A look at the 2021 Hudson Valley apartment market

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With New York's COVID-19 related restrictions lifted the real estate industry has returned to normal operations and the economy is recovering quickly from the COVID-19 shutdowns. Risks going forward in 2022 for the Hudson Valley apartment market include several proposed changes that negatively impact the tax treatment of income in the multifamily industry that will have a large effect on future investment decisions.

Abolishing the 1031 tax deferred exchange is proposed as a means of raising government revenue by capturing the capital gains tax on real estate investment sales at the time of sale instead of allowing the closing proceeds to be used tax free as the equity in the purchase of a new property; many apartment complex investment sale contracts are contingent on the sale of a property currently owned by the buyer to provide the down payment in an exchange. This issue has received outsize coverage in the real estate press but is of extreme importance to the real estate investment business. The taxes are not forgiven as they are all ultimately due when the property is sold later in a taxable sale. Currently there is a very liquid market for the sale of multifamily properties and other investment real estate supported by investors continually looking to improve and expand their portfolios and this level of activity has lifted values for those looking to sell, retire, or otherwise exit the market. Expect apartment sales to slow until the market figures out the new pricing needed to accommodate buyers who will have on average a smaller down payment if the 1031 exchange is eliminated and now looking to pay a reduced price.

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In concert with the elimination of the 1031 tax deferred exchange, the plan to eliminate the stepped-up basis at death would require people to pay taxes on the appreciation of unsold assets when they die as part of the settlement of their estates, a problem for those looking to pass on their apartment portfolios to their heirs. The market here is majority owned by individual owners and management companies. Long-term holdings like real estate investment property would have to be sold on short notice to generate funds for inheritance taxes if they can't be found elsewhere in the estate. Lower than expected sale prices can result and some may pass on real estate investments to begin with. Also unclear, is whether carried interest will continue to be taxed as a capital gain or as ordinary income. Managing partners in an LLC receive a stake of the proceeds at sale in exchange for their time, expertise, and risk taking in setting up the LLC and managing the property through sale. Ordinary income tax rates can be far higher than capital gains rates and higher taxes on their efforts will lead to fewer partnerships formed and competing in the market.

The New York eviction moratorium has been extended through January 15th next year for those tenants with unpaid rent. The overwhelming majority of tenants have paid on time but for those with missed rent payments in the last year due to COVID-19 starting June 1st New York State is making \$2.7 billion in emergency rental assistance available; the New York State Emergency Rental Assistance Program will provide assistance with up to 12 months of past-due rent, three months of prospective rental assistance and 12 months of utility arrears payment. The effect will be to bring those in arrears current and prevent a crush of new cases in the eviction courts and compensate multifamily owners for the financial losses of the past year. The payment is made to the landlord but the onus is on the tenant to apply. There is immediate demand for vacant apartments for any tenants who do leave.

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