the scope of the tax occur. There is a set aside of 8% of revenues for an inspector general and oversight staff, but the remaining 92% is earmarked to fund affordable housing in Los Angeles and homelessness prevention.

Most of the money is expected to come from transactions worth over $10 million. At that level, more of the sales come from multifamily and commercial properties rather than single-family homes, according to a September white paper by researchers from the University of California, Los Angeles, the University of Southern California, and Occidental College.

Of course, not everyone is happy about this new tax. Many critics believe it will increase housing prices and create more bureaucracy. Real estate agent Josh Altman thinks it will be the most brutal hit to the real estate market since the 2007-2008 housing market crash.

The tax went into effect on April 1, 2023, just five months after being approved by voters. The tax caused many sellers to frantically slash their home's sale price in early 2023 to sell their property before the tax went into effect.

Since the Measure is still very new, its application has yet to be seen. However, there may be some ways for individuals to avoid such a tax, especially since it is a documentary transfer tax imposed on the sale of a single real property interest.

One potential option is for spouses or business partners to take title to their property as tenants in common, allowing each tenant to list their interest for half the price of the entire property. Assuming their half interest is less than $5 million, this would presumably allow the sales to stay under the $5 million threshold that triggers the tax.

Similarly, a seller might be able to split their property into different parts and sell it as smaller, less expensive parts.

Another option may be to transfer the property to multiple trusts. The sub-trusts or beneficiaries might be able to sell their interests for under the $5 million threshold and as part of a larger sale.

Moreover, a seller may be able to sell removable improvements to the land, separate and apart from the sale of the land, to reduce the sale price of the real property that is subject to the new tax.

Of course, it is essential to consult with an attorney regarding personalized advice and recommendations regarding the application of this new tax.

While the "mansion tax" only applies to property in Los Angeles, residents in other California cities should take note. The Measure could be used as a model by other cities, as a relatively simple way to increase taxes on wealthy individuals, despite the state's wide-ranging restrictions on tax increases.

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