

# 4Q12 Investment Sales Activity Will Be Epic

Thanks to capital gains tax increases, expect sellers to scramble by year's end

Put your space helmet on, strap yourself in and get ready for what is sure to be one of the wildest rides in the history of New York City's commercial real estate investment sales markets.

Yes, the fourth quarter of 2012 is likely to go down as one of the most active periods in the last quarter-century for property sales in the Big Apple.

Changes in tax law often spark activity as market participants rush to beat the deadline, as we saw most notably in 1986.

The looming threat of substantial capital gains tax increases next year has the market poised to see a huge spike in transaction volume. We began alerting clients at Massey Knakal to this possibility back in January, as it was clear at that time that the capital gains

rate, which is an integral variable in determining the after-tax proceeds of most commercial real estate sales, was vulnerable to change. Record deficits, lower-than-expected tax revenue and an economic recovery that is moving at a snail's pace have members of Congress scratching their heads for solutions.



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With government spending as a percentage of GDP extraordinarily high and revenue as a percentage of GDP unusually low, a balanced Simpson-Bowles type approach would seem to be appropriate, but the inertia exhibited in Washington leaves little consensus thus far. On the revenue side, the capital gains rate is most vulnerable, given that it is broadly considered to be a "rich person's tax" by those who favor raising revenue.

We observed the same political

rhetoric in 2010 as we approached the midterm elections. It created a dynamic in which property owners, who were considering a sale of their property in the short-term, elected to sell prior to the year's end, fearing that a capital gains tax increase in 2011 would erode their after-tax proceeds. In October 2010, I wrote that the investment sales brokers in the city should "clear their calendars" and suggested they "don't plan on taking much vacation time in December," as it was clear that 4Q10 would see a whirlwind of activity. And it happened. As a result, of the approximately \$14.5 billion of Gotham's 2010 total sales volume, about \$5.4 billion occurred in 4Q10 alone. This was, at the time, the highest quarterly total in 10 quarters.

This year's threat is even more likely to become reality, as Congress would have to take action—not to make the rate rise, as it would have had to in 2011, but to keep the rate down. As

we have seen recently, getting Congress to do anything would be surprising. To the extent it doesn't take action, the Bush tax cuts will sunset on December 31, automatically raising the capital gains rate from 15 percent to 20 percent. On January 1, the component of Obamacare that implements a covert 3.8 percent increase in the capital gains rate kicks in, meaning that, without government action, the rate will rise to 23.8 percent beginning in the new year, a nearly 60 percent increase. And this assumes that, if the president is re-elected, he does not fulfill his quest to initiate a minimum 30 percent tax rate, which is likely not to include the health care surcharge. That would bring the rate to 33.8 percent.

The impact on after-tax proceeds from sales would be tangible. At Massey Knakal, we have already closed on the sale of dozens of properties, whose sellers were specifically prompted to

sell in 2012 because of the potential increase in the capital gains rate. Additionally, we have an even greater number of properties presently under contract for sale that are due to close in 4Q12, which will save our clients tens of millions of dollars if the increase does come to pass.

Participants in New York City's investment sales market can look forward to extremely robust activity this fall. It would not be surprising to see more than 1,000 buildings sold and more than \$10 billion in sales in the fourth quarter. Both of these totals would be seen for the first time since 2007.

Three, Two, One ...  
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