Transfer Taxes
Who Owes What and How Much

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I. **What are realty transfer taxes?**

Realty transfer taxes are state and local taxes assessed on real property when ownership of the real property is transferred or exchanged between two different persons or entities. Some form of realty transfer tax is applied in a majority of jurisdictions and may be assessed on the buyer or seller, though both are often jointly and severally liable.

   a. **Real Property Taxes vs. Realty Transfer Taxes**

      Real property taxes (sometimes referred to as “ad valorem taxes”) are a tax based on the value of real property. These taxes are assessed on an annual basis regardless of ownership.

      Realty transfer taxes are only applied when ownership of the real property is transferred or exchanged between two different persons or entities.

   b. **What clients are affected by realty transfer taxes?**

      Any client who owns, leases or subleases real property may be subject to realty transfer taxes. It does not only apply to real estate clients.

   c. **When has there been a change of ownership of real property?**

      The answer to the question of when ownership of real property has changed can be very different from jurisdiction to jurisdiction. A realty transfer tax is usually triggered upon the occurrence of one of three events.

      - First, and the most common, is when real property is sold directly from one person or entity to another. This is usually evidenced by a new deed being recorded at the county assessor/recorder’s office.

      - The second, which is more complex, occurs upon the transfer of a “controlling interest” of real property. A deed is not generally recorded as a result of this type of transaction.

      - The third is when debtors are in default and a creditor utilizes a remedy such as foreclosure or deed in lieu of foreclosure. (This generally results in either the transfer of a controlling interest or a deed recordation).

II. **Deed Recordation**

Realty transfer taxes are most commonly applied when a deed is recorded at the local assessor/recorder’s office. The general rule is that a “deed” is defined as an instrument which conveys legal title from one person to another. Consequently, the mere creation of a contract to sell real property would not be subject to realty transfer tax since a mere contract does not convey legal title. (The sale or assignment of a contract to sell real property may trigger a transfer tax in New York State).

   a. **Basis of Realty Transfer Tax—General Rule**

      The basis of the realty transfer tax due is the price actually paid or required to be paid for the real property (or economic interest therein), plus the amount of any pre-
existing mortgages (whether or not the underlying indebtedness is assumed), liens and encumbrances, whether or not expressed in the deed or instrument to be assumed by the grantee. It also includes the cancellation or discharge of an indebtedness or obligation.

III. Controlling Interest

Realty transfer taxes are also commonly applied when a “controlling interest” in real property is transferred. This is different than the imposition of the tax on a deed recordation. Upon the occurrence of a transfer of a controlling interest in real property, no deed is generally recorded since the legal owner of the property does not change. Controlling interest transfers are more complex because it is more difficult to determine when the control of the real property has been transferred.

A controlling interest transfer occurs in New York (State and City) when a controlling interest in an entity (which owns real property) is transferred to a separate person or entity. In order to consider whether a transfer of a controlling interest has occurred, it is necessary to understand the difference between “legal” ownership and “beneficial” ownership.

- Legal ownership is easy to define—it is the legal owner of the real property, or even more simply, usually it is the entity or person whose name is recorded at the local assessor/recorder’s office as the owner of the property assuming the legal owner is not the nominee.

- Beneficial ownership is more complex. While it may include legal ownership, it does not need to—but it must include a beneficial right to receive a profit or some form of income or remuneration from the real property—present or future.

A. Legal Ownership vs. Beneficial Ownership

(i) Legal Ownership

See Example 1. If you were to go to the local assessor/recorder’s office to see the legal owner of the real property, only the name, “DE L.P.” would be shown. This is because all of the legal incidences of ownership are held by DE L.P.

a. When will a transfer tax be due when legal ownership changes?

In jurisdictions where a realty transfer tax is applied, a transfer tax will be due when DE L.P. sells the real property or a portion of the real property to a separate and distinct person or legal entity.

(ii) Beneficial Ownership

See Example 1. As you can see, DE L.P. is a partnership (a “flow-through” entity used as a conduit so that all of the entity’s tax attributes (such as profits and losses) are allocated and distributed to each partner per the partnership agreement). Consequently, DE L.P.’s two partners, Adam Smith and LP each indirectly receive income from the underlying real property. Based on these facts, the partners, Adam Smith and LP, while not legal owners of the property, are considered “beneficial owners” of the underlying real property.
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Note in Example 1 that Adam Smith and LP each own 50% of DE L.P. which in turn owns the real property.

   a.  When will a transfer tax be due upon the transfer of a controlling interest?

In order to possess a controlling interest in real property, one must have a beneficial interest. To determine when a controlling interest is transferred, it is necessary to look at each jurisdiction’s law and regulations. The general rule in the tri-state area is that realty transfer tax will be due when a 50% or more beneficial interest changes hands in New York State and New York City or Connecticut, and when more than a 50% beneficial interest changes hands in New Jersey.

Based on these facts, to see when a controlling interest is transferred, it is necessary to look through the legal owner—regardless of whether or not it is a flow-through entity (such as a partnership or limited liability company) or a corporation.

Look again at Example 1. If Adam Smith or LP were to sell their entire partnership interest to another person or entity, realty transfer tax would be due in those jurisdictions, such as New York State and New York City that impose a tax on the transfer of a controlling interest in real property (and define a controlling interest as 50% or more).

B. “Controlling Interest” in New York

Take a look at the way New York State and New York City define controlling interest in TABLE 1 below:

<table>
<thead>
<tr>
<th>Entity/Interest Type</th>
<th>New York State</th>
<th>New York City</th>
</tr>
</thead>
<tbody>
<tr>
<td>Controlling Interest (for a corporation)</td>
<td>50% or more of the total combined voting power of all classes of stock in such corporation, [or 50% or more of the capital, profits or beneficial interest in such voting stock of such corporation]</td>
<td>50% or more of the total combined voting power of all classes of stock in such corporation, [or 50% or more of the total fair market value of all classes of stock of such corporation]</td>
</tr>
<tr>
<td>Controlling Interest (for a partnership, association, trust or other entity)</td>
<td>50% or more of the capital, profits, or beneficial interest in such partnership, association, trust or other entity.</td>
<td>50% or more of the capital, profits, or beneficial interest in such partnership, association, trust or other entity.</td>
</tr>
</tbody>
</table>
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Definition of Controlling Interest: New York City vs. New York State

1. Partnerships and Other Unincorporated Entities

See TABLE 1 above. New York State and New York City both have the same definition for a controlling interest in a partnership, association, trust or other entity the same (50% or more of the entity’s capital, profits or beneficial interest).

- While a partnership’s capital and profits can easily be explained, the term “beneficial interest” is not defined.
- It appears “beneficial interest” does not mean capital and profits, but some other interest. This term is likely deliberately undefined but remains an important question mark when planning these types of transactions. See Exhibit A: In The Matter of the Petition of Viacom, Inc. DTA No. 819591, Tax Appeals Tribunal, May 3, 2007 for a discussion on the meaning of “beneficial ownership” and a change in substance vs. a mere change in form.

2. Corporations

See TABLE 1 above. New York State and New York City have some different interpretations of the definition of controlling interest for a corporation.

While both New York City and New York State agree that a transfer or acquisition of 50% or more of the total combined voting power of all classes of stock in such corporation will be deemed a transfer of a controlling interest, each jurisdiction has distinct differences.

- First, New York City also considers the transfer or acquisition of 50% or more of the total fair market value of all classes of stock of such corporation a transfer of a controlling interest. Therefore, New York City considers non-voting stock, such as “preferred” stock (which has an economic value) to trigger the realty transfer tax when the fair market value is 50% or more of all classes of stock of such corporation.

- Second, New York State, unlike New York City, also considers (just like in a partnership) the transfer of 50% or more of the capital, profits or beneficial interest in such voting stock of such corporation.

In contrast, New York State does not appear to consider non-voting stock when determining if a controlling interest transfer has occurred. In the alternative, New York State uses the terms, “or 50% or more of the capital, profits or beneficial interest in such voting stock of such corporation.”

See Example 2

To be subject to the realty transfer tax in New York, it is not enough to acquire a controlling interest in an entity that owns real property. The entity within which you acquire a controlling interest must itself own at least a 50% interest in real property in New York.
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See Example 3

Now Adam Smith owns an 80% interest in DE L.P. and LP owns a 20% interest in DE L.P. Assume another person or entity acquires 99% of LP. In this instance, no transfer tax would be due because a controlling interest in real property has not been transferred—only a controlling interest in an entity (which does not own a controlling interest in real property within New York).

See Example 4 and Exhibit B and Exhibit C

Exhibit B: 595 Investors Limited Partnership v. Biderman, 140 Misc. 2d 441 (Sup. Ct. N.Y. County 1988) and Exhibit C: In the Matter of Corwood Enterprises, Inc., Tax Appeals Tribunal, June 2, 2006, TAT (E) 00-39 (RP), ET AL.

3. What is a Partnership Interest/What is a Transfer?


4. Determining the Transfer Tax Base With the Transfer of a Controlling Interest in an Entity with an Interest in Real Property

New York City: An apportionment of the consideration between the real property (or an interest therein) and the other assets, which in the opinion of the Commissioner of Finance represents an apportionment made in good faith, will be accepted by the Department. If no apportionment of the consideration for the real property (or interest therein) and the other assets has been made, or if, in the opinion of the Commissioner of Finance, the apportionment of the consideration does not represent an apportionment made in good faith, then the consideration for the real property (or interest therein) shall be calculated by multiplying total consideration by the following ratio:

Fair market value of the real property (or interest therein) owned by the entity being transferred.

Fair market value of all assets owned by the entity, including the real property (or interest therein)

New York State: the fair market value of the real property or interest therein, apportioned based on the percentage of the ownership interest transferred or acquired in the entity.

C. Aggregation

Realty transfer tax laws, which assess such a tax on the transfer of a controlling interest in real property, usually are drafted (such as New York State and New York City) to prevent persons or entities from avoiding the realty transfer tax when the transfer of a controlling interest in real property is accomplished by bifurcating transactions to avoid the sale or acquisition of a controlling interest in one transaction.

- An example would be transferring a 49.9% interest on one day, and then transferring a 0.1% interest the next day.
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These rules are called the “aggregation” rules. These rules provide that a transfer of a controlling interest made by one or several persons, or in one or several “related” transfers, is subject to the realty transfer tax.

1. New York City

In New York City, transfers made within a three-year period are presumed to be related and are aggregated, unless the grantor(s) or grantee(s) can rebut this presumption by proving that the transfers are unrelated. Note, since the transfers are presumed to be related, the taxpayer has the burden of proof to show they are unrelated. The New York City rules further provide that transfers pursuant to a plan to either transfer or acquire a controlling interest are deemed to be related. There are several illustrations to help us interpret how the aggregation rules will be applied:

Illustration (i)— Rule 19 RCNY 23-02, Controlling Interest

Two transferors, “acting in concert” sell their interests, aggregating more than 50%. Notwithstanding that the sales are four years apart, the transfers are related.

Illustration (ii)— Rule 19 RCNY 23-02, Controlling Interest

Each of two one-third shareholders sells his entire interest to one purchaser, within a three-year period. These transfers are presumed to be related because they were within a three-year period. As the gross consideration in this Illustration exceeded $25,000, “the transfer tax will apply….”

NOTE the above transfers are “presumed related”

Illustration (iii)— Rule 19 RCNY 23-02, Controlling Interest

A shareholder transfers 20% to one purchaser and, within three years, transfers 30% to another purchaser. Because the shareholder has transferred a controlling economic interest in real property within a three-year period, the transfer tax will apply to both sales.

Here unlike the previous illustration, there is no mention of presumption of taxability, just a statement that such transaction is taxable.

Illustration (iv)— Rule 19 RCNY 23-02, Controlling Interest

A shareholder transfers 20% to one purchaser and, within three years, transfers 30% to another purchaser.

This illustration is the same as above, however, now the City states that the transfers are “presumed to be related”.

Illustration (v)— Rule 19 RCNY 23-02, Controlling Interest

X Corporation owns real property in New York City. A owns 100% of the stock in X. In year 1, A transfers 20% of X to B. In year 3, A transfers 10% of X to C. In year 5, A transfers 20% of X to D.
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In this illustration, the rules say no transfer of a controlling economic interest in X has occurred within three years and the transfers are not presumed to be related.

Illustration (viii)—Rule 19 RCNY 23-02, Controlling Interest

X Corporation owns real property in New York City. A owns 4% of the outstanding stock of X. B, C, D, E, F, G, H, and I each own 12% of the outstanding stock of X. J enters into agreements with A, B, C, D, and E to purchase their interests in X over a five year period.

All of the transfers to J are related and, therefore, will be aggregated. A transfer tax will be due and transfer tax returns will be required to be filed for each transfer once a 50% interest in X, in the aggregate, has been transferred.

Illustration (xi)—Rule 19 RCNY 23-02, Controlling Interest

X Corporation owns real property in New York City worth $3,000,000. A, B and C each own 1/3 of X and are unrelated. In 1987, A loses a lawsuit related to her business and transfers her 1/3 interest in X in satisfaction of a $1,000,000 judgment. In 1989, pursuant to a separation agreement, B transfers his 1/3 interest in X to his spouse.

The transfers by A and B will not be aggregated because the transfers are not related. Thus, no tax is due. This is the one illustration which shows that transfers can be unrelated—though the “presumption” is not discussed here, presumably the facts simply show the transfers were unrelated so there was no need to mention the presumption.

See Exhibit E: New York City Finance Letter Ruling (“FLR”) 129-RP-10/88,10/05/1988

In this Finance Letter Ruling (“FLR”), Corporation X (“X”) owned real property in New York City. X was owned by Y (50.7%) and his son Z (49.3%). In December, 1986, V transferred .4% of X stock to his two daughters (Z’s sisters). In January, 1987, Y transferred another .4% interest in X to his two daughters. Thereafter, Y owned 49.9% of X, Z owned 49.3% of X and Y’s daughters owned .8% of X. At the time of these two transfers, Y was in good health. Y entered the hospital on December 17, 1987, for prostate surgery, which was successful. However, Y was readmitted to the hospital on January 6, 1988, when a cancerous tumor was discovered on Y’s spine. Y died on February 3, 1988, and, pursuant to the X shareholders’ agreement, X must redeem Y’s shares from his estate for cash. After the redemption, Z owned 98 .5% of X and Y’s daughters owned 1.5%.

Based on the facts, a controlling interest in X was transferred within a three-year period. This would seem to give rise to the presumption of taxability.

Illustration (xii) Illustration (xi)—Rule 19 RCNY 23-02, Aggregation

A owns 100% of the stock of X Corporation. X owns real property in New York City. A sells 30% of X to B. One year after this sale, B sells this 30% interest in X to C. Resales of the same interests are not aggregated. Thus, no tax is due.

2. New York State

New York State’s aggregation rules (see 20 NYCRR § 575.6(d)) provide that transfers will be per se aggregated and transfer tax will be due when a person or group of persons acting in concert
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transfer or acquire a controlling interest in an entity which owns an interest in real property. To determine if the grantor(s) or grantee(s) are “acting in concert”:

- Persons are deemed to be acting in concert when they have a relationship such that one person influences or controls the actions of another (such as a parent corporation and wholly-owned subsidiary that each sell or purchase a 25% percent interest).

- Where the individuals or entities are not commonly controlled or owned, persons will be treated as acting in concert when the unity with which the sellers or purchasers have negotiated and will consummate the transfer of ownership interests indicates they are acting as a single entity. However, if the individuals are not commonly controlled or owned, persons can show the transactions are completely independent of each other.

- In order to prove the transactions are independent of each other, it is necessary to show that the grantor(s) and grantee(s) are not “acting in concert” to consummate the transaction.

- In order to show a transaction is independent, each grantor selling and each grantee buying should be able to show each person is buying without regard to the identity of the other grantors or grantees, and then the transfers may be treated independently. The grantors or grantees may be required to provide a sworn statement that their transfers or acquisitions are independent of each other.


NYS Illustration 1: A owns 100 percent of X Corporation, the only asset of which is real property. B, C, D and E as a group, negotiate to buy all of A’s interest with B, C, D and E each buying 25 percent of A’s interest. The contracts of B, C, D and E are identical and the purchases are to occur simultaneously. B, C, D and E have also negotiated an agreement binding themselves to a course of action with respect to the acquisition of X corporation and the terms of a shareholders’ agreement which would govern their relationship as owners of X corporation. The acquisitions by B, C, D and E would be treated as a single acquisition which is subject to the real estate transfer tax.

NYS Illustration 2: Partnership X, which owns real property, is composed of partners A and B, each having a 50 percent partnership interest. In November, 1989, A and B, decided to raise more capital by agreeing that they each will sell a percentage of their partnership interest. On November 20, 1989, A and B each sold a 12 1/2 percent partner-ship interest to C. On October 11, 1990, A and B each sold a 15 percent partnership interest to D. Since A and B have acted in concert and transferred a 55 percent interest (12 1/2 + 12 1/2 + 15 + 15) within a three year period (see subdivision (d) of this section for the three year aggregation rule), the transfers are subject to the real estate transfer tax. A and B would each owe transfer tax on the respective transfers of their 12 1/2 percent and 15 percent interests.

3. “Creeping” Aggregation

If an investor buys into a partnership which holds a direct or indirect interest in real property, and other sales or acquisitions have taken place before that partner was admitted, this transaction
could be aggregated with previous transactions and subject the partnership to realty transfer tax
upon the admittance of this partner or a future partner within a three-year time period. Very fact
intensive.

IV. Transfers During Bankruptcy

A. New York City

1 - Exemptions

(i) Transfers made pursuant to a confirmed plan of reorganization as provided under 11
U.S.C. §1146(c) (chapter 11 bankruptcy) are specifically exempt. 19 RCNY 23-03(j)(8).

   a. This includes any transfer of an economic interest in real property necessary to
   effect reorganization. What if the entity has only one asset—the real estate? Will a transfer
   pursuant to Chapter 11 be respected under this circumstance?

(ii) Specifically exempted is the transfer of a deed from the bankrupt party to the trustee for
any type of bankruptcy (including Chapter 7 and 13). 19 RCNY 23-03(j)(5) and (j)(6).

(iii) A deed executed by a debtor conveying real property to an assignee for the benefit of his
creditors; however, when the assignee conveys such property to a creditor or sells it to any other
person, the deed by him is taxable if the consideration exceeds $25,000. 19 RCNY 23-03(j)(5).

   a. Who will pay the transfer tax?

(iv) Conveyance to a receiver of realty included in the receivership assets, and reconveyance
of such realty upon termination of the receivership. 19 RCNY 23-03(j)(6).

(v) Finance Letter Ruling 96-4675: Transfer from the bankrupt insurance company to a trust
was not subject to the tax because the trust was created to facilitate the liquidation of the
taxpayer’s real estate assets fulfilling a function comparable to that of a receiver (see 19 RCNY
23-03(j)(6)) and because the trust acquired mere legal title to the assets, with record title
remaining in the taxpayer.

2 - What is Taxable?

(i) Transfers made pursuant to bankruptcy do trigger the transfer tax (only Ch 11 is exempt,
as discussed). The tax is triggered when the property passes from the bankrupt party or the
trustee to the third party buyer (not when trustee takes property). (FLR: 034808-021) (FLR 93-
128).

(ii) Finance Letter Ruling 96-4675 seems to make clear that transfers pursuant to any
bankruptcy except Chapter 11 reorganization are subject to the transfer tax without regard to
whether the proceeds of any liquidation are paid over to creditors.

I. Deed in Lieu of Foreclosure - NYC

(1) A conveyance by a defaulting mortgagor to the mortgagee. The tax is computed
on the amount of the outstanding mortgage debt and unpaid accrued interest. The tax applies
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without regard to whether the mortgagor is personally liable for the mortgage debt or whether the mortgage is cancelled of record. 19 RCNY 23-03(c) (4) (1).

a. NYC Corporation Counsel Opinion dated July 28, 1983 confirms that a deed given by a mortgagor to a mortgage in lieu of foreclosure of a non-recourse mortgage is subject to the transfer tax (rephrasing the last line of the statute paraphrased in 1)).

<table>
<thead>
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<th>Deed in Lieu</th>
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</thead>
<tbody>
<tr>
<td><strong>Type of Debt</strong></td>
</tr>
</tbody>
</table>
| Nonrecourse or Recourse | Mortgagee or Third Party | (1) Unpaid mortgage Debt +
| | | (2) Accrued Interest |

**For NYC purposes the tax is always computed on outstanding mortgage debt and unpaid accrued interest.**

The tax applies without regard to whether the mortgagor is personally liable for the mortgage debt or whether the mortgage is cancelled of record.

II. Foreclosure - NYC

(1) Deeds given by referees, receivers, sheriffs, etc., for realty sold under foreclosure or execution are also subject to the tax. The tax is computed on the amount bid for the property, senior liens not canceled by the sale, and advertising expenses, taxes and other costs paid by the purchaser, whether the purchaser is the mortgagee, judgment creditor, or other person. 19 RCNY 23-03(d)(2).

<table>
<thead>
<tr>
<th>Foreclosure</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Type of Debt</strong></td>
</tr>
</tbody>
</table>
| Nonrecourse or Recourse | Anyone | (1) Amount bid for the property+
| | | (2) Senior liens not cancelled by the sale+
| | | (3) Other expenses paid (such as advertising expenses, taxes and other costs paid by the purchaser, whether the purchaser is the mortgagee, judgment creditor, or other person).

III. Mezzanine Debt - NYC

Subordinate loans on real estate, secured by pledges of equity interest in the owners of the property.
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### Mezzanine Assignment in Lieu

<table>
<thead>
<tr>
<th>Type of Debt</th>
<th>The Grantee Is</th>
<th>NYC Tax Base</th>
</tr>
</thead>
</table>
| Mezzanine    | Anyone         | (1) Unpaid balance due on the mezzanine loan (no FMV cap)  
               |                | (2) Transfer Tax paid by transferee |

### Mezzanine Foreclosure

<table>
<thead>
<tr>
<th>Type of Debt</th>
<th>The Grantee Is...</th>
<th>NYC Tax Base</th>
</tr>
</thead>
</table>
| Mezzanine    | Anyone            | (1) Amount bid for the property  
               |                    | (2) Senior liens on the equity interest—including the unpaid balance of any more senior mezzanine loans not cancelled by the sale  
               |                    | (3) Any unpaid balance of any outstanding mortgage on the real property +  
               |                    | (4) Advertising expenses, taxes and other costs paid by the purchaser, whether the purchaser is the mortgagee, judgment creditor, or other person. |
B. New York State

1 - Exemptions

(i) Sec. 1405 of the Tax Law gives a blanket exemption for conveyances made pursuant to the Federal Bankruptcy Act. This covers both the transfer to a bankruptcy trustee as well as a transfer from the debtor or trustee to creditors or presumably even third-party purchasers as long as it is part of the plan. It does not matter if the conveyance is pursuant to a chapter 7, 11, or 13 but must be pursuant to an official approved plan.

2 – What is Taxable?

I. Deed in Lieu of Foreclosure - NYS

- A transfer in lieu of foreclosure is taxed. The definition of a conveyance covers the transfer or transfers of any interest in real property by any method including: mortgage foreclosure, transfer in lieu of foreclosure. Sec. 1401(e), Tax Law.

<table>
<thead>
<tr>
<th>Type of Debt</th>
<th>The Grantee Is</th>
<th>NYS Tax Base</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-recourse</td>
<td>Mortgagee</td>
<td>(1) Unpaid balance of debt secured by mortgage</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(2) Any other encumbrances remaining after conveyance</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(3) Any other consideration paid for the real property.*</td>
</tr>
<tr>
<td></td>
<td></td>
<td>*State or local transfer taxes are not included provided the grantee has not assumed the liability for the payment of such taxes or has not released a right to seek recovery of the payment from the grantor</td>
</tr>
<tr>
<td>Recourse*</td>
<td>Mortgagee</td>
<td>FMV + # (3) below if (1) and (2) exceed the FMV as of the date of conveyance:</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(1) Any unpaid balance of debt secured by the mortgage +</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(2) Any other encumbrances remaining after conveyance +</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(3) Any other consideration paid for the real property.*</td>
</tr>
<tr>
<td></td>
<td></td>
<td>*State or local transfer taxes are not includable provided the grantee has not assumed the liability for the payment of such taxes or has not released a right to seek recovery of the payment from the grantor</td>
</tr>
</tbody>
</table>

*A debt is recourse to the extent that, as of the date of conveyance, the grantor or a person related to the grantor including any guarantor, bears the economic risk of loss for the debt beyond any loss attributable to the value of the property securing the debt.

NOTE: Debt that was originally nonrecourse which was converted to recourse will be examined for integrated steps/part of plan to reduce transfer tax.
NEW YORK CITY AND NEW YORK STATE REALTY TRANSFER TAXES

PROBLEM 1: Bank A made a nonrecourse loan of $10 million to individual X secured by a mortgage on New York State real property owned by X. X also provided a personal recourse guarantee of the last $1 million of the debt, that is, if the value of the mortgaged real property decreased to less than $10 million X would be obligated to pay the difference between $10 million and the value of the mortgaged real property to Bank A up to a maximum amount of $1 million. X defaulted on the loan. The real property was conveyed to Bank A in lieu of foreclosure and, at the time of the conveyance, the real property had a fair market value of $8 million. As a result of the conveyance the $9 million nonrecourse component of the loan is discharged. Simultaneously, Bank A discharged X from any obligation under the personal guarantee. The consideration for the conveyance consists only of the $9 million nonrecourse component of the loan that was discharged, as no part of the excess $1 million personal obligation can be satisfied by the conveyance of the real property.

PROBLEM 2: Same facts as Example 4, except instead of the personal guarantee on the last $1 million, X guaranteed the first $1 million i.e., X would be liable for any deficiency only if the mortgaged real property was worth less than $1 million. Since the FMV of the real property at the time of the conveyance was $8 million, there was no continuing recourse exposure to X, and therefore the consideration for the conveyance is equal to $10 million, which was the full amount of the nonrecourse indebtedness discharged as a result of the conveyance of the real property.

II. Foreclosure - NYS

<table>
<thead>
<tr>
<th>Foreclosure</th>
<th>The Grantee Is</th>
<th>NYS Tax Base</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Non-recourse</strong></td>
<td>Mortgagee</td>
<td><em>The higher of the following:</em></td>
</tr>
<tr>
<td></td>
<td></td>
<td>A. (1) Bid price +</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(2) Any other encumbrances remaining after conveyance, OR;</td>
</tr>
<tr>
<td></td>
<td></td>
<td>B. (1) The amount of judgment +</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(2) Any other encumbrances remaining after conveyance</td>
</tr>
<tr>
<td>*<em>Recourse</em></td>
<td>Mortgagee</td>
<td>FMV when the higher of such amount in A or B above exceeds FMV at the time of conveyance</td>
</tr>
<tr>
<td><strong>Nonrecourse or Recourse</strong></td>
<td>Unrelated to the Mortgagee</td>
<td>(1) The bid Price +</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(2) Any other encumbrances remaining after the conveyance</td>
</tr>
</tbody>
</table>

*A debt is recourse to the extent that, as of the date of conveyance, the grantor or a person related to the grantor including any guarantor, bears the economic risk of loss for the debt beyond any loss attributable to the value of the property securing the debt.*
NEW YORK CITY AND NEW YORK STATE REALTY TRANSFER TAXES

III. Mezzanine Debt - NYS

<table>
<thead>
<tr>
<th>Mezzanine Foreclosure/Assignment in Lieu</th>
<th>The Grantee Is</th>
<th>NYC Tax Base</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Type of Debt</strong></td>
<td><strong>Secured Party</strong></td>
<td><strong>The lesser of:</strong></td>
</tr>
<tr>
<td>Mezzanine</td>
<td></td>
<td>(1) The FMV of the real property multiplied by the percentage in the entity being transferred or acquired; or</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(2) The sum of:</td>
</tr>
<tr>
<td></td>
<td></td>
<td>a. A reasonable apportionment to the interests in real property owned by the entity of the amount of any liens, security interests or other obligations remaining on the ownership interest in the entity after conveyance, whether the underlying indebtedness is assumed or taken to;</td>
</tr>
<tr>
<td></td>
<td></td>
<td>b. A reasonable apportionment to the interests in real property owned by the entity of the amount of any liens or encumbrances remaining on the real property of the entity multiplied by the % in the entity transferred or acquired;</td>
</tr>
<tr>
<td></td>
<td></td>
<td>c. A reasonable apportionment to the interests in real property owned by the entity of the amount of any liens or encumbrances remaining on the real property of the entity multiplied by the % in the entity transferred or acquired;</td>
</tr>
<tr>
<td></td>
<td></td>
<td>d. A reasonable apportionment to the interests in real property owned by the entity of the amount of any other debt or obligation of the entity multiplied by the</td>
</tr>
</tbody>
</table>
% in the entity being transferred or acquired and;
e. A reasonable apportionment
to the interests in real
property owned by the
entity of any other amount
paid by the grantee for the
conveyance

<table>
<thead>
<tr>
<th>Mezzanine Foreclosure</th>
<th>The Grantee Is…</th>
<th>NYS Tax Base</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mezzanine</td>
<td>Third Party</td>
<td>(1) Amount of successful bid; and</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(2) Senior liens on the equity interest—including the unpaid balance of any more senior mezzanine loans not cancelled by the sale; and</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(3) Any unpaid balance of any outstanding mortgage on the real property</td>
</tr>
</tbody>
</table>

See Exhibit H (From Enforcing Mezzanine Loans Triggers Transfer Taxes, New York Law Journal, June 22, 2009 by John M. Zizzo, Bonnie A. Neuman and Michael J. Berey) for Problems on Mezzanine Foreclosure and Assignment in Lieu

C. New York State and New York City

No special rules apply in the case of “workouts” (other than the Chapter 11 exemption) though income taxes may be an issue.
V. Leases/Options

a. Payment from Lessor to Lessee in Exchange for Tenant to Vacate Premises
   - This is a taxable transaction because consideration for the surrender of a
     leasehold interest includes the amount paid for the surrender by the lessor to the
     lessee. However, consideration would not include the value of remaining rental
     payments required to be made pursuant to the terms of the lease.

b. Payment from Lessee to Lessor in Exchange for Right of Lessee to Cancel Lease
   Without Further Liability to Lessee
   - In contrast, if the Lessee is the moving party wishing to pay the Lessor for the
     right to surrender the lease early, no tax would be due since the grantor (here the
     lessee) would not receive any consideration for the conveyance.

c. Option/Contract to Purchase
   - The sale, exchange, assignment, surrender, or transfer of an option or contract to
     purchase real property is subject to realty transfer tax in New York State but not
     New York City.

d. Leasehold grant of more than 49 years
   - Such leasehold will be subject to the New York State real estate transfer tax
     provided that:
     (1) the sum of the term of the lease or sublease and any options for renewal
     exceeds 49 years;
     (2) substantial capital improvements are or may be made by or for the benefit
     of the lessee or sublessee; and
     (3) the lease or sublease is for substantially all of the premises constituting the
     real property. Substantially all is defined to mean 90 percent of the total
     rentable space of the premises, exclusive of common areas.

     Examples: (i) an individual building, except for space which constitutes an
     individual condominium or cooperative unit; (ii) an individual condominium
     or cooperative unit; or (iii) where a lease or sublease is of vacant land only,
     any portion of such vacant land.

   - NOTE: No New York City real property transfer tax will be due to the extent the
     only consideration transferred is considered “rent” for purposes of the New York
     City Commercial Rent and Occupancy Tax (but such lease payments will be
     subject to New York City’s commercial rent tax if it is in Manhattan and below
     96th street).
NEW YORK CITY AND NEW YORK STATE REALTY TRANSFER TAXES

e. Leasehold for less than 49 years with option to buy

- In the case of the creation of a leasehold interest where any options for renewal form a term of 49 years or less, but provides an option to purchase, the value of any amount paid for an option to purchase or renew and the value of rental or other payments attributable to the exercise of any option to renew will be subject to the realty transfer tax.

f. The assignment or transfer of a leasehold interest when there is a positive value will be subject to the realty transfer tax in New York State and New York City.

g. The transfer of a controlling interest in an entity with a leasehold interest is subject to tax regardless of the length of the remaining lease term, though how much consideration is applicable to the leasehold interest will be the most important factor.

VI. Mergers

a. Corporations

See In the Matter of the Petitions of The Chase Manhattan Corporation (f/k/a Chemical Banking Corporation) and Shareholders of The Chase Manhattan Corporation, February 4, 2005, Division of Tax Appeals, TAT (H) 88-99 (RP), TAT (H) 99-100 (RP), 2005 N.Y. Tax LEXIS 28.

Illustration from the New York City Rules: X Corporation owns real property in New York City with a fair market value of $300,000 and has cash of $100,000. X is to be merged into Y Corporation under Article 9 of the New York Business Corporation Law. Prior to the merger, Y Corporation owns no real property in New York City. Under the plan of merger, shareholders of X will receive consideration valued at $400,000 consisting of 25% of the stock of Y and cash. The shares of X exchanged or converted under the merger plan for the cash and stock of Y represent a controlling economic interest in real property and the transfer of such shares constitutes a taxable transfer. The shareholders of X, therefore, are subject to tax as a result of the statutory merger. A deed confirming title to property vested in the surviving Y Corporation pursuant to section 906(b)(2) of the New York Business Corporation Law will not be subject to the transfer tax. The tax on the transfer of a controlling economic interest in X would be exempt to the extent that the beneficial ownership in the real property remains the same. In that event, because the X shareholders receive 25% of the stock of Y and therefore retain a 25% beneficial interest in the real property previously owned by X, the transaction would be exempt to the extent of 25% and the tax would be imposed on 75% of the value of the consideration attributable to the real property (75% of $300,000 or $225,000). See §23-05(b)(8) of these rules.

b. Partnership

NEW YORK CITY AND NEW YORK STATE REALTY TRANSFER TAXES

Illustration from the New York City Rules: A owns a 90% limited partnership interest in capital and profits in each of limited partnerships X and Y. B is a general partner of both partnerships and owns the remaining 10% partnership interest in capital and profits in each limited partnership. X owns real property in New York City. Pursuant to Article 8-A of the New York Partnership Law, X will merge into Y. Following the merger A will have a 90% limited partnership interest in capital and profits in Y, and B will be the general partner with a 10% partnership interest in capital and profits in Y. Because A and B were the 100% beneficial owners of the property before the transaction and retain the same beneficial ownership interests in the property afterwards, the transaction is exempt as a mere change of identity or form of ownership or organization. The vesting of X’s assets in Y, by operation of law, is also not subject to tax.

VII. Bulk Sales

a. New York City issue only (all transfers, regardless of consideration or type of property are subject to the .4% rate for New York State – but see next section on the Mansion Tax).

b. Residential/Commercial/Other Units:
   (i) Where consideration is $500,000 or less, 1% (Residential only);
   (ii) Where consideration is more than $500,000, 1.425% (Residential only);
   (iii) Commercial Properties/Residential bulk sale: 2.625%.

c. See In the Matter of the Petition of Emerson Unitrust and Mark Emerson, Administrative Law Judge Division, TAT (H) 99-82 (RP) TAT (H) 99-83 (RP); In the Matter of Cambridge Leasing Corporation, Tax Appeals Tribunal, September 28, 2004, TAT (H) 03-11 (RP), 2004 Tax Lexis 196; In the Matter of David Gruber, Tax Appeals Tribunal, September 12, 2006, TAT (E)03-7, 8 & 9 (RP); In the Matter of Daniel and Sheila Rosenblum, Tax Appeals Tribunal, September 12, 2006, TAT (E) 01-31 (RP).

VIII. Mansion Tax

a. New York State issue only (no New York City Mansion Tax).


c. 1% of consideration for residential real property—generally a one, two, or three-family house; an individual condominium unit; a cooperative apartment unit.

d. “Residential real property” means any premises that is or may be used in whole or in part as a personal residence.”

e. Same exemptions to real estate transfer tax should apply, though there does not appear to be a continuing lien deduction (especially important when gifting residential real property).

IX. Certain Transfers to Real Estate Investment Trusts

a. 50% discount on certain transfers to real estate investment trusts (“REITs”)—or
tentities controlled by a REIT.

b. Continuity of Interest requirement either 40% or 50%, depending on whether the
transfer is to a newly formed REIT or existing REIT.

c. If newly formed REIT, other requirements also imposed.

d. Calculation of continuity of interest requirement different for New York City vs.
New York State

X. Mitchell-Lama Transfers/Other Transfers


b. Transfers pursuant to divorce or separation agreements: See In the Matter of S.
Jean Smith-Hoffman, Ricardo Smith-Hoffman, Tax Appeals Tribunal, March 7,
2003, TAT(E)93-2341(RP).

XI. Step-Transaction Doctrine

a. See Exhibit I—Statement of Audit Procedures: Transfers Into and Out of
Charitable Organizations

XII. Notable Exceptions to the Real Property/Real Estate Transfer Tax:

1. Mere Change in Form

A deed, instrument or transaction conveying or transferring real property or an economic
interest in real property to another person or entity, otherwise subject to tax, that effects a
mere change of identity or form of ownership or organization to the extent the beneficial
ownership of such real property (or for New York City only, economic interest) remains the
same. A sale of real property or an economic interest therein for cash or other valuable
consideration will be exempt to the extent the beneficial ownership remains the same,
provided the transaction represents a mere change of identity or form of owner-ship or
organization. See Exhibit A: In The Matter of the Petition of Viacom, Inc. DTA No.

See Example 5

A partnership owns real property in New York and the partnership entity transfers its
interest in the real property to each of its partners in the same pro-rata percentage of
ownership as their partnership interest. The transaction will require a filing of a realty
transfer tax return, however, no tax will be due since beneficial ownership will be identical
and this transaction would represent a mere change in the form of ownership.

NOTE: Just because a transfer may be exempt because it is a “mere change of identity or
form of ownership or organization” does not mean it is not “a transfer”. This means an
exempt transfer may still be aggregated with another non-exempt transfer, which by itself
NEW YORK CITY AND NEW YORK STATE REALTY TRANSFER TAXES

would not constitute a controlling interest, but because of the time period and facts involved, the two transfers together create a taxable transfer.

2. Mere Agent/Dummy, Strawman or Conduit Exemption

See Exhibit J—Statement of Audit Procedure: “Dummy/Strawman” Transfers in Connection with Real Estate Syndications

If two or more investors purchase real property together, they will form a partnership or a limited liability company to hold the real property (“vehicles” of investment). Investors in real estate use a variety of vehicles to acquire and finance the acquisition of real property or interests therein.

If the promoter is not able to obtain commitments from other investors at the time of the acquisition of the real property, a “nominee” (usually a separate entity) will usually acquire the property until investors can be added.

Once the appropriate capital has been raised and investors are ready to be added, the owner or “promoter” will usually make a small capital contribution to another partnership—this type of partnership is usually referred to as a syndicate. The promoter will then add other investors to this syndicate and transfer the real property to this syndicate from the nominee.

Now take a look at the way syndication may be affected by the realty transfer tax:

See Example 6:

On Day one, a partnership, which is a syndicate, is formed (hereinafter “Partnership A”) for the purpose of purchasing 360 Madison Avenue. Absent any rule to the contrary, if Partnership A purchases the real property commonly referred to as 360 Madison Avenue—or a controlling interest in an existing entity which holds legal title or a (50% or more) beneficial interest in the real property, a transfer tax would then be paid.

Since Partnership A is a syndicate, we know the main purpose of the original interest in 360 Madison was to syndicate the interests.

Applying the aggregation rules, we see the syndication is pursuant to a plan—therefore we know, absent any rule to the contrary, that all the interests sold and acquired, if such interests were to add up to 50% or more of a beneficial interest in the real property, a transfer tax would then be due a second time.

"Luckily, there are ways to avoid paying a realty transfer tax twice in New York."

New York City has codified an exemption known as the “mere agent/dummy, straw man, or conduit” exemption. If the taxpayer follows the procedures outlined in the New York City’s Statement of Audit Procedures (See Safe Harbor below), the taxpayer should qualify for an exemption from payment of the realty transfer tax twice (though two returns need to be filed, one to pay the tax, and the other to claim the exemption).

- Safe Harbor Procedures for the “Dummy Straw Man” Exemption from the SAP
  1. Return: If the taxpayer is claiming an exemption from the RPTTT under the “dummy/straw man” exemption, the taxpayer must check
NEW YORK CITY AND NEW YORK STATE REALTY TRANSFER TAXES

condition (h) on the form NYC-RPT and complete Schedule E.

2. Documentation: The taxpayer should maintain as much documentation as possible. There should always be a nominee or agency agreement, formation documents for the nominee and syndication materials. Loan agreements may also prove to be valuable documentation.

3. Duration: The nominee agreement should be for a limited period of time, usually within one year after acquisition of the property.

4. Consideration: There should be no consideration, other than a nominal amount not in excess of ten dollars, for the conveyance of the property from the nominee to the owner/principal. The property should not be conveyed with any indebtedness since consideration includes any underlying indebtedness on real property.

If any of these factors are missing, based on the individual facts of the situation, the dummy/straw man exception may be disallowed. Consequently, it is imperative any person wishing to take advantage of this exemption follow the necessary procedures to avoid paying double taxation.

NOTE: NYS has no dummy exception, though by following the procedure above it may be possible to avoid double taxation.

See Exhibit K: FLR 024795-021 and Exhibit L: FLR 99-4745

XIII. All Exceptions to the Real Property Transfer Tax (19 RCNY 23-05)

(a) The following persons are exempt from the payment of tax and from filing a return:

(1) The State of New York, or any public corporation (including a public corporation created pursuant to agreement or compact with another state or the Dominion of Canada), improvement district or other political subdivision of the state.

(2) The United States of America, and any of its agencies and instrumentalities insofar as they are immune from taxation.

(3) A foreign government, a person acting on behalf of a foreign government, or the head of a foreign government's diplomatic mission, with respect to premises used exclusively for diplomatic or consular purposes, or as the residence of the head of the diplomatic mission or consular post, to the extent exempt from the payment of tax pursuant to the Vienna Convention on Consular Relations (21 UST 77; TIAS 6820) or the Vienna Convention on Diplomatic Relations (23 UST 3227; TIAS 7502).

(4) A foreign government or a person acting on behalf of a foreign government to the extent exempt from the payment of tax pursuant to a treaty or convention to which the United States and the foreign government are parties, other than as provided under paragraph (3), above.
NEW YORK CITY AND NEW YORK STATE REALTY TRANSFER TAXES

The exemption of such governmental bodies or persons shall not, however, relieve a grantee from them of liability for the tax or from filing a return.

(b) **The tax does not apply to any of the following deeds, instruments, or transactions:**

1. A deed, instrument, or transaction conveying or transferring real property or an economic interest therein by or to the United Nations or other world-wide international organizations of which the United States of America is a member.

2. A deed, instrument, or transaction conveying or transferring real property or an economic interest therein by or to any corporation, or association, or trust, or community chest, fund or foundation, organized and operated exclusively for religious, charitable or educational purposes or for the prevention of cruelty to children or animals, and no part of the net earnings of which inures to the benefit of any private shareholder or individual and no substantial part of the activities of which is carrying on propaganda, or otherwise attempting to influence legislation, provided, however, that nothing in this paragraph shall include an organization operated for the primary purpose of carrying on a trade or business for profit, whether or not all of its profits are payable to one or more organizations described in this paragraph.

3. A deed, instrument, or transaction conveying or transferring real property or an economic interest therein to any governmental body or person exempt from payment of the tax pursuant to paragraph (1) or (2) of subdivision (a) of §23-05.

4. A deed delivered pursuant to a contract made prior to May 1, 1959.

5. A deed delivered by any governmental body or person exempt from payment of the tax pursuant to §23-05(a) as a result of a sale at a public auction held in accordance with the provisions of a contract made prior to May 1, 1959.

6. A deed or instrument given solely as security for, or a transaction the sole purpose of which is to secure, a debt or obligation or a deed or instrument given, or a transaction entered into, solely for the purpose of returning such security.

7. A deed, instrument, or transaction conveying or transferring real property or an economic interest therein from a mere agent, dummy, straw man or conduit to a principal, or a deed, instrument or transaction conveying or transferring real property or an economic interest therein from the principal to his agent, dummy, straw man or conduit.

The following are examples of deeds, instruments and transactions in which this exemption applies:

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(i) The conveyance of realty by an individual to a corporation solely for the purpose of obtaining mortgage financing, followed by the immediate reconveyance of the realty by the corporation to the individual after such mortgage financing is obtained.

(ii) A deed transferring real property to an existing corporation solely for the purpose of effectuating the terms of a mortgage spreader agreement. The deed returning the mortgaged realty to its true owner is also exempt from the tax.

(iii) A conveyance between a principal and its agent where

(A) a written agreement is entered into at the time of the transaction establishing such a relationship with respect to the realty or economic interest therein,
(B) the purported agent functions as an agent with respect to the realty or economic interest therein for all purposes, and
(C) the purported agent is held out as the agent and not the principal in all dealings with third parties relating to the realty or economic interest therein.

Since the tax does not apply to any deed, instrument, or transaction described in §23-05(b), neither the grantor nor the grantee is required to pay the tax. However, a return relating to the deed, instrument, or transaction must be filed.

(8) A deed, instrument or transaction conveying or transferring real property or an economic interest in real property to another person or entity, otherwise subject to tax, that effects a mere change of identity or form of ownership or organization to the extent the beneficial ownership of such real property or economic interest remains the same. A sale of real property or an economic interest therein for cash or other valuable consideration will be exempt to the extent the beneficial ownership remains the same, provided the transaction represents a mere change of identity or form of owner-ship or organization.

XIV. All Exceptions to the Real Estate Transfer Tax (20 NYCRR § 575.9)

(a) Certain governmental organizations or entities are exempt from the payment of the real estate transfer tax. In addition, there are certain types of transactions to which this tax does not apply.

(b) The exemption for certain governmental organizations or entities does not extend to the grantee: that is, if the exempt governmental entity conveys title to real property to a nonexempt individual or entity, there will be a tax due which is payable by the grantee. The exemption for governmental organizations or entities includes the following:

(1) the State of New York, or any of its agencies, instrumentalities, political subdivisions, or public corporations including a public corporation created pursuant to agreement or compact with another state or the Dominion of Canada. A public corporation includes a public benefit corporation such as the Urban Development Corporation. (For a full definition of public corporation, see section 66 of the General Construction Law);

(2) the United Nations; and

(3) the United States of America and any of its agencies or instrumentalities.
(c) In addition to the exemptions described in subdivision (b) of this section, certain transactions are not subject to the real estate transfer tax. These include:
(1) conveyances to any of the governmental organizations or entities described in subdivision (b) of this section, including any instrumentality or agency of the United Nations;
(2) conveyances which are or were used to secure a debt or other obligation;
(3) conveyances which, without additional consideration, confirm, correct, modify or supplement a prior conveyance;
(4) conveyances without consideration and otherwise than in connection with a sale, including conveyances by bona fide gift;
(5) conveyances given in connection with a tax sale;
(6) conveyances to effectuate a mere chance of identity or form of ownership or organization where there is no change in beneficial ownership, other than conveyances to a cooperative housing corporation of the real property comprising the cooperative dwelling or dwellings. Examples of such conveyances are set out at section 575.10 of this Part:
(7) conveyances which consist of a deed of partition;
(8) conveyances given pursuant to the Federal Bankruptcy Act;
(9) conveyances which consist of the execution of a contract to sell real property without the use or occupancy of such property, or the granting of an option to purchase real property without the use or occupancy of such property; and
(10) conveyances of an option or contract to purchase real property which include the right to use or occupy such property where:

(i) the consideration is less than $200,000; and

(ii) such property or at least one unit of a two- or three-family house was used solely as the grantor's personal residence;

(iii) the real property consists of a one-, two- or three-family house, an individual residential condominium unit or the sale of stock in a cooperative housing corporation in connection with the grant or transfer of proprietary leasehold covering an individual residential cooperative unit.

XV. Responsibility for Transfer Tax

Although transfer taxes are usually imposed on the transferor, the transferee may be secondarily liable for the payment of such taxes. Thus, when the defaulting borrower cannot pay these taxes, the lender's costs of exercising its remedies may be significantly increased. For example, a lender taking a deed to New York City commercial property in lieu of foreclosure could become secondarily liable for New York State and City transfer taxes. (Cardinali, TAX ASPECTS OF NON-CORPORATE SINGLE ASSET BANKRUPTCIES AND WORKOUTS, 1 Am. Bankr. Inst. L. Rev. 87, 1993)
STATE OF NEW YORK
TAX APPEALS TRIBUNAL

In the Matter of the Petition

of

VIACOM, INC.

for Revision of a Determination or for Refund of Real
Estate Transfer Tax under Article 31 of the Tax Law for
the Period May 4, 2000.

Petitioner Viacom, Inc., 1515 Broadway, New York, New York 10036-8901, filed an
exception to the determination of the Administrative Law Judge issued on May 26, 2005.
Petitioner appeared by Roberts & Holland LLP (Carolyn Joy Lee, Esq., of counsel). The
Division of Taxation appeared by Mark F. Volk, Esq. (Barbara J. Russo, Esq., of
counsel).

Petitioner filed a brief in support of its exception and the Division of Taxation filed a
brief in opposition. Petitioner filed a reply brief. Oral argument, at petitioner's request,
was heard on November 6, 2006 in New York, New York.

After reviewing the entire record in this matter, the Tax Appeals Tribunal renders the
following decision. Commissioner McDermott dissents for the reasons set forth in a
separate opinion.

ISSUES

I. Whether a conveyance of real property was properly excluded from the real estate
transfer tax pursuant to Tax Law
§ 1405(b)(6) as a "mere change of identity or form of ownership or organization where
there is no change in beneficial ownership."

II. Whether penalty imposed under Tax Law § 1416(b) should be sustained.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge except for finding of
fact "10" which has been modified. The Administrative Law Judge's findings of fact and
the modified finding of fact are set forth below.
On May 4, 2000, the CBS Corporation ("CBS") merged into Viacom, Inc. ("Viacom") (the "Merger"). CBS had been a Pennsylvania corporation; Viacom is a Delaware corporation. The Joint Proxy Statement describes CBS, Viacom, and the terms and conditions of the Merger.

The Merger was a statutory merger effected under the Delaware General Corporation Law ("Delaware Corporate Law") by filing a Certificate of Merger with the Secretary of State of the State of Delaware. A Restated Certificate of Incorporation of Viacom became effective upon the Merger.

At the time of the Merger, Viacom had two outstanding classes of common stock, Viacom Class A voting common stock ("Class A Stock") and Viacom Class B nonvoting common stock ("Class B Stock"). In the Merger, the holders of CBS voting common stock received Viacom Class B nonvoting common stock.

In the Merger, the CBS shareholders received Viacom Class B Stock equal in the aggregate to a 54.88% ownership interest in Viacom.

The terms of the Class B Stock are set forth in the Restated Certificate of Incorporation of Viacom. As set forth therein,

(i) the holders of Class A Stock and Class B Stock receive dividends ratably;
(ii) upon a dissolution or liquidation of Viacom, the holders of Class A Stock and Class B Stock divide the net assets of Viacom available to common stockholders ratably; and
(iii) any split, subdivision or combination of the outstanding Class A Stock or Class B Stock is to be matched by a proportionate split, subdivision or combination of the other Class's stock. The Certificate of Merger states that each share of Class B Stock has rights, privileges, limitations, restrictions and qualifications identical to a share of Class A Stock, except that shares of Class B Stock have no voting rights other than those required by the Delaware Corporate Law.

The Restated Certificate of Incorporation provided that, contemporaneous with the Merger, the Board of Directors of Viacom was expanded from 10 to 18 directors. In addition, the Stockholders Agreement was entered into by National Amusements, Inc., which owned 68% of Viacom's Class A Stock at the time of the Merger, and CBS. In the Stockholders Agreement it was agreed that, subject to fiduciary limitations, for a three-year period subsequent to the Merger, 8 of the 18 members of Viacom's board of directors would be individuals who had been directors of the former CBS ("CBS Directors"), or replacements those CBS Directors might designate. The remaining ten directors of the combined company were the individuals who were the Viacom Board members prior to the Merger ("Viacom Directors"). Of these ten Viacom Directors, two were required to be either current independent directors of Viacom or other disinterested independent persons who are chief executive officers of a Fortune 500 company or a non-U.S. company of comparable size. Except with respect to matters delineated in Annex 1 of Viacom's Restated Certificate of Incorporation, all actions of the board of directors for the three-year period subsequent to the Merger required the approval of 14 directors. The
expanded board size could not be changed without the approval of at least 14 directors for the three-year period subsequent to the Merger. The actions of the board, other than those stated in Annex 1 of Viacom's Restated Certificate of Incorporation, including any change in board size, thus would require the approval of at least 50% of the former CBS board members.

Mr. Karmazin, then current CEO and President of CBS, was named the President and Chief Operating Officer ("COO") of Viacom at the time of the Merger. During the three-year period following the Merger, Mr. Karmazin could not be terminated or demoted, nor could his operational responsibilities be curtailed, except on the approval of at least 14 directors.

Prior to the Merger, the stock of CBS and the Viacom Class A Stock and Class B Stock were publicly traded on the New York Stock Exchange ("NYSE"). Following the Merger, the Viacom Class A Stock and Class B Stock continued to be publicly traded on the NYSE.

Since the Merger, Viacom has made two dividend payments to holders of Class A Stock and Class B Stock, which dividends were paid ratably as specified in the Restated Certificate of Incorporation of Viacom. On October 14, 2003, Viacom announced the payment of a dividend of $0.06 per share for each share of Class A Stock and Class B Stock. On January 28, 2004, Viacom announced the payment of a dividend of $0.06 per share for each share of Class A Stock and Class B Stock.

We modify finding of fact "10" of the Administrative Law Judge's determination to read as follows:

The Merger was effected on May 4, 2000 upon the filing of a certificate of merger with the Secretary of State of Delaware (see, Stipulation of Facts, Exhibit B). The certificate states that the constituent corporations were CBS Corporation, a Pennsylvania corporation, and Viacom Inc., a Delaware corporation, and that Viacom Inc. was the surviving corporation. The parties stipulated that the Merger "effected a transfer of a controlling economic interest in CBS within the meaning of Tax Law Article 31" (see, Stipulation of Facts, p. 4). The interests in real property in New York State owned by CBS at the time of the Merger (collectively the "CBS Real Estate") were reported on Forms TP-584, combined real estate transfer tax returns, filed on May 22, 2000 (collectively the "Returns"). It appears from the forms that the real property was held directly by the CBS parent corporation rather than subsidiaries. \(^1\)

The fair market value of the CBS New York Real Estate at the time of the Merger was $222,505,992.00 in the aggregate, as indicated on the Returns.

The Returns claimed exemptions aggregating 70.44% under Tax Law § 1405(b)(6). Real estate transfer tax ("RETT") in the amount of $258,106.92 was paid to the New York State Department of Taxation and Finance on May 22, 2000.
The Commissioner of Taxation and Finance issued a Notice of Determination ("Notice") dated May 2, 2003 to Viacom.

The Commissioner accepted the exemption claimed under Tax Law § 1405(b)(6) as to 15.56% of the transfer, but disallowed the claim for exemption for the 54.88% (rounded in the Notice to 54.9%) ownership interest that CBS shareholders received in Viacom as a result of the Merger, on the basis that the Class B Stock was nonvoting stock.

The Commissioner has asserted a RETT deficiency of $493,965.08.

The Commissioner has asserted interest as of May 2, 2003 in the amount of $117,908.11 and a penalty of $172,887.75 with respect to the RETT deficiency.

On July 30, 2003, Viacom filed a timely petition for review of the notice with the Division of Tax Appeals.

On October 1, 2003, the Division of Taxation filed a timely answer to the petition.

**THE DETERMINATION OF THE ADMINISTRATIVE LAW JUDGE**

The Administrative Law Judge concluded that where there is a change in the controlling interest in a corporation, it follows that there is a change in the beneficial ownership. Since voting power is an essential aspect of a controlling interest, an exchange of voting stock for nonvoting stock, such as occurred in the present case, necessarily involves a change in controlling interest and accordingly a change in beneficial ownership. Moreover, a different result would create an opportunity for tax avoidance since if the exchange of voting stock for nonvoting stock were not taxed, the nonvoting shares received in the merger could be disposed of in the future without incurring the transfer tax. Finally, the determination concluded that petitioner's failure to pay the applicable tax was not due to reasonable cause and accordingly the imposition of a penalty was appropriate.

**ARGUMENTS ON EXCEPTION**

Petitioner asserts that the Class B Stock of Viacom which was received by the former CBS shareholders in the merger should be counted as a beneficial ownership in the real estate transferred by CBS with the result that the transfer was entitled to a change-in-form exemption under Tax Law § 1405(b)(6) to the extent of 70.44% consisting of 15.56% represented by pre-existing overlapping ownership and 54.88% represented by Viacom nonvoting stock issued in the merger.

The Division argues that the determination of whether there has been a change of "beneficial ownership" must be read together with the definition of "conveyance" and "controlling interest" and concludes that if there is a change in controlling interest and therefore a conveyance, there is a change in beneficial ownership. If the CBS shareholders had received voting stock in the surviving corporation, instead of nonvoting
shares, there would be no such change, because the nature of their ownership interest before and after the conveyance would have been the same, i.e., voting stock in an entity owning real property.

**OPINION**

The real estate transfer tax is "imposed on each conveyance of real property or interest therein" (Tax Law § 1402[a]). All conveyances are presumed subject to the tax (Tax Law § 1404[b]).

The term "conveyance" is defined, to the extent relevant here, as "the transfer or transfers of any interest in real property by any method, including but not limited to sale, exchange, assignment . . . or transfer or acquisition of a controlling interest in any entity with an interest in real property" (Tax Law § 1401[e]). The words "controlling interest" have the following definition:

"Controlling interest" means (i) in the case of a corporation, either fifty percent or more of the total combined voting power of all classes of stock of such corporation, or fifty percent or more of the capital, profits or beneficial interest in such voting stock of such corporation . . . (Tax Law § 1401[b]).

In this case, the parties have agreed and stipulated to the fact that the Merger constituted the transfer of a controlling interest in CBS's real property for purposes of Tax Law Article 31.

However, petitioner claims an exemption from real property transfer tax based on the "change in form" provisions of Tax Law § 1504(b)(6). That section provides an exemption from the real property transfer tax for "[c]onveyances to effectuate a mere change of identity or form of ownership or organization where there is no change in beneficial ownership . . ." [Tax Law § 1405[b][6]).

We note that statutory exemptions are strictly construed against the taxpayer (Bredero Vast Goed, N. V. v. Tax Commn. of the State of New York, 146 AD2d 155, 539 NYS2d 823, *appeal dismissed* 74 NY2d 791, 545 NYS2d 105). In a case such as this, where it is presumed that the determination of the Division is correct, the burden is on petitioner not only to show that its interpretation is reasonable, but that it is the only reasonable interpretation, or that the Division's interpretation is unreasonable (Matter of Marriott Family Rests. v. Tax Appeals Tribunal, 174 AD2d 805, 570 NYS2d 741, *bv denied* 78 NY2d 863, 578 NYS2d 877). These principles of statutory construction also apply to the interpretation of regulations (see, Matter of Cornland-Clinton, Inc. v. New York State Dept. of Health, 59 AD2d 228, 399 NYS2d 492).

Petitioner argues that following the Merger, the CBS shareholders had an *ongoing* "beneficial interest" in the CBS Real Estate thus entitling the Merger to the 54.88% change-in-form exemption claimed.
While the term "beneficial ownership" is not defined in the Tax Law and regulations, it has been defined by both the courts and the Tax Appeals Tribunal in other areas of the law as being more than a mere financial interest. Beneficial ownership is marked by the command over property or enjoyment of its economic benefits (Yelencsics v. Commissioner, 74 T.C. 1513, citing Anderson v. Commissioner, 164 F2d 870, 48-1 USTC ¶ 9109, affg 5 T.C. 443; Matter of Racial Corp. & Decca Elecs., Tax Appeals Tribunal, May 13, 1993; Matter of Shechter, Tax Appeals Tribunal, October 13, 1994; Macon, Dublin, & Savannah R.R. Co. v. Commissioner, 40 BTA 1266 [where the Court stated: "taxation is not so much concerned with the refinements of title as it is with the actual command over the property taxed . . . that is the beneficial ownership"]).

In May 2000, CBS and Viacom merged with Viacom surviving as the new corporate entity. Shareholders of CBS exchanged their voting common stock for shares of Viacom Class B nonvoting common stock. Viacom acquired a controlling interest in CBS which at the time of the Merger had an interest in real property. Pursuant to Tax Law § 1401(b)(i) and (e), we conclude that the Merger between CBS and Viacom resulted in a taxable conveyance of an interest in real property by CBS to Viacom.

Petitioner argues that it is entitled to the change in form exemption because the CBS shareholders continued to have a beneficial interest in the real property transferred to Viacom. To prevail, petitioner needed to show that the beneficial interest owned by the shareholders of CBS after the merger was the same as what they owned prior to the merger (see, Matter of Shechter, supra). We note that the statute only provides an exclusion for real estate transfers where there is no change in beneficial ownership, so any change in this beneficial ownership resulting from the merger would be sufficient to defeat petitioner's entitlement to the claimed exemption.

We reject petitioner's argument, for the reasons set forth by the Administrative Law Judge, that the change-in-form exemption contained in section 1405(b)(6) is to be read independently of the definition of "controlling interest" provided in section 1401(b)(i) so as to determine the issue of "beneficial ownership" without resort to the definition of "control." The degree of one's "beneficial ownership" is an inherent consideration in determining whether "control," to some degree, has been transferred. McKinney's Consolidated Laws of NY, Book 1, Statutes § 97 provides, in pertinent part:

It is a fundamental rule of statutory construction that a statute or legislative act is to be construed as a whole, and that all parts of an act are to be read and construed together to determine the legislative intent . . . .

A general expression or a single sentence detached from its context does not reveal the purpose of the statute as a whole, and particular provisions, therefore, should not be torn from their places and, so isolated,
be given a special meaning at variance with the general purpose and spirit of the enactment.

The term "beneficial ownership" as it is used in the context of Tax Law Article 31 relating to corporations must be determined by considering the exemption together with the definitions of "conveyance" and "controlling interest," since the exemption provides that the tax shall not apply to "[c]onveyances to effectuate a mere change . . ." (Tax Law § 1405 [b][6]). When used in this context, "conveyance" means a "transfer or acquisition of a controlling interest in any entity with an interest in real property" (Tax Law § 1401[e]). The parties have stipulated that there has been a transfer of a controlling interest in CBS Corporation and its real property to Viacom. In defining "controlling interest," the statute refers only to voting stock (Tax Law § 1401[b]). When, a change in the controlling interest occurs, it necessarily results in a change in the beneficial ownership. Under the express provisions of the statute, voting power [of the stock] is an element required for purposes of determining a controlling interest (Tax Law § 1401[b]). Where 100% voting stock of CBS was surrendered in return for nonvoting stock in Viacom, representing a 54.88% interest in the merged company, there was a transfer of a controlling interest in an entity (CBS) with an interest in real property to Viacom (Tax Law § 1401[d] and [e]). There was also a change in the beneficial interest owned by those CBS stockholders. While the CBS stockholders who received nonvoting shares in Viacom continued to have a financial interest in the real property conveyed to Viacom (to the extent of their 54.88% ownership in Viacom nonvoting shares), their "beneficial interest" in the merged company's real property went from 100 percent before the merger to zero\(^3\) after the merger, since the stockholders no longer had a vote in the company or control or dominion (to the extent of the share ownership) in Viacom's real property. We need not quantify what that vote amounted to in terms of the operations of a company's real property. It is sufficient that the CBS shareholders who received nonvoting stock in exchange for voting stock in CBS did not retain the same dominion and control (through their voting shares) of the real property transferred from CBS to Viacom \(\text{see, Matter of Shechter, supra}\). With this change in beneficial ownership, the former CBS stockholders retained a mere financial or economic benefit via their nonvoting shares in Viacom. Thus, their interest in the real property after the Merger differed from their interest in the real property before the Merger. Accordingly, we conclude there has been both a transfer of a controlling interest in real property for purposes of Article 31 of the Tax Law and a change in beneficial ownership.

With respect to the issue of penalty, we agree with the Administrative Law Judge's analysis of this issue in his determination and, as such, the imposition of penalties is sustained.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Viacom, Inc. is denied;

2. The determination of the Administrative Law Judge is affirmed;
3. The petition of Viacom, Inc. is denied; and

4. The Notice of Determination dated May 2, 2003 is sustained.

DATED: Troy, New York
May 3, 2007

______________________________
Charles H.
President

______________________________
Carroll R. Jenkins
Commissioner

COMMISSIONER MCDERMOTT dissenting:

For the reasons discussed below, I am unable to join my colleagues in deciding this case and would instead reverse the determination of the Administrative Law Judge.

The outcome of this case depends on whether two statutory concepts are interrelated in the way that the Division asserts or instead operate independently as petitioner argues. The first concept, which defines the event that causes the tax to apply, is stated in the alternative as (i) an actual transfer of an interest in real property or (ii) a transfer of a controlling interest in an entity that owns real property. The second concept, which appears in the statute in the form of an exemption from tax, measures the extent to which the transferor's direct or indirect interest in the real property has been transferred. The statute and regulations define this measurement by stating that there is no taxable transfer if and to the extent that the transfer effects a mere change in the form of ownership and there is no change in the beneficial ownership of the real property. These provisions of the statute and regulations are described below.

Tax Law § 1402 generally imposes a tax on "each conveyance of real property or interest therein." The term "conveyance" is broadly defined, to the extent relevant here, as "the transfer or transfers of any interest in real property by any method, including but not limited to sale, exchange, assignment . . . or transfer or acquisition of a controlling interest in any entity with an interest in real property" (Tax Law § 1401[e]). The words "controlling interest" have the following definition:
"Controlling interest" means (i) in the case of a corporation, either fifty percent or more of the total combined voting power of all classes of stock of such corporation, or fifty percent or more of the capital, profits or beneficial interest in such voting stock of such corporation, and (ii) in the case of a partnership, association, trust or other entity, fifty percent or more of the capital, profits or beneficial interest in such partnership, association, trust or other entity (Tax Law § 1401[b]).

An exemption from tax is provided in Tax Law § 1405(b)(6) for "[c]onveyances to effectuate a mere change of identity or form of ownership or organization where there is no change in beneficial ownership . . . ." The scope of this exemption is explained in the Division's regulations at 20 NYCRR 575.10 which reads in extenso as follows:

To the extent that a conveyance effectuates a mere change of identity or form of ownership or organization and there is no change in beneficial ownership, the real estate transfer tax does not apply. Examples of transactions where the issue of change in beneficial ownership would arise include the following:

(a) the conveyance by tenants-in-common of their interest in real property to a partnership or a corporation, the partnership or corporation interests being in the same pro rata shares as the tenants-in-common held prior to conveyance. Such conveyance is not taxable as there is no change in beneficial ownership;

(b) the conveyance by a corporation to its shareholders who will hold the real property as tenants-in-common in the same pro rata share as they own the corporation. Such conveyance is not taxable as there is no change in beneficial ownership;

(c) the conveyance by a corporation to its wholly-owned subsidiary, from a wholly-owned subsidiary to its parent, or from one wholly-owned subsidiary to another. Such conveyance is not taxable to the extent that there is no change in beneficial ownership;

(d) the conveyance by a person to a partnership in exchange for an interest in the partnership. Such conveyance is not taxable to the extent of the grantor's interest in the partnership.
There are two principles that can be drawn from these regulations. First, the use of the words "to the extent that" makes clear that a pro tanto application of the exemption is appropriate and that the statutory words "no change" should not be read to disqualify a transaction in its entirety where there is any change. The Division's assertion to the contrary (see, Division's brief in opposition, p. 5), which is accepted by the majority, is accordingly inconsistent with the regulations.

Second, there is no suggestion in the regulations that the ability to vote for corporate directors or to influence the governance of a partnership would be significant in determining whether there has been a change in beneficial ownership. The final example quoted above indicates that in a partnership setting the words "beneficial ownership" are synonymous with the partner's "interest in the partnership." The phrase "the partner's interest in the partnership" is a term of art in section 704(b) of the Internal Revenue Code which is interpreted in section 1.704-1(b)(3) of the Treasury Regulations. That provision of the regulations states that among the factors to be considered in determining a partner's interest in the partnership are (a) the partners' relative contributions to the partnership, (b) the interests of the partners in economic profits and losses, (c) the interests of the partners in cash flow and other non-liquidating distributions, and (d) the rights of the partners in distributions of capital upon liquidation. Again, there is no suggestion that non-economic factors, such as influence on firm governance, are relevant.

The limited case law under similar provisions of the real estate transfer gains tax is also consistent with the conclusion that a change in beneficial ownership should be determined on the basis of economic factors, not the shareholder's role in corporate governance. In Matter of Schrier (Tax Appeals Tribunal, July 16, 1992, confirmed Matter of Schrier v. Tax Appeals Tribunal, 194 AD2d 273, 606 NYS2d 384, appeal dismissed 83 NY2d 944, 615 NYS2d 871), we held that the mere change in form exemption under similar provisions of the gains tax and the underlying regulations applied to a liquidating distribution of real estate to corporate shareholders who thereafter held the property as joint tenants, stating as follows:

[T]he regulations . . . convey the underlying theme of the tax through a series of examples of the mere change in form exemption provided by Tax Law § 1443(5) (see, 20 NYCRR 590.50[a][2]-[5]). In these examples, various types of changes in business form are addressed. Provided the owners of the property retain the same proportion of beneficial ownership, the end result of each change in business form is the same -- the change is deemed a mere change. Any variation in the rights and obligations imposed by the new business form is not addressed by the regulation; the only concern articulated in the examples is whether the proportion of beneficial interest of each owner has varied. Thus, the transfer of property from a tenancy in common to a partnership, where each owner's percentage of beneficial interest in the property is preserved, is considered a mere change in form despite any change in the parties' legal relationship under the new business form (see, 20 NYCRR 590.50(a)(2)). Likewise, the transfer of property from a corporation to its shareholders, who will take the property as tenants in common with the same
proportion of beneficial ownership as they had as shareholders, is considered a mere change in form (see, 20 NYCRR 590.50[a][3]). From this we conclude that the primary concern of the examples is whether the economic interests in the real property have been changed (see, Matter of Bredero Vast Goed, N. V. v. Tax Commn. of the State of New York, 146 AD2d 155, 539 NYS2d 823, 825 [where the court recognizes and upholds economic reality as the key principle underlying the interpretation of the imposition section of the gains tax]).

By contrast, there is some language in two early gains tax cases that seems to support the Division's position here. In Matter of Howes (Tax Appeals Tribunal, September 22, 1988, confirmed Matter of Howes v. Tax Appeals Tribunal, 159 AD2d 813, 552 NYS2d 972), an individual acquired a small apartment house in 1997. He occupied one of the apartments as his residence and contributed the remainder of the real property to a partnership in which he held approximately 98% of the capital interest. In 1985, the real property was sold for $1,396,000.00 of which $488,600.00 was allocable to the personal residence and $907,400.00 was allocable to the business use property owned by the partnership. We rejected the petitioner's position that the sale could be bifurcated for purposes of testing whether the $1 million exemption was applicable. In so holding, the decision relied in part on the mere-change-in-form exemption and stated as follows:

To determine petitioner's ownership interest in the partnership, and thus his beneficial interest in the real property, the definition of controlling interest in the case of a partnership directs us to the ownership of "capital, profits, or beneficial interest in such partnership" (Tax Law § 1440[2]). Since this definition would control how the tax and mere change in form exemption would apply on the transfer of the real property to the partnership in exchange for a partnership interest, [footnote omitted] it also applies in determining the taxability of a subsequent transfer by the partnership.

Similar language is found in Matter of 307 McKibbon St. Realty Corp. (Tax Appeals Tribunal, October 14, 1988).

Nevertheless, these statements do not seem necessary premises for the holdings in Howes and 307 McKibbon St. and do not appear to be supported by authority. Moreover, their significance seems substantially diminished by our subsequent decision in Matter of Muraskin (Tax Appeals Tribunal, March 24, 1994, confirmed Matter of Muraskin v. Tax Appeals Tribunal, 213 AD2d 91, 630 NYS2d 119, lv denied 87 NY2d 806, 641 NYS2d 597), in which we said the following:

The Appellate Division's decision in Matter of Howes v. Tax Appeals Tribunal (159 AD2d 813, 552 NYS2d 972) establishes that it is appropriate for gains tax purposes to "look through" an entity that owns
real property to determine the beneficial owners of the real property. Further, Howes establishes that it is appropriate to aggregate the consideration received from the transfer of the ownership interest in the entity with the consideration received from the transfer of other interests in the real property by the same person to apply the $1 million exemption of section 1443(1) of the Tax Law. Petitioner does not dispute this meaning of Howes but argues that the rule of Howes only applies when the beneficial owner of the entity has at least a controlling interest in the entity. Although the petitioner in Howes did own more than a 50% interest in the entity, we see nothing in the court decision which suggests that this result would only apply where the person owned at least a controlling interest in the entity. . . . [W]e conclude that the principle of Howes applies regardless of the percentage interest held in the entity.

In Muraskin, we thus concluded that beneficial interest is determined on the basis of a look-through principle that is divorced from the definition of "controlling interest" and abandoned the inconsistent dicta found in our decision in Howes.

The Division has cited no authority that actually supports its view that the words "beneficial ownership" imply the existence of control. With the sole exception of Matter of Shechter (Tax Appeals Tribunal, October 13, 1994), the cases cited by the Division involve income and franchise tax statutes and circumstances that are too far removed from the issue here to provide even remote analogies. Moreover, none of those cases involved the issue of how the terms "beneficial ownership" or "beneficial interest" should be interpreted when used in a statute, regulation or contract. Instead, those terms are used by the courts in a more casual way to describe some other standard such as distinguishing mere legal or nominal ownership from real ownership for tax purposes.

In Shechter, an individual sold stock in a corporation owning real property to a partnership in exchange for cash and a promissory note. The partners in the partnership were the seller's brother and a friend. The seller asserted that there was no taxable conveyance because he continued to control the real property through his relationship with the partners. We held that this argument failed by its own terms because the petitioner did not adduce sufficient evidence to establish that he controlled the partnership. The decision does not hold, as the Division argues, that control is an appropriate test for determining the presence of "beneficial ownership." Moreover, the decision went on to state, "To prevail, petitioner also needed to establish a financial interest akin to the ownership interest he had before the transfer . . ." (emphasis added).

The words "beneficial ownership" most immediately call to my mind the interest of the beneficiary of a trust. There the control of the corpus is in the hands of the legal owner, the trustee, and the beneficiary's only right is to insist that the trustee follow the terms of the trust and behave in accordance with its fiduciary duty.
In the present case, I believe we should confirm the concepts articulated in Schrier and Muraskin and give each of the statutory terms "conveyance" and "beneficial ownership" a full and independent scope by using a simple economic look-through test for "beneficial ownership" that would be easy to understand and apply.

DATED: Troy, New York
May 3, 2007

/s/Robert J.

McDermott
Robert J.
Commissioner

1. We modified finding of fact "10" to avoid phrasing a factual matter as a legal conclusion and to better reflect the record.

2. While the grantor is generally responsible for the payment of the transfer tax, the grantee must pay the tax where the grantor fails to do so (Tax Law § 1404[a]).

3. The "zero" refers back to the interest held by the 54.88 percent. The Division accepted the exemption claimed under Tax Law § 1405(b)(6) with respect to 15.55% of the transfer which was not in dispute.
EXHIBIT B
DISPOSITION: Accordingly, plaintiff's motion for summary judgment is denied and defendants' cross motion for summary judgment is granted.

HEADNOTES

Taxation -- New York City Real Property Transfer Tax -- Use of Two-Tiered Partnership Device to Avoid Tax

The New York City Real Property Transfer Tax, which, retroactive to July 13, 1986, imposes a transfer tax "on each instrument or transaction * * * whereby any economic interest in real property is transferred" (Administrative Code of City of New York § 11-2102 [b] [1]), applies to plaintiff's syndication to limited partners in October 1986 of more than a 50% interest in itself when plaintiff did not own any realty in New York City, but was the sole limited partner in a partnership that did, since the two-tiered partnership device, whereby a shell partnership is created to separate title ownership from the entity in which the economic interests with respect thereto were transferred, may not be used as a tax avoidance device when the purpose of the statute is to tax transactions which effectively, but indirectly, convey real property. The sales of plaintiff's partnership interests were, in essence, the sales of interests in real property situated in New York City with the purchasers of the limited partnership interests obtaining their profits exclusively from revenues, capital appreciation and tax benefits attributable to the property and this is precisely the sort of transaction the statute was intended to reach. Taxation of the transfers does not violate the constitutional prohibition against the imposition of an ad valorem tax on intangible personal property (NY Const, art XVI, § 3) nor does it violate either the Commerce or Due Process Clause of the Federal Constitution. In addition, the five-month retrospective application of the statute is lawful since closing a perceived loophole in the law is a reasonable basis on which to legislate retroactively when the public was on notice at all times during the retroactive period of the city's intention to impose a tax on transfers of economic interests in real property.

COUNSEL: Shea & Gould for plaintiff.

Peter L. Zimroth, Corporation Counsel, for defendants.

JUDGES: Edward H. Lehner, J.

OPINION BY: LEHNER

OPINION

The question posed by the motion and cross motion for summary judgment is whether the New York City Real Property Transfer Tax (RPTT) is applicable to plaintiff's syndication of limited partnership interests in itself when the plaintiff did not own any realty, but was the sole limited partner in a partnership that did. Under the facts presented herein, the sale by syndication to limited partners of more than a 50% interest in plaintiff constitutes a taxable conveyance under that statute.

FACTS

On September 3, 1986, 595 Madison Avenue Associates Limited Partnership (Associates), a Delaware limited partnership, acquired title to the building at that address. The sole limited partner then and now of As-
sociates is plaintiff, also a Delaware limited partnership. At the time of such acquisition, plaintiff consisted of one
general and one limited partner.

In October 1986 plaintiff made a public offering of
limited partnership interests, and by November 28 more
than 50% of the interests were conveyed to third parties,
with 80% of the transferees alleged to be nonresidents of
the State of New York.

THE STATUTE

Pursuant to the authority set forth in section 1201 of
the Tax Law, in July 1986 the City of New York enacted
Local Laws, 1986, No. 23 to extend the RPTT to trans-
fers of controlling economic interests in partnerships
which own real [***4] property situated in the city.
However, the law was declared invalid because the no-
tice of the required public hearing was defective. (See,
41 Kew Gardens Rd. Assocs. v Tyburski, NYLJ, Oct. 3,
1986, at 16, col 2 [Sup Ct, Queens County], affd 124
AD2d 553 [2d Dept 1986], lv denied 68 NY2d 612.)
Thereafter, in December 1986, Local Laws, 1986, No. 71
of the City of New York was enacted, which contained
language identical to that of Local Law No. 23, and was
applicable to conveyances made on or after July 13,
1986, the effective date of the defective statute.

Under the statute (Administrative Code of City of
New York § 11-2102 [b] [1]), a transfer tax is imposed
"on each instrument or transaction * * * whereby any
economic interest in real property is transferred".
"Economic interest in real property" is defined as the
"ownership of shares of stock in a corporation which
owns real property; the ownership of an ["443] interest
or interests in a partnership, association or other un-
corporated entity which owns real property; and the
ownership of a beneficial interest or interests in a trust
which owns real property." (Administrative Code
[***5] § 11-2101 [6].)

The term "transferred" includes the "transfers or is-
suance of shares of stock in a corporation, interest or
interests in a partnership, association or other unincor-
porated entity * * * whether made * * * in one or several
related transactions, which shares of stock or interest
or interests constitute a controlling interest in such corpora-
tion, partnership, association, trust or other entity." (Ad-
ministrative Code § 11-2101 [7].) "Controlling interest"
in the case of a partnership means "fifty percent or more
of the capital, profits or beneficial interest in such part-
nership". (Administrative Code § 11-2101 [8].)

[***716] On December 16, 1986 the City Depart-
ment of Finance published Real Property Transfer Tax
Information Bulletin No. 2, which gave numerous hypo-
thetical examples of the application of the RPTT
amendments. Two of the examples dealt with two-tier
structures of the type presented here, one entity owning
another entity which in turn owns real property. The
defendants' position, as demonstrated in that bulletin, is
that the sale of a controlling interest in the first entity (which
does not own realty) is subject to the RPTT if that entity
is a passive holding company [***6] whose sole asset
is its interest in the other entity which owns New York
City real property. There would be no tax, according to
the bulletin, if the first entity engaged in any significant
business activities other than its ownership of the other
entity.

In February 1987, plaintiff paid $1,532,854 under
protest in payment of the asserted RPTT liability on such
transfers. In April 1987, plaintiff made a claim for the
refund of this amount and commenced this action.

THE CONTENTIONS OF THE PARTIES

Plaintiff asserts that: (i) the RPTT has no application
to it since it does not own any real property; (ii) the sales
of partnership interests do not constitute conveyances of
economic interests in real property; (iii) the imposition of
the tax violates the State constitutional prohibition
against an ad valorem tax on intangible personal proper-
ity; (iv) the application of the tax to partnership admis-
sions violates the Due Process and Commerce Clauses of
the US Constitution; and (v) [*444] the retroactive
application of the statute violates the Due Process
Clauses of the NY and US Constitutions.

The city takes the position that, although the trans-
action does not fall within the literal [***7] wording of
the statute in that plaintiff does not hold title to any
real property, the court should look behind the transac-
tion and give effect to the economic realities and not
permit the use of a dummy or shell entity to avoid pay-
ment of the tax.

DISCUSSION

"As a general rule, a statute which levies a tax is to
be construed most strongly against the taxing authority
and in favor of the taxpayer". ( Matter of SIN, Inc. v De-
partment of Fin., 126 AD2d 339, 343 [1st Dept 1987],
affd 71 NY2d 616 [1988].) However, here the issue does
not revolve around the meaning of the words, but rather
whether in administering the statute the city may suc-
sessfully attack, as a tax avoidance device, the use of a
shell partnership to separate title ownership from the
entity in which the economic interests with respect thereto
were transferred.

The enabling act for Local Law No. 71 (Tax Law §
1201 [b]) was passed in 1981, with the impetus generally
considered to have been the sale of the Pan Am Building
in New York City by the transfer of stock, which enabled
the seller to avoid the imposition of the RPTT. In ap-
proving the bill, Governor Carey wrote (1981 McKinney's **8** Session Laws of NY, at 2636-2637):

"The State has for some time authorized the imposition of a tax on transfers of real property in New York City. At present, the tax is imposed only with respect to direct conveyances of real property in which the transfer is actually reflected in a deed. It is common practice, however, for property owners to effectively transfer property while avoiding the tax by selling the property in transactions not involving the recording of a deed. Where property is owned by a corporation, for example, the tax may be avoided by selling the corporation's stock.

"This bill closes that loophole by permitting the taxation of transfers of controlling interests in corporations, partnerships, associations, trusts and other entities which own real property. As a result, transactions which effectively, albeit indirectly, convey property will now be taxed."

[**717**] In his sponsoring bill memorandum (1981 NY Legis Ann, at 480) Senator Marchi states that "the bill is designed to give [*445] effect to the substance of these transactions, rather than to their mere legal form", and to close the loophole whereby "real estate can be effectively conveyed tax-free by a sale [*446] of the ownership interests in the partnership or other entity."

Plaintiff argues that because article 31-B of the Tax Law (Tax on Gains Derived from Certain Real Property Transfers) uses language somewhat different from that of Tax Law § 1201 (b), it shows "that the legislature meant to exclude a transaction such as partnership admissions from the reach of the RPTT."

Clearly the statute would apply to a transfer of a controlling interest in a partnership that owned real property. To accept plaintiff's argument would ascribe to the Legislature an intent to permit the creation of shell entities to avoid taxation when the whole purpose of the legislation, as stated by the Governor and the Senate sponsor, is to tax transactions which effectively, but indirectly, convey real property.

Tax legislation should be implemented in a manner that gives effect to the economic substance of a transaction. (See, e.g., Matter of Petrolane Northeast Gas Serv. v State Tax Commn., 79 AD2d 1043 [3d Dept 1981], lv denied 53 NY2d 601; Matter of Credit Bur. v State Tax Commn., 105 AD2d 1042, 1043 [3d Dept 1984]; Matter of Chemical Bank v Tully, 94 AD2d 1, 3 [*9**][**10] [3d Dept 1983].) The RPTT would be rendered a nullity if it could be avoided simply by holding the real property through passive corporations or partnerships.

Courts have frequently invoked the substance-over-form rule to disallow taxpayers' use of dummy or shell entities which have a tax avoidance effect. For example, in Higgins v Smith (308 U.S. 473 [1940]), a loss deduction was disallowed on the transfer of depreciated property from the taxpayer to a wholly owned corporation. Although corporate formalities were fully observed, the court held that the corporate existence was without economic substance and applied the general rule that a taxing authority may give effect to the economic substance of a transaction regardless of the form chosen by the taxpayer, stating: "On the other hand, the Government may not be required to acquiesce in the taxpayer's election of that form for doing business which is most advantageous to him. The Government may look at actualities and upon determination that the form employed for doing business or carrying out the challenged tax event is unreal or a sham may sustain or disregard the effect of the fiction as best serves the [*446] [***11] purposes of the tax statute." (Supra, at 477.) See also, Molina Props. v Commissioner (319 U.S. 436, 439 [1943]) where it was said that "in matters relating to the revenue, the corporate form may be disregarded where it is a sham or unreal." This approach also has been followed to prohibit the use of illusory partnerships for tax avoidance. (See, e.g., Haggard v Wood, 298 F2d 24, 26 [9th Cir 1961]; Trousdale v Commissioner of Internal Revenue, 219 F2d 563 [9th Cir 1955]; Matter of Liquor Stores Servs. Co. v State Tax Commn., 46 AD2d 701 [3d Dept 1974].)

In Matter of Ausbrooks v Chu (66 NY2d 281 [1985]) a limited partner was denied a nonresident income tax deduction because his interest in a New York limited partnership was found to be passive since its business was in fact conducted by an out-of-State partnership owned by the New York partnership.

Here the sales of plaintiff's partnership interests were, in essence, the sales of interests in real property situated in New York City, and the economic value of such interests was derived solely from that parcel of realty. [***12] The purchasers of limited partnership interests will obtain their profits [*7**18] exclusively from revenues, capital appreciation and tax benefits attributable to that property. This is precisely the sort of transaction the RPTT amendment in question was intended to reach, and these transactions would have come within the literal terms of the amendment but for the existence of plaintiff, a passive holding company which is engaged in no independent business activity. Accordingly, the court will disregard the passive shell entity, and permit the city to treat the transfers of partnership interests in plaintiff as if they were transfers of interests in the owning partnership.

Contrary to plaintiff's argument, the RPTT amendment at issue does not impose an ad valorem tax on intangible personal property as it possesses none of the
characteristics of such a tax. In *Franklin Soc'y for Bldg. & Sav. v Bennett* (282 NY 79 [1939], appeal dismissed 309 U.S. 640) the court discussed the essential characteristics of an ad valorem property tax in relation to article XVI, § 3 of the NY Constitution. That section provides, in pertinent part, that "intangible personal [*][13] property shall not be taxed ad valorem nor shall any excise tax be levied solely because of the ownership or possession thereof". The two salient features of the mortgage recording tax at issue there which prevented it from coming within the constitutional prohibition were that it was levied not for mere [*][447] ownership or possession of a mortgage, but rather for the right to record the mortgage, and because the tax was imposed only once, at the time of recording. Similarly, the RPTT is also not levied for mere ownership or possession nor imposed at any regular interval, but only upon the occurrence of a single event: to wit, a transfer. Therefore taxation of the transfers of the limited partnership interests does not violate the ad valorem constitutional prohibition.

Nor does the RPTT violate either the Commerce or Due Process Clauses of the Federal Constitution. In *Complete Auto Tr. v Brady* (430 U.S. 274 [1977], reh' d denied 430 U.S. 976) it was held that a State may properly impose a tax on receipts from interstate commerce "when the tax is applied to an activity with a substantial nexus with the taxing State, is fairly apportioned, [*][14] does not discriminate against interstate commerce, and is fairly related to the services provided by the State." (*Supra*, at 279; see also, *Mobil Oil Corp. v Commissioner of Taxes*, 445 U.S. 425, 443 [1980]; *Matter of Weil v Chu*, 120 AD2d 781, 784 [3d Dept 1986], *affd* 70 NY2d 783 [1987].)

The transaction here is the syndication of New York City real estate. Without question New York City is the predominant place where each buyer of a partnership share in plaintiff "in every practical sense invokes and enjoys the protection of the laws, and in consequence realizes the economic advantages of his ownership." (*First Bank Corp. v Minnesota*, 301 U.S. 234, 241 [1937].)

Nor can it be said that the RPTT burdens interstate commerce. On the contrary, the tax is fairly related to the services provided by New York City. The RPTT amendment was intended to tax direct and indirect transfers of New York City real estate on an equal basis, the measure of such tax being the consideration paid.

As to retroactivity, provisions in tax statutes for such an application have been found constitutional. (*See*, e.g., *Welch v Henry*, 305 U.S. 134 [*][15] [1938]; *Canisius Coll. v United States*, 799 F2d 18, 25-26 [2d Cir 1986], *cert denied* 481 U.S. 1014 [1987]; *Matter of Rep-

In *Replan Dev. (supra, at 455)* the Court of Appeals discussed the standards for a retroactive tax statute passing constitutional scrutiny stating:

"Retroactivity provisions in tax statutes, if for a short period, are generally valid * * * and ordinarily are upheld against due process challenges, unless in [*][16] light of 'the nature of the tax and the circumstances in which it is laid', the retroactivity of the law is 'so harsh and oppressive as to transgress the constitutional limitation' * * * Whether the retroactive application of a tax statute is 'harsh and oppressive' is a 'question of degree' * * *"

"In reaching the appropriate balance, several factors may be considered. First, and perhaps predominant, is the taxpayer's forewarning of a change in the legislation and the reasonableness of his reliance on the old law * * * This inquiry focuses on whether 'the taxpayer's 'reliance' has been justified under all the circumstances of the case and whether his 'expectations as to taxation [have been] unreasonably disappointed'" * * * Additionally, the length of the retroactive period often has been a crucial factor, and excessive periods have been held to unconstitutionally deprive taxpayers of a reasonable expectation that they 'will secure repose from the taxation of transactions which have, in all probability, been long forgotten' * * * Finally, the public purpose for retroactive application is important because of the taxing authority's legitimate concern that 'evasive measures taken [*][17] after introduction of a bill but before enactment might frustrate the purpose of the legislation'".

Here, the relevant considerations do not militate in the taxpayer's favor. The public was on notice at all times during the retroactive period of the city's intention to impose a tax on transfers of economic interests in real property. It was only the inadvertent failure to give proper notice of the public hearing regarding Local Law No. 23 which occasioned the retroactive period of five months, which is not excessive, falling within the calendar year of the enactment of the legislation.

The public purpose for the amendment (to close what was perceived to be a loophole in the law) is a rea-
sonable basis on [*449] which to legislate retroactively. (See, Matter of Epstein v New York State Tax Commn., 132 AD2d 52, 55 [3d Dept 1987].) Accordingly, plaintiff's motion for summary judgment is denied and defendants' cross motion for summary judgment is granted.
EXHIBIT C
New York City Tax Appeals Tribunal

In the Matter of

CORWOOD ENTERPRISES, INC., ET AL.
Petitioners.

DECISION

TAT (E) 00-39 (RP), ET AL.

Corwood Enterprises, Inc. ("Corwood"); Edgemont Enterprises, Inc. ("Edgemont"); Bosworth Enterprises, Inc. ("Bosworth"); Surrey Hill Enterprises, Inc. ("Surrey Hill"); and Milewood International, Inc. ("Milewood"); 1 [collectively, "Petitioners"] filed an Exception to the Determination of an Administrative Law Judge ("ALJ") dated March 11, 2004. The ALJ's Determination denied the Petition filed by each of the Petitioners requesting a refund of New York City Real Property Transfer Tax ("RPTT") paid in connection with certain transfers of stock that occurred on March 12, 1999, described below, and sustained the Notices of Disallowance, dated August 1, 2000, issued by the New York City Department of Finance (the "Department") to each of the Petitioners.

Petitioners appeared by Herbert Teitelbaum, Esq. and David P. Kasakove, Esq. of Bryan Cave LLP and the Commissioner of Finance of the City of New York (the "Commissioner" or "Respondent") appeared by Robert F. Firestone, Esq, Senior Tax Counsel; and Martin Nussbaum, Esq., Assistant Corporation Counsel, New York City Law

1These matters have been designated, respectively, TAT(E) 00-39 (RP); TAT(E) 00-40 (RP); TAT(E) 00-41(RP); TAT(E) 00-42(RP); and TAT(E) 00-43(RP).
Department. Both parties filed briefs and/or letter briefs and oral argument was held by the Tribunal.

**Corporate Structure**

Each Petitioner is an International Business Company ("IBC") incorporated in the British Virgin Islands ("BVI") in 1997 pursuant to the BVI International Business Companies Act. The registered office of each Petitioner was located in the BVI. Each Petitioner was listed on the BVI's register of IBCs as being in good legal standing and as having paid all fees, license fees, and penalties due and payable under the BVI International Business Companies Act.

Petitioners were the indirect owners, through two tiers of intervening entities, of Hotel 57 LLC ("LLC"), a limited liability company formed under the laws of the State of Delaware on June 11, 1996. LLC had a registered office in Delaware and was in good

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3For purposes of this decision, we have generally adopted all of the ALJ's Findings of Fact except as noted in footnote 5 of this decision. Only those findings germane to this decision have been restated above and, in some instances, those findings have been paraphrased. The remaining Findings of Fact of the ALJ can be found in the ALJ's Determination dated March 11, 2004. References to ownership status and activities are for all periods or dates pertinent to this Decision. Pursuant to a letter dated April 8, 2005 and the accompanying Amended Attachment to Notice of Exception, Petitioners took specific exception to four of the ALJ's Findings of Fact. Each of Petitioners' requested modifications to the ALJ's findings is addressed in this decision. See footnotes 3, 6, 7 and 8, infra.

3Petitioners take exception to the ALJ's Finding of Fact 2 to the extent that such finding stated that "Petitioners were the indirect owners, through two tiers of intervening entities, of Hotel 57 LLC ("LLC"), a limited liability company formed under the laws of the State of Delaware on June 11, 1996." Petitioners contend that this finding of the ALJ is not supported by the record and that it should be replaced by a finding setting forth the direct ownership interests of the five Delaware corporations in LLC. Petitioners also seek to amend the finding by adding the statement that LLC "was not Petitioners' agent." We decline to modify the ALJ's finding since Petitioners offer no support for their assertion that the ALJ's finding is not supported by the record. Furthermore, the ALJ's Findings of Fact clearly and concisely set forth the relationships of the various entities. Lastly, Petitioners' requested finding that LLC "was not Petitioners' agent" is clearly not
supported by those paragraphs of the Parties' Stipulation of Facts cited by Petitioners.
standing and had a legal corporate existence under the laws of the State of Delaware, having filed its annual reports and having paid all applicable franchise taxes.

From August 1, 1996 to March 12, 1999, LLC owned the Four Seasons Hotel, including the underlying real property, located at 57 East 57th Street, New York, New York (the "Four Seasons"). LLC was engaged in no business other than in relation to its ownership of the Four Seasons.

Each Petitioner owned all of the stock of a BVI corporation (collectively the "Lower Tier BVI Subs") as follows: Corwood owned 100% of Kaywood Enterprises, Inc. ("Kaywood"); Edgemont owned 100% of Kilborn Trading Corp. ("Kilborn"); Bosworth owned 100% of Romney International Limited ("Romney"); Surrey Hill owned 100% of Expert Tips Limited ("Expert Tips"); and Milewood owned 100% of Brantwood Enterprises, Inc. ("Brantwood"). Each of the Lower Tier BVI Subs is also an IBC incorporated in the BVI pursuant to the BVI International Business Companies Act. The registered office of each of the Lower Tier BVI Subs was located in the BVI. Each of the Lower Tier BVI Subs was listed on the BVI's register of IBCs as being in good legal standing and as having paid all fees, license fees, and penalties due and payable under the BVI International Business Companies Act.

Each of the Lower Tier BVI Subs owned all of the stock of a Delaware corporation (collectively the "Delaware Subs") as follows: Kaywood owned 100% of Hotel 57 Corp. II, Inc. ("Hotel 57 Corp. II"); Kilborn owned 100% of Hotel 57 Corp. III, Inc. ("Hotel 57 Corp. III"); Romney owned 100% of Hotel 57 Corp. IV, Inc. ("Hotel 57 Corp. IV"); Expert Tips owned 100% of Hotel 57 Corp. V, Inc. ("Hotel 57 Corp. V"); and Brantwood owned 100% of Hotel 57 Corp. I, Inc. ("Hotel 57 Corp. I"). Each of the Delaware Subs was formed under the laws of the State of Delaware on June 11, 1996. Each of the Delaware Subs had a
registered office in the State of Delaware and was in good standing and had a legal corporate existence under the laws of the State of Delaware, having filed its annual reports and having paid all applicable franchise taxes.

The Delaware Subs owned all of the interests in LLC. The Delaware Subs' ownership interests in LLC (which represented the value, vote and profits of LLC) were as follows:

<table>
<thead>
<tr>
<th>Entity</th>
<th>Percent Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hotel 57 Corp. I</td>
<td>50</td>
</tr>
<tr>
<td>Hotel 57 Corp. II</td>
<td>10</td>
</tr>
<tr>
<td>Hotel 57 Corp. III</td>
<td>5</td>
</tr>
<tr>
<td>Hotel 57 Corp. IV</td>
<td>25</td>
</tr>
<tr>
<td>Hotel 57 Corp. V</td>
<td>10</td>
</tr>
<tr>
<td>Total</td>
<td>100%</td>
</tr>
</tbody>
</table>

LLC was treated for federal, state and local income tax purposes as a partnership, and annually filed federal Form 1065, U.S. Partnership Return of Income, Form IT-204, New York State Partnership Return, and Form NYC 204, Unincorporated Business Tax Return. Each Delaware Sub was treated as a partner in LLC for federal, state and local tax purposes in proportion to its respective percentage ownership interest in LLC.
The diagram below illustrates the corporate structure described above.
The Petitioners sold all of their shares in the Lower Tier BVI Subs (the "Transfers") for an aggregate of $275 million (the "Purchase Price") to 57 BB Property, L.L.C. ("Purchaser"), a Delaware limited liability company, pursuant to a Stock Sale and Purchase Agreement dated February 2, 1999 (the "Contract"). The closing of the Transfers took place on March 12, 1999 in Chicago, Illinois (the "Closing").

**Operation of the Four Seasons**

LLC purchased the Four Seasons pursuant to a purchase agreement dated June 18, 1996 ("Purchase Agreement") for $195 million.

LLC entered into a Second Amended and Restated Hotel Management Agreement, dated August 1, 1996, with Regent International Hotels, Inc. ("Regent") concerning the management of the Four Seasons (the "Hotel Management Agreement"). Regent managed the Four Seasons pursuant to this agreement. Milewood's director, Ambrose Cheung Wing Sum ("Mr. Cheung"), negotiated the Hotel Management Agreement with Regent. (Tr. 1\textsuperscript{4} at 166.) Petitioners played no other role in the management of the Four Seasons.

None of the Petitioners engaged in any business other than in relation to its ownership of the stock of its Lower Tier BVI Sub, including, without limitation, taking all actions necessary to carry out the terms of the Transfers pursuant to the terms of the Contract.

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\textsuperscript{4}The transcript pagination for both the first and second day of the hearing began with page 1. Accordingly, transcript pages for the first day of the hearing are designated "Tr. 1" and transcript pages for
the second day of the hearing are designated "Tr. 2".
Except for activities relating to the marketing of the Four Seasons and actions necessary to carry out the Transfers pursuant to the Contract that took place in New York City (the "City") as described below, each Petitioner conducted its only business, which was to hold the shares of its Lower Tier BVI Sub, in Hong Kong. No Petitioner directly owned any real estate in the City. Apart from their respective indirect interests in LLC, no Petitioner ever held an ownership interest in any other kind of property or other business in the City. No Petitioner ever held a company meeting in the City.

None of the Petitioners ever filed an application for authority to do business in New York State (the "State") with the Department of State of New York.

None of Petitioners ever filed any income tax returns in the United States.

None of the Lower Tier BVI Subs engaged in any business other than in relationship to its ownership of its Delaware Sub, including, without limitation, taking all actions necessary, if any, to carry out the Transfers pursuant to the terms of the Contract.

None of the Delaware Subs engaged in any business other than in relation to its ownership interest in LLC, including, without limitation, taking all actions necessary, if any, to carry out the Transfers pursuant to the terms of the Contract.

All of the Petitioners, the Lower Tier BVI Subs and the Delaware Subs were single purpose entities in the above described corporate structure. This corporate structure was

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3We have modified the ALJ's Finding of Fact 16 to include the fact that activities relating to the marketing of the Four Seasons as well those necessary to carry out, effectuate, and consummate all terms of the Transfers pursuant to the terms of the Contract took place in the City. The modification was necessary in order to accurately reflect the Record and in order for the ALJ's Finding of Fact 16 to be consistent with other Findings of Fact of the ALJ where these activities are considered to be part of the business of
Petitioners. See, ALJ's Finding of Fact 15; infra, pp. 7-18 and; discussion, infra, pp. 41-43.
intended to confer tax benefits, to insulate the ultimate beneficial owners of the Four Seasons from liability and to make it possible for one Petitioner to dispose of its investment in the Four Seasons without disrupting the investments of the other Petitioners.

**The Transfers**

Vincent Kinson Ma ("Mr. Ma") was an officer of Corwood. During the period 1996 to 1999, Mr. Ma resided in Hong Kong. Mr. Ma executed the Contract on behalf of Corwood in Hong Kong.

Jane Chong ("Ms. Chong"), a Hong Kong resident, was an officer of Edgemont. Ms. Chong was also an officer of Kilburn, Edgemont's Lower Tier BVI Sub, and of Hotel 57 Corp. III, Kilburn's Delaware Sub. Ms. Chong executed the Contract on behalf of Edgemont in Hong Kong.

Pei Cheng Ming Michael a/k/a Michael C. Pei ("Mr. Pei") was secretary/treasurer of Bosworth. Mr. Pei was a resident of Hong Kong. Mr. Pei executed the Contract on behalf of Bosworth in Hong Kong.

James Pei Chun Tien ("Mr. Tien") was a Director and the President of Surrey Hill. Mr. Tien executed the Contract on behalf of Surrey Hill in Hong Kong.

Allan Yaf Wah Chung Li ("Mr. Li"), a Hong Kong resident, was Milewood's Assistant Secretary. Mr. Li was also an officer of Brantwood, Milewood's Lower Tier BVI Sub. Mr. Cheung, the director of Milewood, signed the Contract on behalf of
Milewood. Mr. Li testified at the hearing that he believed Mr. Cheung executed the Contract in Hong Kong.

Each Petitioner had one witness testify at the hearing: Mr. Ma for Corwood, Ms. Chong for Edgemont, Mr. Pei for Bosworth, Patrick Chow ("Mr. Chow"), a resident of Hong Kong, as vice-president of Surrey Hill for Surrey Hill, and Mr. Li for Milewood (collectively "Petitioners' Witnesses"). Each of Petitioners' Witnesses was an officer of his or her respective Petitioner and attended the Closing on behalf of that Petitioner. None of Petitioners' Witnesses was a director or shareholder of his or her respective Petitioner corporation. Each of Petitioners' Witnesses had a background in accounting, business, banking, and/or finance and was responsible for overseeing his or her respective Petitioner's investment in its Lower Tier BVI Sub. Each of Petitioners' Witnesses had a very limited knowledge of the Transfers. None of Petitioners' Witnesses purported to be knowledgeable about how the Transfers were marketed or provided a detailed explanation of what role the various "advisors" and "agents," discussed below, played in the Transfers.

The ALJ noted that as to certain of the factual matters that were most relevant to her factual conclusions, Petitioners, who have the burden of proof in this matter (see, New York City Charter §170.d), provided witnesses who lacked, or professed to lack, knowledge of the essential facts. According to the ALJ, this was particularly disconcerting with respect to Mr. Li, since the record indicates that Milewood, the Petitioner for which he served as an officer, owned an indirect 50% interest in the Four Seasons and was the dominant force in the decision-making regarding the Transfers.

Mr. Li testified that since "the hotel has international stature," Petitioners were advised to market the hotel internationally as this was the "proper way of selling this hotel
or selling our interest in the shares." Petitioners retained an agent, Morgan Stanley Dean Witter ("Morgan Stanley"), to assist in the marketing and to prepare a marketing brochure (the "Marketing Memorandum"). Petitioners sent the Marketing Memorandum to selected purchasers. 6 (Tr. 1 at 148.)

The first paragraph of the Marketing Memorandum states that it is based on:

information provided by Hotel 57 L.L.C. (together with its direct and indirect members and shareholders, the "Company" or "Hotel 57 L.L.C."). a Delaware limited liability company, the owner of the Four Seasons Hotel New York (the "Hotel"). It is being delivered on behalf of the Company by Morgan Stanley Dean Witter ("Morgan Stanley") upon receipt of a signed Confidentiality Agreement to a limited number of parties who may be interested in a transaction involving the Company and the Hotel. [Emphasis added.]

Page 00581 of the Marketing Memorandum states that:

Hotel 57 L.L.C. . . . the owner of the Four Seasons Hotel New York, has authorized Morgan Stanley to act as the Company's exclusive advisor and agent in connection with the potential sale of the Company as described in this Memorandum. [Emphasis added.]

In a section entitled "Proposed Transaction," on page 00584 of the Marketing Memorandum, the proposed transaction is described as follows:

6Petitioners also took exception to this Finding of Fact, ALJ's Finding of Fact 41, to the extent that it stated that "Petitioners retained an agent, Morgan Stanley, to assist in the marketing and to prepare a marketing brochure (the "Marketing Memorandum"). Petitioners sent the Marketing Memorandum to selected purchasers." This finding is clearly supported by the testimony of Mr. Li as referenced by the ALJ (Tr. 1 at 148). Petitioners have requested that Finding of Fact 41 be modified. The ALJ's Findings of Fact concerning the Marketing Memorandum accurately present the facts relevant to the Marketing Memorandum. Thus, we reject Petitioners' request to modify the ALJ's Findings of Fact as not supported by, and
inconsistent with, the Record below.
Morgan Stanley has been retained by **Hotel 57 L.L.C. as its exclusive financial advisor and agent** in the potential sale of the Company. The proposed transaction is to sell the stock of five off-shore entities incorporated in the British Virgin Islands that own individually the interests in five United States corporations that wholly own in the aggregate all of the membership interests in Hotel 57 L.L.C., the owner of the Hotel. See Section III - "Summary of the Ownership Structure".

The Marketing Memorandum is a thirty-three page marketing brochure. Most of the brochure consists of a detailed description and photographs of the Four Seasons including: rooms, meeting rooms and various amenities, extensive information about the financial condition of the hotel's operations, the Management Agreement and information about certain ground leases.

The Hong Kong office of Morgan Stanley prepared the Marketing Memorandum. However, all communications, inquiries and requests for information concerning the material in the Marketing Memorandum are directed to a Morgan Stanley address and telephone number in the City and to Morgan Stanley personnel at telephone numbers in the City. (Marketing Memorandum at 00577.) The Marketing Memorandum also states that a prospective purchaser wishing to proceed should submit a preliminary proposal to a Morgan Stanley address in the City. (Marketing Memorandum at 00581.) Mr. Li testified that Morgan Stanley initially attempted to market the deal but "I think they had no success, and thereafter [sic] a few months, we terminated the engagement." (Tr. 1 at 168-169.)
However, notwithstanding Mr. Li's testimony, Section 16.18 of the Contract states:

. . . Purchaser or its Affiliate dealt with Morgan Stanley Dean Witter with respect to entering into a confidentiality agreement for this transaction. The parties agree that Purchaser is not responsible for any fees or commissions to Morgan Stanley Dean Witter. Sellers [defined as Petitioners herein] have retained PKF Consulting ["PKF"] and Polylinks International Ltd. ["Polylinks"] in connection with the transactions contemplated by the [Contract] . . . [Emphasis added.]

The Closing Statement for the Transfers, dated March 12, 1999, in which the Petitioners are identified as the "Sellers," describes the "Sellers' Agent" as "PKF By: John Fox" and "Sellers' Advisors" as "Polylinks International Ltd. By: Margaret Lau, Daniel Yu, Beatrice Wen and Maureen Wong."

Polylinks was variously characterized by Petitioners' Witnesses as the "advisor," "broker," or "consultant" with respect to the Transfers. (Tr. 1 at 52, 102-103, Tr. 2 at 39-40.) Polylinks was compensated directly by the Petitioners for its services in marketing the Four Seasons and effectuating a sale of the shares of the Lower Tier BVI Subs.7 (Tr. 1 at 55-56, 103, 136.)

7Petitioners took exception to the ALJ's Finding of Fact 50 to the extent that it stated that "Polylinks was compensated directly by the Petitioners for its services in marketing the Four Seasons and effectuating a sale of the shares of the Lower Tier BVI Subs." Petitioners want to replace this finding with the sentence that "Polylinks, with offices located exclusively in Hong Kong, served as an advisor/consultant to Petitioners, not as a real estate broker, and received a fee, not a commission, for services rendered with respect to the subject transactions." The ALJ's finding is supported by the testimony referenced on the transcript pages and such finding accurately reflects the combined testimony of the various witnesses whose testimony was not
always consistent.
PKF was hired through Polylinks to assist with the marketing of the Four Seasons and to provide information to prospective purchasers.8 (Tr. 1 at 52-55.) Ms. Chong explained that PKF was hired because "Polylinks was out of Hong Kong, and they couldn't possibly attend to all of the day-to-day or whatever, all of the myriad number of tasks that they needed to show the hotel." (Tr. 1 at 74.)

In a letter agreement, dated February 3, 1998, on the letterhead of PKF’s San Francisco office to Daniel Yiu at Polylinks at a Hong Kong address (the "PKF Agreement"), the parties agreed that PKF would act as "confidential asset advisor" to LLC with respect to the Four Seasons. Mr. Yiu executed the PKF Agreement as "Polylinks International Limited on behalf of Hotel 57 LLC." Among the services PKF agreed to provide were:

1. Analyzing the Implications of Holding or Selling the Asset [the Four Seasons],

2. Assisting in Preparing the Property for Sale (if Appropriate),

3. Communicating that Decision to a Carefully Selected Market of Investors,

4. Monitoring the Sales/Bidding Process to Maximize the Value of the Asset, [and]

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8Petitioners took exception to the ALJ's Finding of Fact 53 to the extent that such finding stated that "PKF was hired through Polylinks to assist with the marketing of the Four Seasons and to provide information to prospective purchasers." Petitioners request that this finding be replaced by the statement that "(a) PKF was retained by Hotel 57 L.L.C. not Petitioners; (b) PKF's principal offices were in San Francisco not New York City; and (c) PKF served as the 'confidential asset advisor' and did not act, and was not compensated, as a real estate agent or broker." Again, we decline to modify the ALJ's Findings of Fact as we find that her findings are reflective of the Record in this matter and especially the testimony referenced.
above.
5. Assisting in monitoring the due diligence exercises conducted by potential buyers.

The PKF Agreement provided that "[t]he Senior Vice President and Director of [PKF's] New York office, John Fox, will be assigned as the Four Seasons' on-site liaison with you and/or your designated representatives." PKF was to be compensated by a fixed fee for services rendered and not by a commission based on a sale.

The importance of having someone on site in the City to show the Four Seasons is illustrated by the following exchanges on cross examination of Mr. Li:

Q. (Mr. Nussbaum) Were you made aware of which particular prospective purchasers were visiting the hotel or inspecting the hotel?

A. (Mr. Li) I think any serious purchaser would look at the hotel and inspect the hotel.

Q. How would they get such permission to enter the premises?

A. They were qualified by the agents, because they came up with the price and the agents told us they were credible purchasers with the ability and capacity to buy these interests. (Tr. 1 at 170-171.)

... 

Q. Did you help in any way facilitate or did you help facilitate any purchaser viewing the Four Seasons Hotel?

A. No, the agents do that.
Q. Did you provide the authorization to those agents? In other words, did you authorize the agent to act on your behalf to do that?

A. I am not sure whether I did personally.

Q. Did another officer or director of Milewood?

A. I am not sure. (Tr. 1 at 153-154.)

Ms. Chong, an officer of Edgemont, received marketing information from Polylinks and PKF. (Tr. 1 at 49.) She was also apprised by Polylinks and/or PKF that arrangements were made for prospective purchasers to be shown around the Four Seasons.

Ms. Chong was in the City on at least two occasions when she met with prospective purchasers. In one case she met the prospective purchaser at the office of Robinson Silverman Pearce Aronson & Berman ("Petitioners' Attorneys"). In the other case the location was at an airport hotel near J.F.K. Airport. (Tr. 1 at 50-51.)

Ms. Chong was also in the City for one day just prior to attending the Closing in Chicago, during which time an inventory of the Four Seasons was taken and certain closing adjustments were computed. She testified that she was in the City to receive the attorneys' advice and to give instructions as to how certain final adjustments such as inventory, receivables, taxes and other cut-off issues should be dealt with. (Tr. 1 at 45-46.)

In early 1999, Petitioners' Witnesses attended a meeting with Petitioners' Attorneys, at their offices in the City to discuss various issues relating to the Contract. The Purchaser was not present at that meeting. (Tr. 1 at 96, 123, 138.)
The parties stipulated that with respect to the Contract, Petitioners' Attorneys represented the Petitioners, and attorneys at the firms of Levenfeld Glassberg Tuchman & Goldstein and Kubasiak, Cremieux, Fylstra, Reizen & Rotunno, both located in Chicago, Illinois, represented the Purchaser. Negotiations concerning the terms of the Contract took place between parties' counsel by telephone and in one or more meetings in the City.

The Contract

The Contract is designated a "Stock Sale and Purchase Agreement" and provides for the sale by Petitioners of the shares in the Lower Tier BVI Subs. (Contract, section 2.1.) Petitioners are designated "Sellers." (Contract, opening paragraph.) The five Lower Tier BVI Subs, the shares of which constitute the property being sold, are defined as "Seller BVI Companies." (Contract, section 1.81.) The five Delaware Subs are defined as "Seller US Companies." (Contract, section 1.88.) LLC is defined as "Owner." (Contract, section 1.51.)

Article IV of the Contract states that:

The parties hereto acknowledge and agree that although this transaction is a stock purchase, they wish the adjustments to the Cash Balance [the portion of the purchase price to be paid at the Closing] to be made as if the transaction were an acquisition of the Property [the Four Seasons, personal property, accounts receivable, etc.]

For example, real estate taxes were required to be prorated as if the real property, rather than the shares of the Lower Tier BVI Subs, had been sold. (Contract, section 4.1.)
In addition, Article V of the Contract, dealing with title and permitted exceptions, provides that Petitioners are required to provide Purchaser with good title to the real property.

a. It is a condition to Purchaser's obligation to purchase the [shares of the BVI Subs] that on the Closing date the Title Insurer (or Title Insurers) would be prepared to issue to [LLC] a [title insurance policy] . . . (Contract, section 5.1);

b. [Petitioners] shall discharge, or cause [LLC] to discharge, all Voluntary Title Exceptions on or prior to the Closing . . . (Contract, section 5.5); and

c. [Petitioners] shall use a portion of the [sale proceeds] to [discharge any title exceptions] (Contract, section 5.3).

Various portions of the Contract provide that Petitioners were responsible for how the Four Seasons was managed up to the Closing. In numerous places, the Contract provides that the Petitioners are required to "cause Owner" [LLC] to take certain actions required by the Contract relating to the operation of the Four Seasons during the period up to and including the time of the Closing.

The Contract, by its terms, is governed by the substantive laws of New York State. (Contract, section 16.1(a).)

Contract, Section 16.1(b) provides that:

[Petitioners] and Purchasers . . . irrevocably consent and submit to the jurisdiction of any Federal, state, county or municipal court sitting in the State of New York with respect to any action or proceeding brought therein by any party
The Contract provides that each Seller shall pay "Transfer Taxes" and that each Seller shall "pay, indemnify, defend and save harmless Purchaser for the damages arising from Seller's failure to pay its Allocable Share of any Transfer Taxes . . . ." (Contract, Section 11.1(a) and (c)).

Contract, Section 2.2(d) provides that the "Closing Location" is either "(i) the Sellers' counsel's offices in New York City or (ii) the offices of Purchaser's counsel in New York City." However, the Closing actually took place in Chicago.

**Tax Payments and Refund Claims**

In connection with the Transfers a portion of the consideration was apportioned to the real property as follows:

<table>
<thead>
<tr>
<th>Petitioner</th>
<th>Total Consideration</th>
<th>Amount Apportioned to Real Property</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corwood</td>
<td>$27,500,000</td>
<td>$23,607,809.80</td>
</tr>
<tr>
<td>Edgemont</td>
<td>13,750,000</td>
<td>11,803,904.90</td>
</tr>
<tr>
<td>Bosworth</td>
<td>68,750,000</td>
<td>59,019,524.50</td>
</tr>
<tr>
<td>Surrey Hill</td>
<td>27,500,000</td>
<td>23,607,809.50</td>
</tr>
<tr>
<td>Milewood</td>
<td>137,500,000</td>
<td>118,039,049.00</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$275,000,000</strong></td>
<td><strong>$236,078,048.70</strong></td>
</tr>
</tbody>
</table>
We have added this finding of fact in order to more accurately reflect the Record.
Petitioners paid the RPTT, including applicable filing fees, on March 12, 1999, as follows:

<table>
<thead>
<tr>
<th>Location</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corwood</td>
<td>$ 619,730.00</td>
</tr>
<tr>
<td>Edgemont</td>
<td>309,877.50</td>
</tr>
<tr>
<td>Bosworth</td>
<td>1,548,287.51</td>
</tr>
<tr>
<td>Surrey Hill</td>
<td>619,730.00</td>
</tr>
<tr>
<td>Milewood</td>
<td>3,098,550.30</td>
</tr>
</tbody>
</table>

**Total**  $6,196,175.31

Under cover letters dated March 8, 2000, each Petitioner filed a claim for refund of the RPTT paid with respect to the Closing, plus interest. By Notices of Disallowance, dated August 1, 2000, the Department denied each Petitioner's refund claim. On October 26, 2000, each Petitioner timely filed a Petition seeking a refund of the RPTT that it had paid.

**ALJ's Conclusions of Law**

In denying Petitioners' refund claims, the ALJ made the following conclusions of law in her Determination:

1) The RPTT enabling legislation does not preclude the imposition of the RPTT on a transfer that closed outside the City since the provision in question merely limits the imposition of the tax to transfers where the property that is the subject of the transfer is located in the City.
2) The imposition of the RPTT on the Transfers does not violate Article XVI, section 3, of the New York State Constitution because the RPTT is not imposed on the presence in the City of the stock certificates and the RPTT is not an *ad valorem* tax.

3) The imposition of the RPTT on the Transfers does not violate the Due Process Clause of the United States Constitution because (1) the values subject to tax are attributable to the benefits given by the City and (2) Petitioners, through their officers and agents, had the minimum connections with the City necessary for *in personam* jurisdiction.

4) The imposition of the RPTT on the Transfers does not violate the Commerce Clause of the United States Constitution because Petitioners, through their officers and agents, had substantial nexus with the City.

**Arguments on Exception**

On appeal, Petitioners argue that the enabling legislation that authorizes the City to tax transfers of economic interests in real property expressly limits the taxing power to the transfer of economic interests within the City itself. Tax Law §1220 provides that "[a]ny tax imposed under the authority of this article shall apply only within the territorial limits of the city . . . imposing the tax." According to Petitioners, this limitation leads to the conclusion that the City does not have the power to tax Petitioners' transfer of their shares in the Lower Tier BVI Subs to Purchaser (a Delaware limited liability company) since the Closing occurred in Chicago, Illinois.

Petitioners also contend that the imposition of the RPTT on the transfer of stock of a foreign corporation by a foreign corporation is prohibited under Article XVI, Section 3,
of the New York State Constitution, which provides, in relevant part, "Moneys, credits, securities and other intangible personal property within the state not employed in carrying on any business therein by the owner shall be deemed to be located at the domicile of the owner for purposes of taxation . . . ."

In addition, Petitioners argue that the Transfers are not subject to the RPTT because they did not constitute transfers of economic interests in real property. According to Petitioners, the Transfers did not fit within the clear language of the definition of the term "economic interest in real property" \(^{10}\) as they were not transfers of an ownership interest in an entity that owns real property. Although, the Transfers involved the sale of all of Petitioners' shares in the Lower Tier BVI Subs, the Lower Tier BVI Subs did not own any real property.

Petitioners further contend that the application of the RPTT to the sale of shares in foreign corporations, based on the location in the City of real property owned by the foreign corporations, violates the Due Process Clause of the United States Constitution. Petitioners argue that the record does not support the finding that Petitioners had minimum contacts with the City in order to meet constitutional due process requirements for jurisdiction.

Finally, Petitioners claim that the RPTT imposed herein improperly burdens interstate and international commerce, and violates the Commerce Clause of the United States Constitution. Petitioners argue that the record does not support a finding of substantial nexus between Petitioners and the City and the RPTT prevents the Federal Government from speaking with one voice when regulating commercial relations with foreign governments.

\(^{10}\)Section 11-2101.6 of the New York City Administrative Code.
Respondent contends that the ALJ's Determination should be affirmed as the ALJ correctly determined that the imposition of RPTT in the matter at bar was within the scope of the enabling law for the RPTT and did not violate the New York State Constitution or the Due Process or Commerce Clauses of the United States Constitution.

Based on the following, we find that the Transfers are subject to the RPTT and deny Petitioners' refund requests.

Section 11-2102.b of the New York City Administrative Code (the "Code") imposes the RPTT on "each instrument or transaction (unless evidenced by a deed subject to tax under subdivision a), at the time of the transfer, whereby any economic interest in real property is transferred by a grantor to a grantee, where the consideration exceeds twenty-five thousand dollars."

An "instrument" is defined in §11-2101.3 of the Code as "[a]ny document or writing (other than a deed or a will), regardless of where made, executed or delivered, whereby any economic interest in real property is transferred." [Emphasis added.]

Section 11-2101.4 of the Code defines "transaction" as "[a]ny act or acts, regardless of where performed, and whether or not reduced to writing, unless evidenced by a deed or instrument, whereby any economic interest in real property is transferred (other than a transfer pursuant to the laws of intestate succession)." [Emphasis added.]

An "economic interest in real property" is defined in §11-2101.6 of the Code as the "ownership of shares of stock in a corporation which owns real property; the ownership of an interest or interests in a partnership, association or other unincorporated entity
which owns real property; and the ownership of a beneficial interest or interests in a trust which owns real property."

Section 11-2107.7 of the Code states that the terms "transfer" or "transferred", when used in relation to an economic interest in real property, "shall include the transfer or transfers or issuance of shares of stock in a corporation, interest or interests in a partnership, association or other unincorporated entity, or beneficial interests in a trust, whether made by one or several persons, or in one or several related transactions, which shares of stock or interest or interests constitute a controlling interest in such corporation, partnership, association, trust or other entity."

A "controlling interest" is defined in §11-2101.8 of the Code as "[i]n the case of a corporation, fifty percent or more of the total combined voting power of all classes of stock of such corporation, or fifty percent or more of the total fair market value of all classes of stock of such corporation; and, in the case of a partnership, association, trust or other entity, fifty percent or more of the capital, profits or beneficial interest in such partnership, association, trust or other entity."

"Real property" is defined in §11-2101.5 of the Code, in relevant part, as "[e]very estate or right, legal or equitable, present or future, vested or contingent, in lands, tenements or hereditaments, which are located in whole or in part within the city of New York."

The RPTT Rules of the Department ("RPTT Rules") provide in the relevant part of 19 RCNY §23-02, containing the definition of controlling interest, that related transfers are aggregated in order to determine whether a controlling economic interest has been transferred, *i.e.*, whether the fifty percent threshold has been met. Related transfers
include "transfers made pursuant to a plan to either transfer or acquire a controlling economic interest in real property."

The basic facts in the matter at bar, while certainly complex, are not significantly disputed. Petitioners sold to Purchaser all of their shares in five BVI corporations (the Lower Tier BVI Subs); each of which owned one of five Delaware corporations (the Delaware Subs); which together held the total ownership interests in a Delaware limited liability company (LLC); which owned the Four Seasons in the City; to Purchaser for an aggregate price of $275 million. It is clear from the documents submitted into evidence as well as the testimony of Petitioners’ Witnesses that the purpose in selling the shares of the Lower Tier BVI Subs was to bring about the sale of the Four Seasons.

**Enabling Legislation**

The authority of the City to impose the RPTT was originally derived from the enabling legislation set forth as an amendment to Tax Law Article 29 (Tax Law §§1201 et seq.) which was adopted in 1959.11 Petitioners contend that the enabling legislation precludes the imposition of the RPTT on the Transfers because the Closing took place in Chicago, Illinois and the enabling legislation expressly limits the City's taxing power to the transfer of economic interests "within the" City itself. Petitioners assert that the limitation is contained in Tax Law §1220 which provides, in relevant part, that ":[a]ny tax imposed under the authority of this article shall apply only within the territorial limits of the city, county, or school district imposing the tax."

Tax Law §1201(b)(i), in relevant part, permits the City to impose the RPTT on "each deed, other instrument or transaction . . . by which any real property or any
economic interest therein is conveyed or transferred . . . ." In addition, Tax Law §1201(b)(i) also provides, with respect to the RPTT, that:

. . . . Such taxes may be imposed on any conveyance or transfer of real property or interest therein where the real property is located in such city regardless of where transactions, negotiations, transfers of deeds or other actions with regard to the transfer or conveyance take place, subject only to the restrictions contained in section twelve hundred thirty. [providing exemptions for certain governmental and charitable organizations].

The above-referenced sentence was adopted as an amendment\textsuperscript{12} to the enabling legislation in response to the decision in Realty Equities Corporation of New York v. Gerosa, 22 Misc.2d 817 (S. Ct. N.Y. Cty., 1959). Prior to the amendment, the enabling legislation contained the following relevant language:

(3) A tax imposed hereunder shall have application only within the territorial limits of any such city . . . .

. . .

(6) This act shall not authorize the imposition of a tax on any transaction, originating and/or consummated outside of the territorial limits of any such city, notwithstanding that some act be necessarily performed with respect to such transaction within such limits.

\textit{Realty Equities, supra}, involved a transfer of real property located in the City where the deed was delivered outside the City. The case held that the above-quoted subdivision (6) precluded the imposition of the RPTT on such a transfer. Following the 1960 amendment to the enabling act, which specifically addressed subdivision (6) but not
subdivision (3), transfers of real property located in the City were subject to the RPTT notwithstanding that the deeds were delivered outside the City. Samkoff v. Gersosa, 29 Misc.2d. 844 (S. Ct. N.Y. Cty., 1961). The decision in Samkoff, supra at 847-848, states that:

The Legislature in 1959 added a provision to the enabling act granting the power to tax transfers of New York City real property. The court subsequently ruled that the general limitation of existing subdivision (6) rendered such tax invalid when applied to deeds delivered outside the city. The Legislature promptly enacted an act amending the enabling act for the purpose of 'clarifying the scope of the authority' to impose this [RPTT]. It added a sentence to the particular subparagraph dealing with such tax, thus making it clear that the authority to impose this tax, as distinguished from the other taxes provided for in the enabling act, was not intended to be limited to city transactions but rather to embrace all transfers of city real property regardless of the place of the making of the transaction therefor.

Thus, we find, as did the ALJ, that former subdivision 3 (now Tax Law §1220) merely limits the City's imposition of the RPTT to transfers of real property or economic interests in real property where the real property is located in the City. Former subdivision 3 (now Tax Law §1220) does not limit the City's imposition of the RPTT with respect to where the transfer takes place. Since the enabling legislation does not require that a closing occur in the City, the imposition of the RPTT to the Transfers is not outside the scope of the enabling legislation. Therefore, we reject Petitioners' argument that the City cannot tax the Transfers because the Closing occurred in Chicago, Illinois.
State Constitution

Petitioners also assert that Article XVI, section 3, of the State Constitution precludes the imposition of the RPTT on the Transfers. Petitioners rely on the language of the first sentence of the first clause of Article XVI, section 3, which provides that:

Moneys, credits, securities and other intangible personal property within the state not employed in carrying on any business therein by the owner shall be deemed to be located at the domicile of the owner for purposes of taxation,13 and if held in trust, shall not be deemed to be located in this state for purposes of taxation because of the trustee being domiciled in this state, provided that if no other state has jurisdiction to subject such property held in trust to death taxation, it may be deemed property having a taxable situs within this state for purposes of death taxation.

The legislative history of Article XVI, section 3, indicates "that it was designed to assure nonresidents that they could 'keep their money and securities [in New York] without any fear that the established legislative policy [of nontaxability] will be changed' (Journal and Documents, N.Y.S. Const. Conv., 1938, Doc. No. 2, p. 3)." Ampco Printing-Advertisers' Offset Corp. v. City of New York, 14 N.Y.2d 11, 23 (1964), appeal dismissed, 379 U.S. 5 (1964). In the matter at bar, the issue of whether the stock certificates were physically present in the City was never raised and was not argued as a basis for asserting the RPTT.

13As the ALJ noted, Petitioners quoted and relied only on the language of this provision up to this point.
The remainder of Article XVI, section 3, states:

Intangible personal property shall not be taxed ad valorem nor shall any excise tax be levied solely because of the ownership or possession thereof, except that the income therefrom may be taken into consideration in computing any excise tax measured by income generally. Undistributed profits shall not be taxed.

595 Investors Limited Partnership, v. Biderman, 140 Misc.2d 441, 446-447 (S. Ct. N.Y. Cty., 1988) held that:

the RPTT amendment at issue does not impose an ad valorem tax on intangible personal property as it possesses none of the characteristics of such a tax. . . . Similarly, the RPTT is also not levied for mere ownership or possession nor imposed at any regular interval, but only upon the occurrence of a single event: to wit, a transfer.

Thus, we find, as did the ALJ, that Article XVI, section 3, of the State Constitution does not bar the imposition of the RPTT on the Transfers.

**Multi-Tiered Structure**

Section 11-2102.b of the Code imposes a tax on "each instrument or transaction . . . whereby any economic interest in real property is transferred . . . ." The term "economic interest in real property" is defined in §11-2101.6 of the Code as the "ownership of shares of stock in a corporation which owns real property; the ownership of an interest or interests in a partnership, association or other unincorporated entity which owns real property; and the ownership of a beneficial interest or interests in a trust which owns real property."
In her Determination, the ALJ concluded that, pursuant to the Code and the applicable RPTT Rules:

by transferring the shares in the Lower Tier BVI Subs pursuant to the plan set forth in the Contract, notwithstanding the fact that the Closing, as well as many events leading up to the Transfers, took place outside the City, Petitioners have transferred a controlling economic interest in the Four Seasons and are subject [to] the RPTT. [Determination at 32.]

Furthermore, the ALJ stated that although Petitioners raised several arguments regarding the application of the RPTT to this matter, Petitioners did not dispute that the statutory and regulatory language resulted in the imposition of the RPTT to the Transfers. Determination at 32. On appeal, Petitioners, however, contend that under the clear language of the statute, the RPTT does not and cannot apply because the Transfers involved the sale of all of Petitioners' shares in the Lower Tier BVI Subs and the Lower Tier BVI Subs did not own any real property. Thus, Petitioners argue that, by definition, they did not transfer an economic interest in real property and, therefore, the Transfers were not subject to the RPTT.14

Petitioners also contend that to the extent the RPTT Rules provide for the taxation of the Transfers, the rules are not in conformity with the plain meaning of the relevant provisions in the Code. Specifically, the RPTT Rules provide in the relevant part of 19 RCNY §23-02, containing the definition of "Economic interest in real property," that:

14Petitioners do not otherwise dispute the existence of the necessary elements to render the Transfers subject to the RPTT (e.g.; that the Transfers constituted a conveyance of 50% or more of the stock of the Lower Tier BVI Subs).
(2) For transfers occurring prior to April 24, 1995, the ownership of shares of stock in a corporation that owns an economic interest in real property, the ownership of an interest or interests in a partnership, association, or other unincorporated entity which owns an economic interest in real property, and the ownership of a beneficial interest or interests in a trust which owns an economic interest in real property, may also constitute an economic interest in real property. The factors to be weighed in determining whether such ownership constitutes an economic interest in real property include the nature of the activities, assets, and purposes of the above-described entities.

To illustrate:

_Illustration (i):_ X Corporation is a holding company whose sole asset is 100% of the stock of Y Corporation. Y owns real property located in New York City. Since X exists principally for the purpose of holding stock in a subsidiary which owns real property, the ownership of X stock constitutes an economic interest in real property and the sale prior to April 24, 1995, of all the stock of X Corporation is a transfer of a controlling economic interest in real property.

_Illustration (ii):_ X Corporation is primarily engaged in manufacturing outside of New York City. X does not own real property in the City, but does own 100% of the stock of Y Corporation, which owns real property in the City. Since X does not exist principally for the purpose of holding stock in a subsidiary which owns real property, but rather is substantially engaged in other bona fide activities, the ownership of X stock does not constitute an economic interest in real property and the sale prior to April 24, 1995 of all the stock of X Corporation will not constitute a transfer of a controlling economic interest in real property.

(3) For transfers occurring on or after April 24, 1995, the ownership of shares of stock in a corporation that owns an economic interest in real property, the ownership of an
interest or interests in a partnership, association, or other unincorporated entity which owns an economic interest in real property, and the ownership of a beneficial interest or interests in a trust which owns an economic interest in real property, also constitutes an economic interest in real property.

To illustrate:

*Illustration (iii):* X Corporation is engaged in manufacturing outside New York City. X Corporation does not own real property in the City but owns 100% of the stock of Y Corporation, which owns real property located in New York City. The ownership of X Corporation stock constitutes an economic interest in real property and the sale on or after April 24, 1995 of all the stock of X corporation is a transfer of a controlling economic interest in real property. The result would be the same if, instead of owning the property directly, Y Corporation owns 100% of the stock of Z Corporation, which owns the property.

*Illustration (iv):* X Corporation is engaged in manufacturing outside New York City. X Corporation does not own real property in the City but owns 49% of the stock of Y Corporation which owns real property in the City. The ownership of X stock constitutes an economic interest in real property. However, a sale on or after April 24, 1995, of all the stock of X Corporation is not subject to tax as a transfer of a controlling economic interest in real property because there has been no transfer of a controlling interest in Y Corporation.

\ldots

(5) In the case of a transfer of an ownership interest in an entity owning an economic interest in real property, where such ownership interest, itself, constitutes an economic interest in real property under these rules, the percentage of both interests must be considered to determine whether a
controlling economic interest in real property has been transferred.15

The RPTT Rules in effect on the date of the Transfers specifically provided that (except under certain circumstances not relevant to the matter at bar) ownership of an entity which owns an economic interest in real property also constitutes an economic interest in real property. Thus, the RPTT Rules treat as taxable a transfer of a controlling economic interest in real property where the entity owning the real property is more than one tier removed from the entity whose ownership interest is being transferred. In addition, under the RPTT Rules, a transfer is subject to RPTT regardless of whether the entity whose ownership interest is being transferred exists principally for the purpose of holding an ownership interest in an entity which owns real property or is substantially engaged in other bona fide activities.

Petitioners argue that the ALJ erroneously relied on the RPTT Rules and specifically on Illustration (iii) as set forth above. Petitioners assert that where the plain meaning of a statute does not impose a tax upon the Transfers, Respondent cannot do so simply by adopting a rule or regulation that imposes such a tax. Dun & Bradstreet, Inc. v. City of New York, 276 N.Y. 198, 204 (1937).

In order to determine whether a transfer of an economic interest in real property (§11-2101.6 of the Code) can include a multi-tiered transaction; i.e., where there is more than one tier between the entity in which an ownership interest is being transferred and the entity that owns the real property, it is important to review the history of the RPTT.

15We have omitted that portion of the RPTT Rules which provides that, under certain circumstances, transfers occurring after April 24, 1995, of the ownership of an entity which owns an economic interest in real property may not constitute a transfer of an economic interest in real property since those circumstances are not relevant to the matter at bar; e.g.; a grandfathered contract.
The RPTT, when first enacted, only applied to transfers of real property by deed. Therefore, real property could be effectively transferred, without the imposition of the RPTT, by transferring an ownership interest in an entity that owned real property. Eventually the enabling legislation was amended to permit the imposition of RPTT on transfers of controlling economic interests. 16 "This bill closes that loophole by permitting the taxation of transfers of controlling interests in corporations, partnerships, associations, trusts and other entities which own real property. As a result, transactions which effectively, albeit indirectly, convey property will now be taxed." 595 Investors, supra at 444 (citing Governor Carey's approval letter, 1981 McKinney's Session Laws at 2636-2637). The impetus for the amendment to the enabling legislation is generally considered to have been the sale of stock of a corporation that owned what was then called the Pan Am Building. The transfer of 100% of the stock enabled the seller to avoid the RPTT that would have been payable had the building been sold directly. 595 Investors, supra at 444.

For transfers occurring prior to April 24, 1995, the Department treated the ownership of an interest in an entity that owned an economic interest in real property as an economic interest in real property only where the entity in which an ownership interest was being transferred existed principally for the purpose of holding an ownership interest in the entity owning real property and was not substantially engaged in other bona fide activities (the "Prior Rule"). See New York City RPTT Information Bulletin Number 2 (December 16, 1986), and subdivision 2 of the definition of "Economic interest in real property" as contained in the relevant part of the RPTT Rules at 19 RCNY §23-02.

For transfers occurring on or after April 24, 1995, the Department treats (with certain modifications not relevant to the matter at bar) the ownership of an interest in an

16Ch. 915, L. 1981.
entity that owns an economic interest in real property as an economic interest in real property regardless of the nature of the activities, assets and purposes of the entities (the "Current Rule"). See Subdivision 3 of the definition of "Economic interest in real property" as contained in the relevant part of the RPTT Rules at 19 RCNY §23-02. The change in the Department's position is generally related to an amendment to the RPTT in 1994 which provided an exemption from RPTT for transactions that effected a "mere change of identity or form of ownership . . . to the extent the beneficial ownership of such real property or economic interest therein remains the same . . ." (the "Mere Change Exemption"). (Section 11-2106.8 of the Code.)

Because the Prior Rule did not "look through" entities that were substantially engaged in other bona fide activities when determining whether there was an economic interest in real property, there were inconsistencies between the application of the Mere Change Exemption and the Prior Rule. For example, after enactment of the Mere Change Exemption an operating company that owned real property in the City could contribute that property to a wholly-owned subsidiary without incurring the RPTT. However, pursuant to the Prior Rule, a subsequent transfer of the operating company's shares would not be subject to the RPTT because the entity was an operating company with other assets and activities. The Current Rule eliminates the difference in treatment between entities that existed principally for the purpose of holding an interest in an entity that owned real property and those that substantially engaged in other bona fide activities. Thus, under the above example, a subsequent transfer of the operating company's shares would be subject to the RPTT. The need to look through tiers is more compelling with the adoption of the Mere Change Exemption. Since an exemption from RPTT is provided where there is no change in ultimate beneficial ownership for transfers of property to one or more tiers

17Prior to the enactment of the Mere Change Exemption, such a transfer would have been subject to the RPTT.
of entities, it stands to reason that taxability must be determined without regard to the number of tiers of active or inactive entities existing between the real property and the entity in which ownership is transferred.\textsuperscript{18}

Notwithstanding the change embodied in the Current Rule, a review of the facts in the matter before us indicates that none of the corporations had any activities or purpose other than to hold their respective ownership interests in the next lower tier entity including taking all actions necessary to carry out, effectuate and consummate the terms of the Transfers pursuant to the Contract. Therefore, under both the Prior Rule and the Current Rule, the Transfers constitute transfers of controlling economic interests in real property.

The State courts have previously considered the issue of whether a "look through" is permitted (within the definition of the term economic interest in real property) where the transaction in question involved multiple tiers of passive holding companies. In \textsuperscript{595}Investors, \textit{supra}, the tax applied with respect to the syndication of a Delaware limited partnership that owned another Delaware limited partnership that owned real property in the City. In finding that the RPTT applied, the decision states at 446 that:

\begin{quote}
Here the sales of plaintiff's partnership interests were, in essence, the sales of interests in real property situated in New York City, and the economic value of such interests were derived solely from that parcel of realty. The purchasers of limited partnership interests will obtain their profits exclusively from revenues, capital appreciation and tax benefits attributable to that property. This is precisely the sort of transaction the RPTT amendment in question was intended
\end{quote}

\textsuperscript{18}Both the State Real Estate Transfer Tax ("RETT") and the State Gains Tax ("Gains Tax") always had exemptions for mere changes in form and rules that provided for looking through tiers. See, RETT Rules at 20 NYCRR §575.6(b), Example 3; and former Gains Tax Rules at 20 NYCRR §590.52.
to reach, and these transactions would have come within the literal terms of the amendment but for the existence of plaintiff, a passive holding company which is engaged in no independent business activity. Accordingly, the court will disregard the passive shell entity, and permit the city to treat the transfers of partnership interests in plaintiff as if they were transfers of interests in the owning partnership.

In reaching this conclusion the court stated, at page 445, that:

Clearly the statute would apply to a transfer of a controlling interest in a partnership that owned real property. To accept plaintiff's argument would ascribe to the Legislature an intent to permit the creation of shell entities to avoid taxation when the whole purpose of the legislation, as stated by the Governor and the Senate sponsor, is to tax transactions which effectively, but indirectly, convey real property.

The court also (at page 445) affirmed the concept that "[t]ax legislation should be implemented in a manner that gives effect to the economic substance of a transaction" and that the RPTT "would be rendered a nullity if it could be avoided simply by holding the real property through passive corporations or partnerships." [Emphasis added.]

Thus, we find that the RPTT applies to the Transfers at issue. The use of layers of passive, single-purpose entities for purposes of holding the Four Seasons should not take the Transfers outside the scope of the RPTT. In determining whether a transaction is a transfer of a controlling economic interest in an entity that owns real property, the Department must be permitted to look through multi-tier transactions to treat the transfer as a transfer of a controlling economic interest in an entity that owns real property because the transaction "effectively" conveyed the real property.19

19Petitioners also contend that Illustration (iii) of the definition of "Economic interest in real property" as set forth in the RPTT Rules at 19 RCNY §23-02 can be distinguished from the Transfers
Our conclusion finds support in the New York State Tax Appeals Tribunal (the "State Tribunal") decision in Matter of Cafcor Trust Reg. Vaduz, DTA Nos. 812682 and 812683 (New York State Tax Appeals Tribunal, April 17, 1997). In Cafcor, supra, the State Tribunal addressed the constitutional issues raised by Petitioners in the context of the New York State Real Estate Transfer Tax ("RETT") and the now repealed New York State Real Property Gains Tax ("Gains Tax"). The decision dealt with the sale by a Liechtenstein trust, beneficially owned by a foreign individual, of the shares of an alien limited liability company created under the laws of Curacao, Netherlands Antilles. The alien limited liability company owned a controlling interest in a State limited partnership because the illustration does not have the same number of tiers as the Transfers. Petitioners argue that "Z Corporation" in the illustration would only correspond to the Delaware Subs and the Delaware Subs did not own the real property (Four Seasons). As we have found that it is appropriate to look through multi-tiered transactions for purposes of determining if a controlling economic interest has been transferred, the number of tiers between the entity in which an ownership interest is being transferred and the entity owning the real property is not relevant for purposes of determining if the transfer is a transfer of a controlling economic interest in real property. Moreover, we disagree with Petitioners' assertion that the illustration does not correspond to the number of tiers in the Transfers. The illustration refers to an "X Corporation" a "Y Corporation" and a "Z Corporation." In the situation where neither "X Corporation" nor "Y Corporation" own real property but all of the stock of "X Corporation" is sold and "X Corporation" owns 100% of the stock of "Y Corporation" which owns 100% of the stock of "Z Corporation" which owns real property in the City, "X Corporation" corresponds to the Lower Tier BVI Subs; "Y Corporation" corresponds to the Delaware Subs and "Z Corporation" is LLC, the entity that owned Four Seasons. Petitioners do not correspond to "X Corporation" in the illustration as it was not Petitioners' stock that was sold but that of the Lower Tier BVI Subs.

The ALJ limited the applicability of Cafcor, supra, to the matter herein on the basis that the statutory language of the RPTT differed significantly from the language of the now repealed Gains Tax. The Gains Tax imposed the tax on "transfers of real property" and included a transfer of an interest in an entity that owned real property in the definition of a transfer of real property. The RPTT, specifically imposes the tax on transfers of shares without defining those transfers as transfers of real property. While we agree with the ALJ's statement as to the difference between the RPTT and the Gains Tax, we note that the State Tribunal in Cafcor, supra, addressed not only the Gains Tax but also the RETT, which uses different language. The RETT applies to the "conveyance of an interest in real property." Tax Law §1402(a). The Tax Law defines "conveyance" as a transfer of "any interest in real property by any method" including a transfer or acquisition of a controlling interest in any entity with an interest in real property. Thus the RETT treats a transfer of a controlling interest in an entity owning real property as a method for transferring an interest in real property. Similarly, the legislative history, discussed supra, of the application of the RPTT to transfers of controlling economic interests in real property recognizes that such a transfer is a method for transferring real property.

95
that owned a hotel in the City. All the activities of the trust connected with the sale took place outside the State. In denying the taxpayer's claims for refund of the Gains Tax and RETT, the State Tribunal stated that the taxpayer's "focus upon the transfer of stock overlooks the fact that the only taxes in issue are those which arise from the transfer of real estate in New York. No taxes have been imposed on the sale of the shares of stock."

Our conclusion is also supported by the Appellate Division's decision in Matter of Bredero Vast Goed, N.V. v. Tax Commission of the State of New York, 146 A.D.2d 155 (1989), appeal dismissed, 74 N.Y.2d 791 (1989) (a Gains Tax case). Bredero, supra, involved the sale by three Netherlands corporations of all the shares in a State corporation that owned an eighty-five percent interest in a State limited partnership that owned real property. The Gains Tax defined a "transfer of real property" to include the "acquisition of a controlling interest in any entity with an interest in real property." At issue was whether the Gains Tax would apply to a two-tiered transaction where the entity in which a controlling interest was being transferred did not own the property directly. In affirming the State Tax Commission, the Appellate Division looked beyond the two-tiered transaction and determined that the taxpayers "effectively" transferred an interest in the building.

**Due Process and Commerce Clauses**

Petitioners assert that the imposition of the RPTT on the Transfers violates both the Due Process Clause and the Commerce Clause of the United States Constitution. Petitioners contend that they are challenging the constitutionality of the application of the RPTT to the Transfers and not the facial constitutionality of the statute. Petitioners argue

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21 Former Tax Law §1440[7], repealed, L. 1996, Ch. 309, section 171.
that a facial challenge is limited to situations where the statute could never be applied in a valid manner, which they do not contend.

This Tribunal has previously held that while it cannot determine whether a statute is unconstitutional on its face; i.e., as written, it can determine whether a statute has been unconstitutionally applied to a particular set of facts. Siemens Corporation f/k/a Siemens Capital Corporation, TAT(E) 93-237 (GC), New York City Tax Appeals Tribunal (1999). In Moran Towing Corporation v. Urbach, 99 N.Y.2d 443, 448 (2003), the State Court of Appeals stated that "[a] party mounting a facial constitutional challenge bears the substantial burden of demonstrating 'that in any degree and in every conceivable application,' the law suffers wholesale constitutional impairment.' (Cohen v. State of New York, 94 N.Y.2d 1, 8 (1999)" Thus, we agree with Petitioners' assertions that their contention is that the statute has been unconstitutionally applied and, thus, such contention can be reviewed by this Tribunal.

Petitioners contend that Respondent seeks to impose a tax on the transfer of stock of non-domiciliary corporations by attributing corporate property to shareholders. Petitioners refer to two cases as support for their argument that the application of the RPTT to Petitioners is unconstitutional because corporate property may not be attributed to shareholders to establish nexus to tax.\textsuperscript{22} Petitioners rely on Rhode Island Hospital Trust Co. v. Doughton, 270 U.S. 69 (1926). That case involved the imposition of an inheritance tax by North Carolina upon the estate of a nonresident on the transfer of shares of stock of the R.J. Reynolds Tobacco Company, a New Jersey corporation that did

\textsuperscript{22}In 2003, the State Legislature on a prospective basis amended the RPTT to redefine "grantor" to include "the entity with an interest in real property or the person or persons who transfer an economic interest in real property." L. 2003, Ch. 63, Part C, section 3. Thus, the ALJ noted that, in the future, there will be a statutory basis for assessing the RPTT against an entity over which the City clearly has jurisdiction where the transferor itself has no contact with the City.
business, and had two thirds of the value of its property, in North Carolina. In invalidating the North Carolina statute, the Supreme Court held that the owner of stock in a corporation is not the owner of the corporation's property and that jurisdiction for tax purposes over the stockholder cannot be based on the situs of part of the corporation's property within the taxing state. Petitioner also relies on *In re Gates' Estate*, 243 N.Y. 193 (1926), which involved the taxation of the transfer of stocks and bonds owned by a nonresident decedent where the corporations whose stocks and bonds were at issue owned real property in the State. Relying on the concept that the owner of the shares of stock in a corporation is not the owner of the corporation's property as set forth in *Rhode Island Hospital Trust*, *supra*, the Court of Appeals struck down this provision of the tax statute.

The State Tribunal in *Cafcor*, *supra* distinguished the two cases stating:

Unlike *Rhode Island Hospital* or *Gates' Estate*, New York is not seeking to impose tax on the transfer of stock. Rather, New York is imposing a tax on the consideration or gain arising from the transfer of real property in New York.

We do not believe that *Rhode Island Hospital*, *supra*, and *Gates' Estate*, *supra*, preclude us from finding the RPTT applicable to multi-tiered transactions such as the case at bar. Both cases involved taxes imposed on the transfer or ownership at death of, among other assets, securities owned by nonresidents of the state to the extent that the securities were issued by entities that owned real property, or as was the case in *Gates' Estate*, *supra*, any property, located in the state. Neither tax was limited to securities representing a controlling equity interest in the entity in question. Moreover, the taxes involved in those cases applies to transfers at death, not intentional negotiated transfers, as were the Transfers involved here. Finally, those cases, decided as they were in 1926,
do not reflect the evolution of economic realities evidenced by the extensive use today of corporate, unincorporated or hybrid business entities.


[t]he Due Process Clause 'requires some definite link, some minimum connection, between a state and the person, property or transaction its seeks to tax', [citation omitted] and that the 'income attributed to the State for tax purposes must be rationally related to "values connected with the taxing State."' [citation omitted]

... if a foreign corporation purposefully avails itself of the benefits of an economic market in the forum State, it may subject itself to the State's *in personam* jurisdiction even if it has no physical presence in the State.

The City had "some minimum connection" with the transaction it sought to tax because for all practical purposes, the Contract was a contract to sell the Four Seasons, which was located in the City. The amount subject to tax was rationally related to values connected to the City as the RPTT is based on the consideration for the conveyance attributable to the real property. The increase in value from 1996, when LLC purchased the Four Seasons for $195 million, to 1999, when the shares of the Lower Tier BVI Subs were sold for $275 million, is due to the increase in value of the Four Seasons, which is located in the City and benefitted from the City's infrastructure and tourism market.

The State Tribunal also found that the Due Process Clause standards as set forth in *Quill*, *supra* were met in *Cafcor*, *supra*, as it was clear that New York had "some
minimum connection” with the transaction it sought to tax and the income attributed to New York was rationally related to values connected to New York.\textsuperscript{23}

The Court in Quill, supra, distinguished the nexus requirements under the Due Process Clause from the substantial nexus requirements of the Commerce Clause. The four-part test set forth in Complete Auto Transit v. Brady, 430 U.S. 274, 279 (1977), \textit{rehearing denied}, 430 U.S. 976 (1977) governs the validity of state taxes under the Commerce Clause and provides that a tax will be sustained against a Commerce Clause challenge if the tax:

[1] is applied to an activity with a substantial nexus with the taxing State, [2] is fairly apportioned, [3] does not discriminate against interstate commerce, and [4] is fairly related to the services provided by the State.

We find, as did the ALJ, that Petitioners had substantial nexus with the City through the activities of their officers and agents in the City. A corporation can have substantial nexus through the activities of an agent. \textit{See}, Tyler Pipe Industries, Inc. \textit{v. Washington State Department of Revenue}, 483 U.S. 232 (1987). Petitioners, through their agents, engaged in significant marketing activities in the City. Morgan Stanley acted not only for LLC but also for all the other entities in the corporate structure up to and including Petitioners. LLC and its direct and indirect shareholders, including Petitioners, acted in concert with respect to the activities of Morgan Stanley concerning the sale of the shares of the Lower Tier BVI Subs and the Four Seasons. Petitioners engaged Polylinks to help with the sale by Petitioners of the Lower Tier BVI Subs and Polylinks was directly compensated by Petitioners for these efforts. Because Polylinks was located in Hong

\textsuperscript{23}\textit{See}, footnote 24, \textit{infra}.
Kong, it hired PKF, which had a New York office and personnel to deal with certain tasks associated with marketing the Four Seasons. The Closing Statement and the Contract identify PKF as Petitioners' agent. The Contract makes it clear that all the entities in the corporate structure were collectively considered the "Seller." Petitioners' complete control of the operations and activities of all the entities below them in the corporate structure allowed them to obligate LLC to complete the activities necessary to effectuate the Transfers.

Therefore, we find, as did the ALJ, that

Based on a combination of the activities of their officers, the activities of their agents Morgan Stanley and PKF, and the activities of LLC (their indirect subsidiary acting on behalf of Petitioners to help effectuate the Transfers), Petitioners had the minimum contacts needed for Due Process and the substantial nexus with the City required by the Commerce Clause.24 [Determination at 46.]

595 Investors, supra at 447, holds that the RPTT does not violate either the Commerce Clause or Due Process Clause of the United States Constitution. In applying the tests set forth in Complete Auto Transit, supra, the court found that:

24 Having found that Petitioners' corporate officers and agents engaged in sufficient activities in the City to create substantial nexus we do not need to address the issue of what the result would be if there were no such activities in the City nor are we subscribing to any requirement for physical presence in a RPTT matter. See Cafcor, supra, where the State Tribunal found that Commerce Clause substantial nexus was met due to the location of the real property and that it was unnecessary to establish Cafcor's physical presence in the State. Nevertheless, we note that in contexts where physical presence is a requirement for substantial nexus, physical presence "need not be substantial. Rather, it must be demonstrably more than a 'slightest presence.'" Orvis Company, Inc. v. Tax Appeals Tribunal of the State of New York, 86 N.Y.2d 165, 178 (1995). In the case at bar, this standard was met as the activities of Petitioners and their agents were more than de minimis and were all related specifically to the transaction sought to be taxed.
The transaction here is the syndication of New York City real estate. Without question New York City is the predominant place where each buyer of a partnership share in plaintiff 'in every practical sense invokes and enjoys the protection of the laws, and in consequence realizes the economic advantages of his ownership.' [citation omitted]

Nor can it be said that the RPTT burdens interstate commerce. On the contrary, the tax is fairly related to the services provided by New York City. The RPTT amendment was intended to tax direct and indirect transfers of New York City real estate on an equal basis, the measure of such tax being the consideration paid. 25

With respect to the issue of international commerce, the Appellate Division in Bredero, supra, held that they were not "persuaded by [taxpayers'] additional suggestion that the enactment of Internal Revenue Code § 897 (26 USC § 897), as part of the Foreign Investment in Real Property Tax Act of 1980, precludes the application of the [State Gains Tax] to the instant conveyance." The Appellate Division concluded that the act did not preempt the State's taxing authority. Similarly, we conclude that Foreign Investment in Real Property Tax Act did not preempt the City's authority to impose the RPTT.

25 While there is no question that the City may impose taxes on partners based on the activities or property of the partnership of which they are members, see, e.g., Varrington Corp. v. City of New York Department of Finance, 85 N.Y.2d 28 (1995), the matter at bar involves an LLC and 3 tiers of corporate entities. Nevertheless, we view the court's reasoning in 595 Investors, supra, as applicable to the case at bar.
Therefore, the imposition of the RPTT on the Transfers does not violate the Due Process Clause or the Commerce Clause of the United States Constitution.26

Thus, for the reasons stated above we, as did the ALJ, deny Petitioners' refund claims with respect to the Transfers and sustain the Notices of Disallowance dated August 1, 2000.

Dated: June 2, 2006
New York, New York

__________________________________________
GLENN NEWMAN
President and Commissioner

__________________________________________
ELLEN E. HOFFMAN
Commissioner

26We have considered all other arguments raised by the parties and find them unpersuasive.
EXHIBIT D
In the Matter of the Petition of NS 1999 AMERICAN COMPANY NOMINEE FOR THE NS 1991 AMERICAN TRUST for Revision of Determinations or for Refunds of Real Property Transfer Tax under Article 31 of the Tax Law and of Tax on Gains Derived from Certain Real Property Transfers under Article 31-B of the Tax Law

DTA NO. 815191

STATE OF NEW YORK-DIVISION OF TAX APPEALS

1998 N.Y. Tax LEXIS 69

February 19, 1998

PANEL:

OPINIONBY:
CORIGLIANO

OPINION:
DETERMINATION

Petitioner, NS 1999 American Company, nominee for the NS 1991 American Trust, c/o Schneider, Schecter & Yoss, 1979 Marcus Avenue #232, Lake Success, New York 11042, filed a petition for revision of determinations or for refunds of real property transfer tax under Article 31 of the Tax Law and of tax on gains derived from certain real property transfers under Article 31-B of the Tax Law. n1

n1 Article 31-B of the Tax Law was repealed on July 13, 1996. The repeal applies to transfers of real property that occur on or after June 15, 1996 (L 1996, ch 309, §§ 171-180). Citations in this determination are to the law in effect at the time of the transfer in issue.

A hearing was held before Jean Corigliano, Administrative Law Judge, at the offices of the Division of Tax Appeals, 641 Lexington Avenue, New York, New York, on May 15, 1997 with all briefs to be submitted by September 9, 1997 which date began the six-month period for issuance of this determination. Petitioner appeared by Diana A. Steele, Esq. The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (Herbert, M. Friedman, Jr., Esq., of counsel). [*2]

ISSUE

Whether, after the transfer of the Empire State Building by petitioner to a partnership, petitioner had a 50 percent interest in the partnership or a 99.745 percent interest in the partnership.

FINDINGS OF FACT

2. Petitioner and the Division of Taxation, by their respective representatives, executed a Stipulation of Facts, dated May 15, 1997. The stipulated facts relevant to resolution of the issues raised by the parties have been incorporated into these findings of fact.

3. In 1993, petitioner acquired ownership of certain real property located at 350 Fifth Avenue, New York, New York, best known as the Empire State Building (the "Property" or "the Empire State Building"). At the time petitioner acquired ownership, the Empire State Building was subject to a long-term lease (the "ESB Lease") which provides for a fixed amount of rent (the "ESB Rent") by the tenant. At that time (and for many years prior), the tenant, or lessee, of the Empire State Building was Harry B. [*3] Helmsley or entities controlled by Helmsley. The term of the lease, if renewed pursuant to the lessee's options, will continue until January 5, 2076.

4. On June 28, 1994, petitioner contributed ownership of the Empire State Building to Trump Empire State Partners (the "Partnership"). The partners of the Partnership are petitioner and Trump Empire State, Inc. ("Trumpco"), whose president is the well-known real estate developer, Donald J. Trump. Both before and after the transfer, the name of the Property was "the Empire State Building", and the name has not changed.

5. On April 13, 1994, petitioner filed a real property gains tax transferor questionnaire with the Division of Taxation ("Division") in connection with the transfer of the Empire State Building to the Partnership. Transfers of real property which are made to effectuate a mere change of identity or form of ownership are generally exempt from the real property transfer tax and the real property gains tax. In its filings, petitioner claimed entitlement to the mere change exemption. At that time, petitioner claimed that Trumpco was obtaining approximately a .111 percent interest in the Property based on Trumpco's expected [*4] $50,000.00 capital contribution to the Partnership. Based partially on that claim, petitioner calculated gains tax due on the transfer of $318.40. A draft copy of the Joint Venture Agreement creating the Partnership was submitted to the Division along with other documents.

6. Upon review of the documents submitted by petitioner in connection with its gains tax filings, the Division concluded that petitioner received a 50 percent interest in the Partnership rather than the 99.889 percent interest claimed by petitioner in its Transferor Questionnaire. In an affidavit, James Sottile, a Tax Technician in the Division's Gains Tax Audit Unit, explained the basis for the Division's determination. The Division relied primarily on its analysis of the Joint Venture Agreement. Section 2.5 of that agreement provides as follows:

"Section 2.5 Percentage Interests."

Subject to the other terms and conditions of this Agreement, including, without limitation, the provisions of Article III and IV, each of NS American and Trumpco shall have a fifty (50%) percent interest in the Venture" (emphasis added).
The Division determined that the language of section 2.5 is in conflict [*5] with petitioner's claim that it retained a 99.889 percent interest in the Partnership.

7. In addition, the Division disputed petitioner's claim that Trumpco's contributions to the Partnership were confined to its contribution to capital. One of the primary purposes of the Partnership was the renegotiation of the ESB Lease to increase the profits flowing from the Partnership's ownership of the Empire State Building. Thus, Section 1.3 of the Joint Venture Agreement includes among the purposes of the Partnership: enforcing the tenant's obligations under the ESB Lease; acquiring the tenant's interest in the ESB Lease; and upgrading and developing the ESB Property. The Division noted that in the introductory paragraphs of the Joint Venture Agreement Trumpco agreed to contribute: "the funds and real estate development expertise necessary to formulate and assess alternatives for the enforcement of the tenant's obligations under the ESB lease, the acquisition of the tenant's interest in the ESB lease, the upgrading and redevelopment of the ESB Property and the possible acquisition and development of the Related Property" (Joint Venture Agreement, p. 3).

Based on these provisions [*6] of the Joint Venture Agreement, the Division concluded that Trumpco made significant contributions to the Partnership in excess of its cash contribution.

8. The Division noted various other provisions of the Joint Venture Agreement which it identified as contradicting petitioner's claim that Trumpco received only a .111 percent beneficial interest in the Property. The significant provisions identified by the Division are as follows:

(a) Section 3.1 which sets forth definitions of income and losses states, among other things: "Trumpco shall make all accounting decisions and elections permitted to be made by the Venture for federal income tax purposes." n2

n2 The preceding sentence states: "Subject to the approval of NS American, such approval not to be unreasonably withheld or delayed, Trumpco shall determine the accounting methods to be followed by the Venture for federal income tax purposes."

(b) In Article III of the agreement, specific allocations of income, losses and credits were agreed to by both parties.

(c) In the event of sale of Partnership property, income and gain is allocated first to petitioner up to the amount of $ 45 million, but income and gain exceeding $ [*7] 45 million is divided equally between petitioner and Trumpco. The remaining provisions of section 3.2 were summarized by Mr. Sottile as follows: "Additionally, remaining rental income, income from taxable dispositions, depreciation and/or amortization deductions, losses from taxable dispositions, and credits shall be allocated fifty (50%) to NS American and fifty (50%) to Trumpco." (Sottile Affidavit, P 12.)
(d) The management and control of the day-to-day business and affairs of the Partnership is vested in Trumpco by section 5.1 of the agreement.

(e) Section 5.1 gives Trumpco absolute authority to deal with all television, radio, newspaper and other media sources in connection with the affairs of the Partnership. Petitioner is prohibited from acting on behalf of the Partnership in connection with any matter without prior written consent of Trumpco. n3

n3 Section 5.2(b) of the Joint Venture Agreement states that Trumpco shall not take any "Major Acts" without the prior written consent of petitioner. "Major Acts" include: sale of the Property, entering into any contract with an affiliate or subsidiary of Trumpco, modifying or amending the ESB lease, approving the terms of a buy-out or termination of the ESB lease, refinancing of the initial borrowing, the incurring of additional indebtedness in excess of $200,000.00 or of any indebtedness secured by the ESB lease or the Property, the acquisition of related properties, the redevelopment of the related property, the redevelopment of the ESB Property, and the selection of architects, contractors, accountants or attorneys. [*8]

(f) Section 6.1 of the agreement states that the books of account of the Partnership shall be kept by Trumpco, and section 6.3 of the agreement states that Trumpco shall be responsible for the maintenance of bank accounts in which income received by the Partnership shall be deposited.

(g) Petitioner has the right, under section 11.5 of the agreement to disclose that petitioner "is a partner of Trump and may use the Trump name in connection with the use of the [Partnership's] name."

9. As support for its determination, the Division also relied on "numerous newspaper and magazine articles [which] have quoted Donald Trump claiming he has a fifty (50%) interest in the joint venture" (Sottile Affidavit, P 13).

10. On August 8, 1994, the Division issued two notices of determination to petitioner. One notice asserted gains tax due of $143,404.80 plus interest. The other asserted real estate transfer tax due of $90,000.00 plus interest. The basis for the assessments of tax was the Division's determination that petitioner transferred a 50 percent interest in the Partnership to Trumpco as stated in section 2.5 of the Joint Venture Agreement. The Division's actual calculations were based [*9] upon the information provided in the gains tax questionnaires.

11. Following a Conciliation Conference in the Bureau of Conciliation and Mediation Services, the Division issued a Conciliation Order, dated April 19, 1996, sustaining the notices of determination.

12. Regarding the transfer, the parties have stipulated to the following facts:

(a) The transfer of the Property to the Partnership and the execution of the Joint Venture Agreement actually occurred on June 28, 1994;

(b) the contribution of the property to the Partnership is a "mere change" transaction under sections 1405(bCo)(6) and 1443(b)(5) of the Tax Law;
(c) the real property was not subject to any mortgage debt;

(d) for purposes of both the transfer tax and the gains tax, the consideration given was $45 million;

(e) the original purchase price of the real property was $42,131,904.00;

(f) Trumpco contributed $115,000.00 to the Partnership as its initial capital contribution under section 2.2(a) of the joint venture agreement;

(g) immediately after the transfer of the real property, the Partnership borrowed $11,700,000.00 using the real property as collateral.

13. Of the $11,700,000.00 initial borrowing, [*10] $76,537.50 was deposited into an interest reserve account, $797,216.00 was used to pay closing costs and $10,826,246.50 was distributed to petitioner.

14. In this proceeding, petitioner asserts that there was no transfer of petitioner's beneficial interest in the Empire State Building as result of the transfer of the Property to the Partnership, and that it had a 99.745 percent interest in the Partnership immediately after the transfer.

15. Petitioner, like the Division, relies on the Joint Venture Agreement as evidence of the correctness of its position. Section 2.5 of the Joint Venture Agreement states that petitioner and Trumpco each have a 50 percent interest in the Partnership, subject, however, to other terms and conditions of the agreement, including the provisions of Articles III and IV. Petitioner claims that when these other terms and conditions are examined it becomes apparent that it did not transfer a 50 percent beneficial interest in the Empire State Building to Trumpco.

16. Article III of the agreement provides for the allocation of ordinary income between the partners. Rental income from the ESB lease is allocated first to petitioner, up to the full amount of [*11] the ESB rent. Trumpco is entitled to rental income only if the ESB rent increases because of a renegotiation of the lease or if the Partnership acquires additional income-producing property. Income and gain from disposition of Partnership property are allocated under section 3.2(b) of Article III. Under this provision, income or gain from the sale of Partnership property is allocated 100 percent to petitioner until petitioner's capital account balance equals its Unreturned Capital Contribution. For purposes of the agreement, petitioner's Unreturned Capital Contribution consists of $45,000,000.00 less the amount of the initial borrowing distributed to petitioner ($10,826,246.50) and the amount of prior distributions of the proceeds of sales or exchanges of the Partnership under section 4.4(e) of the Joint Venture Agreement.

17. Article IV of the Joint Venture Agreement sets forth the partners' agreement regarding distributions to the partners. Pursuant to section 4.3, the proceeds from refinancing or from the sale or disposition of Partnership property are to be distributed, after payment of any Partnership debts and the establishment of reserves, 100 percent to petitioner until [*12] it has received the aggregate amount of the ESB Rent plus its Unreturned Capital Contribution. Additional proceeds are distributed to Trumpco until it receives its Unreturned Capital Contribution (defined as Trumpco's aggregate capital contributions less aggregate distributions to
Trumpco). After these distributions are made, any additional proceeds are to be distributed in equal amounts to petitioner and Trumpco.

18. Article VIII of the Joint Venture Agreement contains the partners’ agreement with respect to distributions upon liquidation of the Partnership. Upon dissolution, the capital accounts of the partners are to be adjusted in accordance with the allocation provisions of Article III, section 3.2. Any partner with a deficit capital account is required to contribute cash to the Partnership in the amount of the deficit. After payment of the debts and obligations of the Partnership and the establishment of reserves, the liquidation proceeds are to be distributed to petitioner and Trumpco in accordance with their capital accounts.

19. Petitioner's only witness was Joel Kravitz, an accountant with the firm of Schneider, Schechter & Voss, P.C.. Mr. Kravitz has prepared the tax returns [*13] of the Partnership from its inception to the present. He testified that in each year in which the Partnership has filed Federal income tax returns, 1994, 1995 and 1996, allocations of income and expenses have been made in accordance with the terms of the Joint Venture Agreement. One hundred percent of the ESB Rent has been allocated to petitioner; 100 percent of the depreciation on the Empire State Building has been allocated to petitioner; 100 percent of capital expenditures incurred in connection with the Property prior to its contribution to the Partnership has been allocated to Petitioner; and 100 percent of the available cash of the Partnership, namely the ESB Rent, has been distributed to petitioner.

20. The Partnership received interest income associated with the $ 11,800,000.00 loan taken immediately after the real property transfer. A cash account was established to receive the loan proceeds, and the monies were then distributed to the two partners with Trumpco receiving $ 400,000.00 or approximately 3.3 percent of the total. The interest income and interest expense on the loan proceeds were distributed 97 percent to petitioner and 3 percent to Trumpco reflecting the percentage [*14] of the loan proceeds received by each partner.

21. In July 1994, Mr. Trump announced his purchase of an interest in the Empire State Building. An Associated Press article, reprinted in the July 7, 1994 edition of the Troy Record, states that Mr. Trump, through his publicist, released a statement claiming that he "arranged equity financing for NS America in return for 50 percent ownership" in the Empire State Building. In Emperors of the Air, an article published in the May 1995 issue of Vanity Fair magazine, Bryan Burrough describes the purchase of the Empire State Building by Hideki Yokoi, a Japanese businessman with reputed ties to organized crime figures in Japan; transfer of control of the Empire State Building to one of Yokoi's daughters; and the ensuing lawsuit brought by Yokoi who claims that his daughter stole the Empire State Building from him. Regarding Mr. Trump's ownership interests in the Partnership, the article reports that both Yokoi and the Helmsleys say that "Trump almost certainly doesn't own half the [Empire State] building, but rather, "owns an interest in the financial 'upside' he can create by ousting the Helmsleys from their lease" (id., at 165). In [*15] response, to this claim, Mr. Trump is reported to have said: "I'd rather not comment on that . . . . But the ultimate answer is that I own 50 percent of the building. It's a complicated formula. A case could be made I actually own 50 percent. It's just a very complicated formula" (id.).

22. At the time of the hearing, the ESB lease was still in effect under the terms existing at the time the Partnership was formed. The ESB rent is $ 1,970,000.00 per
year, representing less than a 5 percent return on the $45 million valuation of the Property.

CONCLUSIONS OF LAW

A. Tax Law § 1402 imposes tax on conveyances of real property or interests in real property when the consideration exceeds $500.00. Former Article 31-B of the Tax Law imposes a tax on gains derived from the transfer of real property (Tax Law § 1441). Under both statutes, the transfer or acquisition of a controlling interest in an entity with an interest in real property is a taxable transaction (Tax Law § 1401[e]; § 1440[7]). Certain transactions are exempt from the transfer tax and the gains tax, including transfers which consist of "a mere change of identity or form of ownership or organization where there [*16] is no change in beneficial interest" (Tax Law § 1405[b][6]; see also, Tax Law § 1443[b][5]). The Division's regulations provide that the transfer of real property by a person to a partnership in exchange for an interest in the partnership is a mere change of identity or form of ownership, and in such circumstances the conveyance or transfer is not taxable to the extent of the transferor's interest in the partnership (20 NYCRR 575.10[d]; 590.51[a][1]). The parties agree that petitioner's transfer of the Empire State Building to the Partnership is a mere change transaction. They differ over the extent of petitioner's interest in the Partnership after the transfer.

B. Petitioner claims that its transfer of the Empire State Building to the Partnership is exempt from the gains tax and the transfer tax at least to the extent of petitioner's 99.745 percent interest in partnership capital immediately after the transfer. It premises this claim on its interpretation of what constitutes an "interest in the partnership" pursuant to sections 575.10 and 590.50 of the Division's regulations. Since neither the Tax Law nor the regulations provide a definition of what constitutes an "interest [*17] in a partnership" for purposes of the mere change exemptions, petitioner turns to three other sources to support its argument: provisions of articles 31 and 31-B of the Tax Law not concerned with the mere change exemption; a decision of the Tax Appeals Tribunal, Matter of Tomback (Tax Appeals Tribunal, September 1, 1994); and a Private Letter Ruling (No. 307) issued by the Division to an unrelated taxpayer. It is petitioner's position that these three sources show that an interest in a partnership is consistently defined in terms of the partner's interest in the property, profits and losses of the partnership.

For purposes of both the gains tax and transfer tax, a partnership "controlling interest" is defined as "fifty percent or more of the capital, profits or beneficial interest in such partnership" (Tax Law § 1440[2]; § 1401[b]). Petitioner argues that a partner's interest in the capital, profits or beneficial interest in a partnership is reflected in its entitlement to the income, gain or loss of the partnership. Thus, to determine a partner's interest in the partnership, petitioner would turn to the allocations of income and gain as set forth in the partnership agreement. [*18] In this case, those allocations are contained in Articles III and IV of the Joint Venture Agreement, and those provisions establish that Partnership property, profits and losses are allocated to the partners in proportion to each partner's capital contribution.

Petitioner notes that in Matter of Tomback (supra) the Tax Appeals Tribunal, in deciding an issue unrelated to the instant matter, described the interest in the partnership held by the petitioner as a 10 percent interest "in the partnership's property, profits and losses". This, according to petitioner, supports its position that
in determining a partner's "interest in a partnership", the partnership's allocations of gain, income, loss and deduction to each partner must be taken into account. Petitioner also points to Private Letter Ruling 307 (March 16, 1987) where the Division found that an "interest in a partnership" should be determined by reference to each partner's capital interests in the Partnership.

The Division takes the position that section 2.5 of the Joint Venture Agreement establishes that the partners each have a 50 percent interest in the Partnership. According to the Division, that section's statement [*19] that each partner "shall have a fifty (50%) interest in the Venture" is determinative of the issue. The Division argues that the newspaper and magazine articles discussed above bolster its position inasmuch as they each report Mr. Trump's assertion that he has a 50 percent interest in the **Empire State Building.**

The Division dismisses the significance of allocations of income, gain and loss as set forth in Articles III and IV of the Joint Venture Agreement, arguing that the reference to these articles in section 2.5 "are nothing more than terms relating to the disposition of proceeds and liabilities and do not alter the underlying ownership interests" (Division's brief, p. 5). The vast disparity in the initial capital contributions of the partners is dismissed by the Division as not determinative of each partner's ownership interest in the Partnership, inasmuch as the partners explicitly stated that each would have a 50 percent interest in the Partnership. The Division also argues that Trumpco's contribution was not limited to the initial $ 115,000.00 cash contribution since Trumpco agreed to contribute the funds and financial expertise necessary to enforce the tenant's obligations [*20] under the ESB lease, to acquire the ESB lease, and to upgrade and redevelop the **Empire State Building.**

The Division asserts that Matter of Tomback (supra) offers no support for petitioner's position because it does not address the legal issue presented in this case. Moreover, the Division finds that the Tribunal's references to "property", "profits" and "losses" supports its position that these are three separate items which may be allocated as the partners choose without affecting their underlying interest in the partnership itself. According to the Division, the partners in Tomback identically allocated partnership property, profits and losses by agreement, while petitioner and Trumpco divided their partnership interest in an equal manner and divided their profits and losses by a different method. The Division did not address the Private Letter Ruling cited by petitioner. I note that Private Letter Rulings have no precedential value and are not binding on the Division in cases with other taxpayers.

C. Where the petitioner claims entitlement to a statutory exemption, it bears the burden of proof and must demonstrate that its is the only reasonable interpretation of the [*21] statutes and that the statutes provide petitioner with the exemption it seeks (Matter of Howes v. Tax Appeals Tribunal, 159 AD2d 813, 552 NYS2d 972, 973).

D. The Joint Venture Agreement evidences the creation of the Partnership and the allocation of each partner's interest in the Partnership. Each party argues that the plain language of section 2.5 of the agreement supports its position. Since the parties differ over the interpretation of section 2.5, the first question which must be addressed is the meaning of that section.

The Joint Venture Agreement is an independent contract subject to the principles of contract interpretation. "The cardinal rule of contract interpretation is that, where the
language of the contract is clear and unambiguous, the parties' intent is to be gleaned from the language of the agreement and whatever may be reasonably implied therefrom" (H.R.S. Hunt Club v. Town of Claverack, 222 AD2d 769, 634 NYS2d 816, lv denied 89 NY2d 804, 653 NYS2d 543; see also, W.W. Assocs. V. Giancontieri, 77 NY2d 157, 565 NYS2d 440; Weisberger v. Goldstein, AD2d , 662 NYS2d 544). In carrying out this task, the words and phrases used by the [*22] parties must . . . be given their plain meaning1 (Brooke Group Ltd. V. JCH Syndicate 488, 87 NY2d 530, 640 NYS2d 479).

Section 2.5 read as a whole, and in the context of the entire agreement, plainly manifests the intention of the parties to subject each party's 50 percent interest in the Partnership to other terms and conditions, including those set out in Articles III and IV of the Joint Venture Agreement. I cannot agree with the Division that the reference to other terms and conditions, specifically including those in Articles III and IV, is irrelevant to the allocation of Partnership interests. The drafters of the contract could not have been more precise or clear in stating that the equal division of the Partnership is subject to the allocations of income, profit and gain found in Articles III and IV, as well as to other terms and conditions of the Joint Venture Agreement.

The next question then is to determine petitioner's interest in the Partnership based upon the various terms and conditions of the Joint Venture Agreement. The Division's position is that petitioner transferred the Empire State Building, valued at $45 million, to the Partnership in return for a 50% [*23] interest in the Partnership, in essence transferring a 50% beneficial interest in the Empire State Building to Trumpco. Petitioner argues that by subjecting each party's 50 percent interest in the Partnership to other terms and agreements of the Joint Venture Agreement, the parties manifested their intention to allocate partnership interests in accordance with each party's capital contribution and to divide property, profits and losses from the Partnership on an equal basis only when, and if, the value of the property or the level of profit from the ESB lease rise above that which existed at the time of the real property transfer. Petitioner's interpretation of the Joint Venture Agreement is the only one consistent with the plain language of the agreement, the economic reality of the transaction and the theory of the gains tax.

E. There are no Tax Appeals Tribunal decisions or court cases which address the specific issue raised here: how to determine each party's interest in a partnership after the transfer of real property to the partnership. There are, however, cases concerned with whether a taxpayer has shown entitlement to the mere change exemption in the first instance, and [*24] these cases provide helpful guidance. Before examining these cases, it is important to return to the exemption statutes themselves. They each provide an exemption from tax where the transfer involves "a mere change of identity or form of ownership or organization where there is no change in beneficial interest" (Tax Law § 1405[b][6]; emphasis added; see also, Tax Law § 1443[5]). The exemption statutes direct attention first to whether there has been a change in the beneficial ownership of the real property and second to the extent of the change in beneficial ownership. In Matter of 307 McKibbon St. Realty Corp. (Tax Appeals Tribunal, October 14, 1988), the Tax Appeals Tribunal stated that the structure of the gains tax is to "look through entity ownership of real property to determine the beneficial ownership of the property." The Tribunal went on to state that the focus "through entities" to determine beneficial ownership is required by both statutes imposing the tax and the statutes providing exemptions from tax.
In *Matter of Schrier* (Tax Appeals Tribunal, July 16, 1992), the Tribunal examined the examples of mere change transactions which are set forth in the Division's [*25] regulations (see, 20 NYCRR 590.50(a)[2] - [5]) and found evidence there of the underlying theme of the gains tax: the focus through entities to determine the beneficial ownership of the real property. The Tribunal notes that in each example various changes in business form are considered, with the same result in each case: "provided the owners of the property retain the same proportion of beneficial ownership . . . the change is deemed a mere change." As the Tribunal points out, the only concern of the examples is "whether the proportion of beneficial interest in the property is preserved." From this, the Tribunal concluded that "the primary concern of the examples is whether the economic interests in the real property have been changed" (*id.*). Thus, the gains tax places the focus on the economic reality of the transaction, reversing the general rule that form takes precedence over substance in the analysis of tax cases (*Matter of Schecter*, Tax Appeals Tribunal, October 13, 1994, *see also*, *Matter of Bredero Vast Goed, N.V. v. Tax Commun.*, 146 AD2d 155, 539 NYS2d 823, *appeal dismissed* 74 NY2d 791, 545 NYS2d 105 [where the court recognizes and upholds economic reality [*26* as the key principle underlying the interpretation of the imposition section of the gains tax]; *Matter of Von-Mar Realty Co.*, Tax Appeals Tribunal, December 19, 1991, *confirmed Matter of Von-Mar Realty v. Tax Appeals Tribunal*, 191 AD2d 753, 594 NYS2d 414, *iv denied* 82 NY2d 655, 602 NYS2d 803).

While the "look through" principle has primarily been employed to determine whether there is a change in beneficial interest, it must also apply to determine the extent of the change. Therefore, it is appropriate to look at the economic reality of the transaction between petitioner and Trumpco as reflected in the Joint Venture Agreement to determine the extent of petitioner's interest in the Partnership. This analysis plainly establishes that petitioner had at least a 99.745 percent interest in the Partnership after the transfer.

F. Petitioner asserts that it retained a 100 percent beneficial interest in the **Empire State Building** after the transfer to the Partnership. Its position is supported by the terms of the Joint Venture Agreement. Under Article III, section 3.2(a)(1) of the Joint Venture Agreement, 100 percent of the ordinary income of the Partnership up to the amount of [*27*] the ESB Rent is allocated to petitioner. Under Article IV, section 4.2 of the agreement, cash is to be distributed to petitioner until it has received an amount equal to the aggregate amount of the ESB Rent. Immediately after the transfer, petitioner was entitled to allocations of 100 percent of the depreciation attributable to the Property and to the capital expenditures incurred in connection with the Property prior to its contribution to the Partnership.

Petitioner offers the following hypothetical to demonstrate that petitioner retained its interest in the Property after the transfer. The agreed upon value of the Property at the time of transfer was $ 45 million. Trumpco contributed $ 115,000.00 to the Partnership at that time, yielding total Partnership capital of $ 45,115,000.00. If the Property were then sold for its agreed upon value of $ 45 million immediately after the transfer, the Partnership would receive $ 45 million as consideration. The Partnership would then have $ 45,115,000.00. Under section 8.3 of the Joint Venture Agreement, the $ 45,115,000.00 would be distributed to petitioner and Trumpco in accordance with their capital accounts. Petitioner would receive $ [*28*] 45 million and Trumpco would receive $ 115,000.00. This hypothetical demonstrates that at the time of the transfer petitioner was entitled to receive 100% of the value of the Property upon a constructive liquidation of the Partnership.
The principles set forth in *Schrier* suggest that in determining the percentage of petitioner's Partnership interest, it is appropriate to first determine the proportion of its economic interest in the real property that was transferred. Based on the terms of the Joint Venture Agreement, I conclude that the proportion of petitioner's beneficial interest in the Property was preserved by the terms of that agreement. There is simply no basis for the Division's determination that petitioner transferred 50 percent of its beneficial interest in the Property to Trumpco under the terms of the Joint Venture Agreement. The agreement entitles it to a 50 percent interest in any future appreciation in the Property and any potential increases in rent under the ESB lease and no more.

Petitioner calculates its 99.745 percent interest in the Partnership on the basis of each party's capital contribution. Petitioner contributed the *Empire State Building* with a book [*29*] value of $45 million, while Trumpco contributed $115,000.00. Thus, petitioner contributed 99.745 percent of Partnership capital and claims a 99.745 percent beneficial interest in the Partnership. Petitioner's calculation of its interest in the Partnership after the transfer is reasonable and consistent with the statute and the regulations. Accordingly, I conclude that petitioner had a 99.745 percent interest in the Partnership as it claims.

G. The Division's arguments for its position fail to take into account the economic realities of this transaction. The allocation of Partnership income, gain, profit and loss is not peripheral to the allocation of Partnership interests. The references to provisions of Articles III and IV and other terms and conditions of the Joint Venture Agreement in section 2.5 of the agreement clearly manifest the parties' intention to qualify the equal division of Partnership interest. The last clause of section 2.5 cannot be read in isolation from the rest of the Joint Venture Agreement.

The Vanity Fair article and newspaper accounts of the transfer do not bolster the Division's position. They merely report, with some skepticism, that Donald Trump claimed [*30*] to have acquired a 50-percent interest in the *Empire State Building* without investing his own funds. Evidence of Mr. Trump's interest in the *Empire State Building* must be found in the unambiguous language of the Joint Venture Agreement, not in his statements to the press.

The value of Trumpco's nonmonetary contributions to the Partnership is far too speculative to consider. In any case, it would appear that those contributions were intended to entitle it to exactly what it received: a 50-percent stake in any increase in property value or income brought about as a result of its efforts.

H. The petition of NS 1999 American Company, Nominee for the 1991 American Trust is granted, and the notices of determination of real property transfer tax and real property transfer gains tax, dated April 13, 1994, are canceled.
New York City Finance Letter Ruling No. 129-RP-10/88, 10/05/1988

Date Issued: 10/05/1988

Tax Type(s): New York City Other Special Taxes

RE: Request for Ruling Real Property Transfer Tax

"Furnished under the Freedom of Information Law. This ruling reflects the opinion of the Office of Legal Affairs as of the date of issuance and may not reflect subsequent court decisions or statutory changes pertaining to the subject matter of the opinion or the current policy of the Department of Finance."

October 5, 1988

This is in response to your letter dated April 13, 1988, concerning the applicability of the New York City Real Property Transfer Tax to the following situation as described in your letter:

X, Inc. ***** owns realty in New York City at the following locations: *****.

Prior to December, 1986, X was owned by Y and his son Z. Y held a 50.7% interest in ***** and Z held a 49.3% interest in X. In December, 1986, Y transferred .4% of X stock to his two daughters (Z's sisters). In January, 1987, Y transferred another .4% interest in X to his two daughters. Thereafter, Y owned 49.9% of X, Z owned 49.3% of X and Y's daughters owned .8% of X. At the time of these two transfers, Y was in good health. Y entered the hospital on December 17, 1987, for prostate surgery, which was successful. However, Y was readmitted to the hospital on January 6, 1988, when a cancerous tumor was discovered on Y's spine.

Y died on February 3, 1988, and, pursuant to the X shareholders' agreement, X must redeem Y's shares from his estate ***** for cash. After the redemption, Z will own 98.5% of X and Y's daughters will own 1.5%. You contend that no Real Property Transfer Tax is due, since there has not been a transfer of a controlling economic interest in X.

Section 11-2102.b(1) of the New York City Administrative Code imposes the Real Property Transfer Tax on each instrument or transaction effecting a transfer of a controlling economic interest in real property located in the City where the consideration for the economic interest exceeds $25,000. A controlling economic interest in real property includes the ownership of 50% or more of the total combined voting power or total fair market value of all classes of stock in a corporation which owns or leases real property. N.Y.C. Administrative Code § 11-2101.6 & .8.

In determining whether a controlling economic interest in real property has been conveyed, multiple transfers of economic interests made pursuant to a plan to transfer or acquire a controlling economic interest are aggregated. Furthermore, all transfers made by or to one or more parties within a three year period will be presumed related and will be aggregated. New York City Real Property Transfer Tax, Information Bulletin No. 2, Questions 17 and 20 (Dec. 16, 1986).

Clearly, neither of the described transfers alone (4%, .4% and 49.9% of X stock) constitute the transfer of a controlling economic interest. Therefore, it must be determined whether the transfers, made within a three year period, should be aggregated, thereby constituting a transfer of 50.7% of X stock. Provided that the December, 1986, and January, 1987, transfers by Y totaling .8% were made...
while he was in good health and not in contemplation of death, then these transactions will not be deemed related to the redemption and, therefore, will not be aggregated. In addition, interests transferred prior to July 13, 1986, will not be aggregated. Thus, there will be no transfer of a controlling economic interest in X for Real Property Transfer Tax purposes and, hence, no tax is due.

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EXHIBIT F
In the Matter of the Petitions of ESTATE OF MORTON J. GOLDMAN for Revision of Determinations or for Refunds of Real Estate Transfer Tax under Article 31 of the Tax Law and Tax on Gains Derived from Certain Real Property Transfers under Article 31-B of the Tax Law

DTA Nos. 813420 through 813423; TSB-D-97-(18)-R; Real Property Transfer Gains Tax

STATE OF NEW YORK-TAX APPEALS TRIBUNAL

1997 N.Y. Tax LEXIS 342

August 14, 1997

PANEL:
[*1] Donald C. DeWitt, President; Carroll R. Jenkins, Commissioner; Joseph W. Pinto, Jr., Commissioner.

OPINIONBY:
PER CURIAM

OPINION:
DECISION


Petitioner did not file a brief in support of its exception. The Division of Taxation filed a brief in opposition and petitioner filed a reply brief. Oral argument was not requested.

After reviewing the entire record in this matter, the Tax Appeals Tribunal renders the following decision.

Issues

I. Whether the Administrative Law Judge properly determined that real estate transfer tax, imposed pursuant to the provisions of Article 31 of the Tax Law, was due upon petitioner's sales of its shares of stock in two corporations, each of which owned an interest in New York real property.

II. Whether the Administrative Law Judge properly determined [*2] that tax on gains derived from certain real property transfers ("gains tax"), imposed pursuant to the provisions of Article 31-B of the Tax Law, n1 was due upon petitioner's sales of its shares of stock in two corporations, each of which owned an interest in New York real property.

n1 The real property transfer gains tax imposed by Tax Law Article 31-B was repealed on July 13, 1996. The repeal applies to transfers of real property that occur on or after June 15, 1996 (L 1996, ch 309, §§ 171-180).

III. Whether the imposition of these taxes by the Division of Taxation, under the facts and circumstances presented herein, violates the Equal Protection Clause and the Due Process Clause of the United States Constitution and the New York State Constitution.

Findings of Fact
We find the facts as determined by the Administrative Law Judge except for findings of fact "1," "2," "18," "20," "22" and "24" which have been modified. The Administrative Law Judge's findings of fact and the modified findings of fact are set forth below.

The representatives of petitioner and the Division of Taxation ("Division") entered into a written stipulation of facts the relevant portions of which are [*3] incorporated herein.

We modify findings of fact "1" and "2" of the Administrative Law Judge's determination to read as follows:

Prior to April 3, 1990, the capital stock of GKKS, Inc., an entity which owned an interest in real property located on Old Tarrytown Road, White Plains, New York, was owned by three shareholders: Morton J. Goldman ("Goldman"), Joseph Kruger ("Kruger") and Stephen M. Schainman ("Schainman"). Each shareholder owned one-third of the shares of capital stock of GKKS, Inc.

Prior to April 3, 1990, the capital stock of Mohawk Country-Home School, Inc. ("Mohawk"), an entity which owned an interest in real property located on Old Tarrytown Road, White Plains, New York, was owned by three shareholders: Goldman, Kruger and Schainman. Each shareholder owned one-third of the shares of capital stock of Mohawk. Each of the shareholders acquired their shares prior to 1983. n2

n2 We modified findings of fact "1" and "2" of the Administrative Law Judge's determination to show that each of the shareholders acquired their shares prior to the 1983 effective date of the gains tax.

Goldman died on April 3, 1990.

Elise R. Goldman, Executrix of the Estate of Goldman [*4] ("the executrix"), was issued Letters Testamentary on April 18, 1990.

On November 1, 1990, the Estate of Morton J. Goldman ("petitioner"), by its executrix, sold Goldman's shares of stock in GKKS, Inc. to GKKS, Inc. After the sale, the two remaining shareholders, Kruger and Schainman, each owned 50 percent of the outstanding shares of GKKS, Inc.

Neither Kruger nor Schainman acquired control of GKKS, Inc. as a result of the sale of petitioner's shares of GKKS, Inc. to it.

A 1989 agreement to which GKKS, Inc., Mohawk and the three equal shareholders of each were parties ("1989 shareholders' agreement") made the sale of the GKKS, Inc. shares by petitioner mandatory on Goldman's death.

On May 1, 1991, Schainman sold all of his shares of GKKS, Inc. to GKKS, Inc.

After the sale by Schainman, Kruger owned 100 percent of the outstanding shares of GKKS, Inc. and, thus, controlled GKKS, Inc.

The 1989 shareholders' agreement required GKKS, Inc. to buy its shares tendered by Schainman.

On November 1, 1990, petitioner, by its executrix, sold Goldman's shares of stock in Mohawk to Mohawk. After the sale, the two remaining shareholders, Kruger and Schainman, each owned 50 percent of the outstanding [*5] shares of Mohawk.

Neither Kruger nor Schainman acquired control of Mohawk as a result of the sale of petitioner's shares of Mohawk to it.

The 1989 shareholders' agreement made the sale of the Mohawk shares by petitioner mandatory on Goldman's death.

On May 1, 1991, Schainman sold all of his shares of Mohawk to Mohawk.

After the sale by Schainman, Kruger owned 100 percent of the outstanding shares of Mohawk and, thus, controlled Mohawk.

The 1989 shareholders' agreement required Mohawk to buy its shares tendered by Schainman.
After an audit, the Division, on April 16, 1993, issued a Statement of Proposed Audit Changes which asserted a real estate transfer tax liability, relating to petitioner's sale of the GKKS, Inc. stock, in the amount of $1,400.00, plus interest, for a total amount due of $1,647.84. The Statement of Proposed Audit Changes explained, in part, as follows:

"Pursuant to Section 575.6(d) of the Real Estate Transfer Tax Regulations, 'where there is a transfer or acquisition of an interest in an entity that has an interest in real property, on or after July 1, 1989, and subsequently there is a transfer or acquisition of an additional interest or interests in [§6] the same entity, the transfers or acquisitions will be added together to determine if a controlling interest has occurred.' As a result of stock redemptions on 11/1/90 and 5/1/91, Joseph L. Kruger effectively acquired a 66 2/3% controlling interest in GKKS, Inc.

"Regulation Section 575.1(d)(4) states that 'in the case of a transfer or acquisition of a controlling interest in any entity that owns real property, consideration means the fair market value of the real property or interest therein, apportioned based on the percentage of the ownership interest transferred or acquired in the entity.'

"Since the arms length shareholders' agreement, dated 5/16/89, has established consideration for a 33 1/3% interest to be $700,000, it has been determined that a 16 2/3% interest has a fair market value of $350,000.

"Tax determined to be due under Article 31, Real Estate Transfer Tax Law, on the acquisition of the Goldman Estate's interest in GKKS, Inc. was calculated as follows:

"Consideration: $350,000.

"Tax Due ($2.00 per $500, or fractional part thereof, of the consideration amount) 1,400.

"Interest has been assessed in accordance with Section 1416 of [§7] the Tax Law, for the period beginning May 17, 1991, for failure to pay the tax within the time frame allowed."

We modify finding of fact "18" of the Administrative Law Judge's determination to read as follows:

On May 27, 1993, the Division issued a Notice of Determination to petitioner in the amount of $1,400.00 (real estate transfer tax), plus interest, for a total amount due of $1,660.85. Petitioner paid the tax and interest determined to be due pursuant to the Notice of Determination and, therefore, requests a refund of monies paid. n3

n3 We modified finding of fact "18" of the Administrative Law Judge's determination to clarify that interest was also paid.

After an audit, the Division, on April 16, 1993, issued a Statement of Proposed Audit Changes to petitioner relating to its sale of Mohawk stock which contained an explanation nearly identical to the one set forth in the statement issued for the sale of the GKKS, Inc. stock.

We modify finding of fact "20" of the Administrative Law Judge's determination to read as follows:

On May 27, 1993, the Division issued another Notice of Determination to petitioner in the amount of $1,400.00, plus interest, for a total [§8] amount due of $1,660.85 (the same amount of real estate transfer tax assessed for the sale of the GKKS, Inc. stock). Petitioner paid the tax and interest determined to be due pursuant to the Notice of Determination and, therefore, requests a refund of monies paid. n4
n4 We modified finding of fact "20" of the Administrative Law Judge's determination to clarify that interest was also paid.

After an audit, the Division, on April 16, 1993, issued a Statement of Proposed Audit Changes to petitioner, relating to its sale of the GKKS, Inc. stock, asserting additional gains tax of $34,160.97, plus interest, for a total amount due of $40,208.49. The Statement of Proposed Audit Changes explained, in part, as follows:

"In accordance with Regulation Section 590.45(c) and (d), 'interests acquired after March 23, 1983, are added together for purposes of determining whether an acquisition of a controlling interest has occurred.' This includes all interests acquired within a three year period. Since the statute looks to the acquisition, it is the act of the transferee which triggers the tax (Emphasis added).

"Your tax liability is a result of Joseph L. Kruger's acquisition [*9] of a 66 2/3% interest within a three year period. Pursuant to the stock redemptions by GKKS, Inc. of the shares held by the Estate of Morton Goldman and Stephen Schainman, on 11/1/90 and 5/1/90, [sic] respectively, a controlling interest was acquired by Mr. Kruger on 5/1/91. Your liability is to the extent of the interest that was transferred to Joseph L. Kruger by the Estate of Morton Goldman.

"Tax determined to be due under Article 31-B was calculated as follows:

\[
\begin{align*}
\text{Consideration}^* (\$ 2,100,000 \times 16.67\%) &= 350,000.00 \\
\text{Less Original Purchase Price} (\$ 50,332 \times 16.67\%) &= 8,390.34 \\
\text{Gain subject to tax} &= 341,609.66 \\
\text{Tax determined to be due (10\%)} &= 34,160.97 \\
\end{align*}
\]

* Since the arms length shareholder's agreement, dated 5/16/89, establishes the fair market value of a 33 1/3% interest to be $700,000., the fair market value of a 16 2/3% interest is determined to be $350,000.00.

"In addition, interest was assessed for the period beginning May 17, 1991, pursuant to Section 1446(1) of the Tax Law, which provides, in part, that 'if the tax commission determines that there has been an underpayment of tax, the transferor shall pay interest to the commission on the [*10] amount of tax not paid.'"

We modify finding of fact "22" of the Administrative Law Judge's determination to read as follows:

On May 27, 1993, the Division issued a Notice of Determination to petitioner assessing gains tax in the amount of $34,160.97, plus interest, for a total amount due of $40,525.87 for petitioner's sale of the GKKS, Inc. stock. Petitioner paid the tax and interest determined to be due pursuant to the Notice of Determination and now requests a refund of the monies paid. n5

n5 We modified finding of fact "22" of the Administrative Law Judge's determination to clarify that tax and interest have been paid and that a refund is requested.
After an audit, the Division issued a Statement of Proposed Audit Changes to petitioner asserting additional gains tax due, relating to its sale of the Mohawk stock, in the amount of $3,521.31, plus interest, for a total amount due of $4,144.69. The Statement of Proposed Audit Changes contained an explanation similar to the notice which asserted additional gains tax due on petitioner's sale of the GKKKS, Inc. stock. The notice computed the additional tax due as follows:

"Tax determined to be due under Article 31-B was calculated as follows:

Consideration * ($2,100,000 x 16.67%) = $350,000.00
Less Original Purchase Price
   ($1,888,344 x 16.67%) = $314,786.94
Gain subject to tax
   $35,213.06
Tax due (10% of gain) $3,521.31

* Since the arms length shareholder's agreement, dated 5/16/89, establishes the fair market value of a 33 1/3% interest to be $700,000, the fair market value of a 16 2/3% interest is determined to be $350,000.00.

"In addition, interest was assessed for the period beginning May 17, 1991, pursuant to Section 1446(1) of the Tax Law, which provides, in part, that 'if the tax commission determines that there has been and [sic] underpayment of tax, the transferor shall pay interest to the commission on the amount of tax not paid.'"

We modify finding of fact "24" of the Administrative Law Judge's determination to read as follows:

On May 27, 1993, the Division issued a Notice of Determination to petitioner assessing gains tax, relating to petitioner's sale of the Mohawk stock, in the amount of $3,521.31, plus interest, for a total amount due of $4,177.41. Petitioner paid the tax and interest determined to be due pursuant to [*12] the Notice of Determination and is, therefore, requesting a refund of the monies paid. n6

n6 We modified finding of fact "24" of the Administrative Law Judge's determination to clarify that interest was also paid.

Subsequent to the issuance of the notices of determination which assessed gains tax on petitioner's transfers of stock in the two corporations, the Division issued two notices of assessment resolution in response to information received from petitioner's representative. These documents, which contained identical explanations, stated, in part, as follows:

"You cite the aggregation clause of Tax Law Section 1440.7 as the basis for your disagreement. The aggregation clause of Section 1440.7 (20 NYCRR 590.43), however, does not apply for purposes of determining whether an acquisition of a controlling interest was acquired or for purposes of computing consideration in the case of an acquisition of a controlling interest in an entity with an interest in real property. The aggregation clause of Tax Law Section 1440.7 applies only in the case of successive transfers by one transferor of contiguous or adjacent parcels of real property. It does not apply in the case of [*13] successive acquisitions by one transferee of ownership interests in an entity which owns a single parcel of real property.

"The statutory authority for aggregating successive acquisitions of stock in an entity with an interest in real property is found in the regulatory interpretation of Tax Law Section 1440(2), wherein Section
590.45 specifically requires that all ownership interests acquired by one transferee within a 3 year period be added together for purposes of determining whether an acquisition of a controlling interest has occurred.

"Further, for purposes of computing consideration in the case of an acquisition of a controlling interest in an entity which owns an interest in real property, Tax Law Section 1440.1(c) requires that there be an apportionment of the fair market value of the interest in real property to the controlling interest ACQUIRED. If the fair market value of the property apportioned to the percentage interest acquired is $1 million or more, each transferor is subject to tax based upon his/her pro rata interest transferred. Because the statute looks to the acquisition of the controlling interest, it is the act of the transferee which triggers the tax [*14] (20 NYCRR 590.44)."

The affidavit of petitioner's executrix, Elise R. Goldman, attached to the written stipulation of facts (as Stipulation Exhibit "B") stated, in pertinent part, as follows:

"As executrix of the estate of Morton J. Goldman, I sold stock in each of the corporations to the respective corporations. My sale was made on 11/1/90. The sale on 5/1/91 was of stock owned by Stephen Schainman. He and I did not act in concert. The facts here make absolutely clear that the transfers were independent of each other.

"The estate's stock was tendered pursuant to a stockholders' agreement entered into May 16, 1989, a copy of which is attached hereto, and made part hereof. Paragraph 2 thereof made it mandatory that I, as executrix of my husband's estate, sell all his shares in the two corporations herein involved, namely GKKS, Inc. and Mohawk Country-Home School, Inc., upon his death.

* * *

"My husband died April 3, 1990. Accordingly, pursuant to the mandatory provisions of the contract, the shares owned by the estate in each of those corporations were sold on November 1, 1990.

"There was no plan that either of the two remaining shareholders would subsequently sell his stock [*15] to the corporation. Mr. Schainman did not consult me with regard to the sale of his shares.

"Indeed, that sale by Mr. Schainman was detrimental to the estate. Paragraph 3 of the agreement provides that over 70% of the sale price for the estate's shares would be paid in 20 consecutive semi-annual installments represented by notes. However, paragraph 3(c) of the agreement provides that in the event of a second sale, then one-half of the principal amount of each installment thereafter payable is deferred until the date of the last installment payable to the estate. Thus, the result of Mr. Schainman's sale of his stock was that the estate is receiving only one-half the original amount of each note due it and will receive the deferred amount only after 10 years from the date of sale by the estate."

The shareholders' agreement, entered into on May 16, 1989 among Goldman, Kruger, Schainman, GKKS, Inc., Mohawk and a third corporation, Mohawk-White Plains, provided, in paragraphs 1 and 2 thereof, as follows:

"1. Lifetime Sale of Stock.

"Goldman, Kruger and Schainman each hereby agrees that he will not sell, transfer, pledge or otherwise encumber any of his shares of stock of the [*16] Corporations, except as provided in this Agreement. Should any of them during his lifetime desire to sell his shares, he shall give to each of the Corporations not less than six months written notice, by certified or registered mail, prior to a stated date of sale, which shall be on a subsequent May 1 or November 1 of any year, and shall state in such notice that he desires to sell all of his shares in all three of the Corporations at the prices and on the terms hereinafter specified in paragraph 3. At the same time that such notice shall be given, the selling shareholder shall also send copies of such written notice, by certified or registered mail, to each of the other individual shareholders. Each of the Corporations hereby agrees to purchase its shares from the selling shareholder on the stated date of sale at the price and on the terms set forth below in paragraph 3."

"2. Sale of Stock on Death.
"Goldman, Kruger and Schainman each hereby agrees that, upon his death, the executors or administrators of his estate shall sell all of his shares in all three Corporations for purchase by their respective treasuries at the prices and on the terms hereinafter specified in paragraph [*17] 3. Each of the Corporations hereby agrees to purchase its shares from the estate of the deceased shareholder at the price and on the terms set forth below in paragraph 3. The date of such sale shall be the May 1 or November 1 next succeeding the date of death, whichever shall first occur more than six months following the date of death."

The affidavit of Joseph Kruger, sworn to the 25th day of April 1994, establishes the following facts:

"I did not intend to acquire control of the corporations by their purchases of the Goldman shares.

"At the time of Morton Goldman's death, I did not know that Stephen Schainman would subsequently tender his shares in each of the corporations to that corporation, which, under the May 16, 1989 agreement, each corporation was required to buy the tendered shares.

"I did not acquire control of the corporations by acting in concert at any time with Mr. Schainman. Such control was not acquired by reason of the mandatory purchase by the corporations of their respective shares from the Goldman estate. Control was acquired only as a result of Mr. Schainman's subsequent unilateral decision to tender his shares in the corporations."

Petitioner submitted [*18] the affidavit of Stephen M. Schainman, sworn to the 12th day of June 1995, to establish the following facts:

"Prior to the death of Morton Goldman, he, Joseph Kruger and I each owned one-third of the shares of GKKS, Inc. and of Mohawk Country-Home School, Inc.

"A stockholders' agreement provided that each corporation had to buy its own shares when a stockholder offered them. Accordingly, when I offered my shares to the corporations, each corporation bought its shares on May 1, 1991.

"I did not consult Elise Goldman, the executrix of Morton Goldman's estate, in connection with my offer to sell, or sale of my shares of the two corporations. I did not act in concert at any time with her. I made my own independent decision to sell my shares in the two corporations. I did not make any agreement with her or have any plan with her that I would sell my shares in the two corporations."

The Determination of the Administrative Law Judge

The Administrative Law Judge concluded, in relevant part, that: i) Kruger acquired a controlling interest in each corporation by virtue of the transfers by petitioner and by Schainman to the two corporations pursuant to 20 NYCRR 575.6(d); ii) petitioner's [*19] argument that there is no provision in Article 31 of the Tax Law permitting aggregation of successive sale of shares of stock by different transferors to determine whether there has been a transfer or acquisition of a controlling interest is without merit; iii) the real property transfer tax is imposed by Tax Law § 1402, not the regulation (20 NYCRR 575.6[d]); and iv) the transfer tax here was only imposed once (conclusion of law "C").

The Administrative Law Judge also concluded with respect to the gains tax that: i) our decision in Matter of Harris (Tax Appeals Tribunal, December 30, 1993) is controlling in this matter and the aggregation clause of Tax Law former § 1440(7) is not applicable in determining whether an acquisition of a controlling interest has occurred; ii) the intent of the transferors was immaterial to the determination of whether there was an acquisition of a controlling interest; iii) it is the acts of transferees acting in concert that are looked to in determining whether there has been an acquisition of a controlling interest; iv) Kruger, as the only transferee, could not act in concert with himself, so his intent too, is irrelevant; v) petitioner's argument, [*20] that Chapter 170 of the Laws of 1994 n7 provides that successive transfers before June 9, 1994 should not be aggregated under the law and rules in effect immediately prior to June 9, 1994, lacks merit (conclusions of law "F" and "G"); vi) petitioner was not deprived of due process and equal protection (conclusion of law "I"); vii) petitioner failed to show any specific facts that would support its claim that the subject regulations (20 NYCRR 575.6[a], [c] and [d] [relating to real property transfer tax] and 590.44[a] and 590.45[c] and [d] [relating to the
gains tax)) violate its due process or equal protection rights facially or as applied (conclusion of law "J"); and viii) the notices of determination issued on May 27, 1993 were proper and he sustained them (conclusion of law "K").

n7 The effective clause.

Arguments on Exception

Petitioner takes exception to each of the above conclusions of law of the Administrative Law Judge. Petitioner also makes proposed modifications to the findings of fact of the Administrative Law Judge. We have incorporated petitioner's proposed changes in the findings of fact above.

Petitioner argues, as it did below, that gains tax is not due [*21] under Article 31-B of the Tax Law. Petitioner urges that Matter of Harris (supra) is not controlling here. It is petitioner's contention that the affidavits of Elise Goldman, Schainman and Kruger show that there was no plan or agreement to effectuate a transfer or acquisition of a controlling interest. Petitioner also claims that the Department's regulation (i.e., 20 NYCRR 575.6(e)) exempts petitioner from the transfer tax. Further, petitioner maintains that the amendments to the gains tax statutes made by Chapter 170 of the Laws of 1994 demonstrate that the Division's interpretation of the statutes as they existed in 1990 was erroneous.

Petitioner also contends that transfer tax is not due under Article 31 of the Tax Law. This is true, petitioner argues, because it did not sell a controlling interest. In addition, petitioner contends that there is no provision in Article 31 (while there is such a provision in Article 31-B) which permits aggregation of successive shares of stock. In particular, petitioner argues that the transactions involved here are not governed by 20 NYCRR 575.6(d) because there was no transfer of a controlling interest by a single document. Further, petitioner [*22] urges that, under 20 NYCRR 575.6(e), the transfer tax can only be imposed once. Imposing the tax on both petitioner and Schainman, it argues, is to impose the tax twice.

Petitioner also maintains that the regulations, not the statutes, impose the transfer and/or gains taxes on the subject transactions. Therefore, petitioner asserts that, to the extent that it is the regulations and not the statutes which impose these taxes, the taxes are unlawful.

Petitioner also argues that the Administrative Law Judge erred in rejecting petitioner's argument that Articles 31 and 31-B of the Tax Law and the corresponding regulations, as applied to these transactions, are unconstitutional and violate the Equal Protection and the Due Process Clauses of the New York State Constitution and the United States Constitution.

The Division counters that petitioner's transfers are properly subject to the imposition of gains tax because, as a result of the transfers of their shares by petitioner and Schainman to the two corporations within a three-year period, Kruger acquired a controlling interest in the corporations. Moreover, the Division argues, petitioner's reliance on the aggregation clause provision [*23] of Tax Law former § 1440(7) is misplaced since we held in Matter of Harris (supra) that the aggregation clause was inapplicable in determining whether an acquisition of a controlling interest has occurred. The decision in Harris, the Division argues, also held that the transferor's intent does not determine whether there has been a taxable transaction. As to petitioner's contentions that the 1994 amendments to the statute show that the Division's interpretations are erroneous, the Division states that such amendments dealt solely with the aggregation clause which is not applicable in determining whether a taxable transaction occurred.

With regard to the transfer tax, the Division argues that Article 31 plainly imposes the tax upon the acquisition of a controlling interest in an entity owning an interest in real property. The Division states that, contrary to petitioner's contentions, the language of Articles 31 and 31-B are identical with respect to the definition of transfer or conveyance of real property in that both include the transfer or acquisition of a controlling interest in an entity with an interest in real property. The Division rejects the claim that the transfer [*24] has been imposed twice and argues that 20 NYCRR 575.6(d) deals directly with the type of situation which is at issue herein.

With regard to the issue of the constitutionality of the application of the taxing statutes, the Division urges that petitioner is, in fact, challenging the facial constitutionality of the statutes. In the alternative, if we decide that petitioner is challenging the statutes as applied, the Division states petitioner's arguments are still without merit. With respect to petitioner's due process argument, the Division contends that the State of New York has a sufficient link to the transaction which it is taxing. As to petitioner's equal protection contentions, the Division maintains that the statutes do not differentiate between those who make sales of non-controlling interests and those who make identical sales of non-controlling interests together with later, independent sales of controlling interests by others. This is true, the Divi-
sion states, because the tax is imposed only on the acquisition of a controlling interest. The Division asserts that all transfers within a three-year period are aggregated to determine whether a taxable acquisition of a controlling [*25] interest has occurred.

Opinion

As to petitioner's claims with respect to the transfer tax, Tax Law former § 1402 n8 imposed a real estate transfer tax on each conveyance of real property or interest therein "when the consideration . . . exceeds five hundred dollars, at the rate of two dollars for each five hundred dollars or fractional part thereof . . . ." Tax Law § 1404(a) provided, in relevant part, that the real estate transfer tax shall be paid by the grantor.

n8 As amended by L 1989, ch 61. Effective July 1, 1989 and applicable to conveyances occurring on or after that date, except for conveyances which are made pursuant to binding written contracts entered into on or before February 16, 1989, provided that the date of execution of such contract is confirmed by independent evidence. Future references to Articles 31 and 31-B are to those articles as amended by this chapter law.

Tax Law § 1401(e) defines a "conveyance" of real property, for purposes of the transfer tax, to include, among other things, the "transfer or acquisition of a controlling interest in any entity with an interest in real property."

Tax Law § 1401(b) n9 defines "controlling interest," as pertains [*26] to a corporation, to mean:

"either fifty percent or more of the total combined voting power of all classes of stock of such corporation, or fifty percent or more of the capital, profits or beneficial interest in such voting stock of such corporation . . . ."

20 NYCRR 575.6(a) provides, in pertinent part, that:

"In the case of a corporation which has an interest in real property, the transfer or acquisition of a controlling interest in the corporation, as defined in section 575.1(b) of this Part, occurs when a person, or group of persons acting in concert, transfers or acquires a total of 50 percent or more of the voting stock in such corporation."

20 NYCRR 575.6(c) states, in pertinent part, that:

"for purposes of determining whether a controlling interest is transferred or acquired, only transfers or acquisitions of interests occurring on or after July 1, 1989 are added together."

20 NYCRR 575.6(d) provides, in pertinent part, as follows:

"Where there is a transfer or acquisition of an interest in an entity that has an interest in real property, on or after July 1, 1989, and subsequently there is a transfer or acquisition of an additional interest or interests [*27] in the same entity, the transfers or acquisitions will be added together to determine if a transfer or acquisition of a controlling interest has occurred. Where there is a transfer or acquisition of a controlling interest in an entity on or after July 1, 1989, and the real estate transfer tax is paid on that transfer or acquisition and there is a subsequent transfer or acquisition of an additional interest in the same entity, it is considered that a second transfer or acquisition of a controlling interest has occurred which is subject to the real estate transfer tax. No transfer or acquisition of an interest in an entity that has an interest in real property will be added to another transfer or acquisition of a interest in the same entity if they occur more than three years apart, unless the transfers or acquisitions were so timed as part of a plan to avoid the real estate transfer tax."

n9 As added by L 1989, ch 61, § 176.
There is no dispute that petitioner's transfers of the stock of both corporations on November 1, 1990 did not constitute transfers or acquisitions of controlling interests in entities owning an interest in real property. While it is true that after the [*28] transfer of petitioner's shares the remaining shareholders (Kruger and Schainman) each owned 50 percent of the stock in each of the corporations, the shares transferred by petitioner were not added to the shares already owned by Kruger and Schainman since 20 NYCRR 575.6(c) provides that, for purposes of determining whether a controlling interest is transferred or acquired, only transfers or acquisitions occurring on or after July 1, 1989 are added together. All of these shareholders had acquired their shares prior to July 1, 1989. 

However, upon the transfer of Schainman's shares in the two corporations on May 1, 1991, the sole remaining shareholder, Kruger, acquired a controlling interest in each, i.e., by virtue of the transfers by petitioner and by Schainman, he acquired a 66 2/3% interest in GKKS, Inc. and in Mohawk. Despite petitioner's contentions to the contrary, the Administrative Law Judge correctly concluded that the provisions of 20 NYCRR 575.6(d), relating to the transfer tax, is on point with the facts here. 

Petitioner next claims that, unlike Article 31-B of the Tax Law, there is no provision in Article 31 which permits an aggregation of successive sales of shares of [*29] stock by different transferors to determine whether there has been a transfer or acquisition of a controlling interest. Petitioner's argument is without merit. The definition of a transfer or conveyance of real property in Articles 31 and 31-B and the definition (in those articles) of a transfer or acquisition of a controlling interest in an entity with an interest in real property were identical. Petitioner further contends that it is the regulation (20 NYCRR 575.6[d]), and not the statute, upon which the Division relies to impose the transfer tax upon petitioner's sales of shares. If the statute does not impose the tax, the Division, by means of a regulation, cannot do so. This argument, too, is rejected. 

When reviewing an administrative determination, the construction given statutes and regulations by the agency which is responsible for their administration will, if not irrational or unreasonable, be upheld (Mobil Intl. Fin. Corp. v. State Tax Commn., 117 AD2d 103, 501 NYS2d 947).

In Blue Spruce Farms v. State Tax Commn. (99 AD2d 867, 472 NYS2d 744, 745, affd 64 NY2d 682, 485 NYS2d 526), the court stated:

"To prevail over the administrative construction, petitioner [*30] must establish not only that its interpretation of the law is a plausible one but, also, that its interpretation is the only reasonable construction (see, Matter of Lakeland Farms v. State Tax Commn., 40 AD2d 15, 18, 336 NYS2d 972). Thus, unless the Department of Taxation and Finance's regulation is shown to be irrational and inconsistent with the statute (Matter of Slattery Assoc. v. Tully, 79 AD2d 761, 434 NYS2d 788 [affd 54 NY2d 711, 442 NYS2d 978]) or erroneous (Matter of Kroner v. Procaccino, 39 NY2d 258, 383 NYS2d 295), it should be upheld."

It is not the regulation (20 NYCRR 575.6[d]) which imposes the transfer tax. The first words appearing in Tax Law former § 1402 were "[a] tax is hereby imposed" n10 upon each conveyance of real property or interest therein. The term "conveyance" includes, by definition, "the transfer or acquisition of a controlling interest in any entity with an interest in real property" (see, Tax Law § 1401[e]). The statute, by its express terms, imposes the transfer tax. The regulation merely sets forth the manner in which it is determined whether a transfer or acquisition of "a controlling interest" has occurred. As such, this [*31] regulation does not extend beyond the permissible limits of the statute.

n10 Emphasis added.

Petitioner next contends that: i) to tax petitioner as well as Schainman would be to impose the tax twice; and ii) the Department's regulation (20 NYCRR 575.6[e]) actually exempts petitioner from tax because the regulation states that "the tax is only imposed once when there is both a transfer and an acquisition of a controlling interest in the same conveyance." Petitioner argues that there were two conveyances here (petitioner's and Schainman's), so the controlling interest was not conveyed in a single document.

We address petitioner's last claim first. The transfer of petitioner's shares of both corporations did not result in the transfer or acquisition of a controlling interest and did not result in the imposition of real estate transfer tax against petitioner. It was only upon Schainman's transfers of his stock that Kruger acquired a controlling interest in the corporations. The sale of Schainman's shares of each corporation resulted in the acquisition of a controlling interest by Kruger in a single conveyance. There was only one conveyance that resulted in a transfer or acquisition [*32] of a controlling...
interest, i.e. Schainman's. Thus, 20 NYCRR 575.6(e) does not exempt petitioner from tax. Petitioner's claim that the tax is being imposed twice is similarly rejected. Petitioner was assessed tax only upon the consideration received for its shares. To the extent the transfer tax was also imposed upon Schainman, it would only have been imposed upon the consideration he received for his shares. The tax is imposed once, but each transferor is paying his respective share of the total.

We now address petitioner's claims with respect to the gains tax.

Tax Law former § 1441 imposed a 10 percent tax on gains derived from the transfer of real property within New York State.

Tax Law former § 1440(7), n11 in effect during the period at issue, provided, in pertinent part, as follows:

"transfer of real property' means the transfer or transfers of any interest in real property by any method, including . . . acquisition of a controlling interest in any entity with an interest in real property.

* * *

"Transfer of real property shall also include partial or successive transfers, unless the transferor or transferors furnish a sworn statement that such transfers are not pursuant [*33] to an agreement or plan to effectuate by partial or successive transfers a transfer which would otherwise be included in the coverage of this article . . . ."

Tax Law former § 1440(2)(i) defined "controlling interest" to mean:

"in the case of a corporation, either fifty percent or more of the total combined voting power of all classes of stock of such corporation, or fifty percent or more of the capital, profits or beneficial interest in such voting stock of such corporation."

20 NYCRR former 590.44(a) provided, in pertinent part, as follows:

"Question: How is the phrase 'acquisition of a controlling interest in an entity with an interest in real property' applied?

"Answer: The term 'controlling interest' is defined in section 1440(2) of the Tax Law to mean:

'(i) in the case of a corporation, either fifty percent or more of the total combined voting power of all classes of stock of such corporation, or fifty percent or more of the capital, profits or beneficial interest in such voting stock of such corporation, and (ii) in the case of a partnership, association, trust or other entity, fifty percent or more of the capital, profits or beneficial interest in such [*34] partnership, association, trust or other entity.'

"Thus, for purposes of the gains tax, in the case of a corporation which has an interest in real property, the acquisition of a controlling interest in the corporation occurs when a person or group of persons, acting in concert, acquires a total of 50 percent or more of the voting stock in such corporation . . . . Because the statute looks to the acquisition of the controlling interest, it is the act of the transferee which triggers the tax" (emphasis added).

20 NYCRR former 590.45(c) and (d) provided as follows:

"(c) Question: If a shareholder owned a 20-percent interest in a corporation prior to March 28, 1983 and acquires an additional 35 percent on July 10, 1984, has there been an acquisition of a controlling interest?
"Answer: No. For purposes of determining whether a controlling interest is acquired, only acquisitions of interests occurring after March 28, 1983 are added together.

"(d) Question: If a shareholder acquires a 50-percent interest in a corporation and gains tax is paid on the transfer, and one year later the same shareholder acquires an additional 20 percent, is there a second acquisition [*35] of a controlling interest?

"Answer: Yes. The interests acquired after March 28, 1983 are added together in determining whether an acquisition of a controlling interest has occurred. No acquisition of stock will be added to another acquisition of stock if they occur more than three years apart, unless the acquisitions were so timed as part of a plan to avoid the gains tax. An example of this would be if T acquired 80 percent of the stock and simultaneously contracted for the purchase of the remaining 20 percent in three years and one day."

n11 As amended by L 1989, ch 61. All future references to provisions of Article 31-B are to the law in effect during the subject period.

Petitioner again argues that each of its sales of corporate stock was exempt from the imposition of gains tax because it was not a transfer or acquisition of a controlling interest and that the tax was imposed solely by virtue of Schaiman's subsequent sales of his stock in the corporations. Petitioner is correct that its transfers alone did not constitute a transfer or acquisition of a controlling interest. It is also true that it was by virtue of Schaiman's subsequent sale of his shares that a transfer [*36] or acquisition of a controlling interest occurred and tax became due.

Petitioner also points to the provisions of Tax Law former § 1440(7) which exempted partial or successive transfers wherein the transferors furnish a sworn statement that the transfers were not pursuant to an agreement or plan. Petitioner points out that it has provided such sworn statements in the form of affidavits of the executrix, Elise Goldman, and also from Messrs. Kruger and Schaiman.

Petitioner's reliance on the "aggregation clause" portion of Tax Law former § 1440(7) is misplaced. As the Administrative Law Judge noted, we rejected a similar contention in Matter of Harris (supra). In Harris, the petitioner also argued that the aggregation clause was applicable in determining whether an acquisition of a controlling interest had occurred. We stated in Harris that:

"At the time of this transaction, the first sentence of section 1440(7) of the Tax Law defined 'transfer of real property' to mean:

'the transfer or transfers of any interest in real property by an [sic] method, including but not limited to sale, exchange, assignment, surrender, mortgage foreclosure, transfer in lieu of [*37] foreclosure, option, trust indenture, taking by eminent domain, conveyance upon liquidation or by a receiver or acquisition of a controlling interest in any entity with an interest in real property."

"The structure of this sentence is significant because it switches from the term 'transfer' to the term 'acquisition' when describing a taxable entity transaction, i.e., a transaction involving an ownership interest in an entity that owns real property, rather than a direct ownership interest in real property (see, Matter of Bredero Vast Goed, N.V. v. Tax Commn. of State of New York, 146 AD2d 155, 539 NYS2d 823, appeal dismissed 74 NY2d 791, 545 NYS2d 105). We agree with the Division that the use of the word 'acquisition' rather than 'transfer' reflects a legislative decision to impose tax in entity transactions based on the acts of the transferee or transferees rather than on the acts of the transferors.

* * *
"We conclude that these regulations (20 NYCRR 590.44 and 590.45) are a correct interpretation of section 1440(7) of the Tax Law because they are consistent with the Legislature's choice of the word 'acquisition.'

* * *

"With respect to petitioner's contention [*38] that the aggregation clause must be applied to determine whether a taxable acquisition has occurred, we agree with the Division that the so-called aggregation clause is not applicable. The aggregation clause is a separate sentence in the section 1440(7) definition of transfer of real property which expands upon the basic definition included in the first sentence of section 1440(7) by stating that the 'transfer of real property shall also include partial or successive transfers' (citation omitted). Petitioner's construction would turn the statutory scheme on its head by applying the aggregation clause as a limitation on the basic definition of transfer of real property" (emphasis added).

Therefore, the aggregation clause is not applicable to the facts in this case and the intent of the transfereors, i.e., petitioner and Schainman, is not germane to the outcome. Petitioner asserts that, if the aggregation clause does not apply here, it is unclear what situation would trigger its application. It is clear that Tax Law former § 1440(7) provided for aggregation of the consideration of certain transfers of real property to determine whether the total consideration exceeds the $1,000,000.00 [*39] threshold for imposition of the gains tax. In this case, the issue of the $1,000,000.00 exemption is not before us.

Petitioner next points to that part of our decision in Matter of Harris (supra) wherein we stated:

"as the record reveals no information about the intent of the transferees, we conclude that petitioner has not established that the transferees were not acting in concert in acquiring 100% of the stock (see, 20 NYCRR 590.44[a])."

In the present matter, petitioner maintains that the Kruger affidavit clearly proves that he had no intention of acquiring control of the corporations by the two corporations' purchases of the Goldman stock.

The Administrative Law Judge rejected this argument stating that, while we noted in Harris the importance of determining the intent of the transferees, in the matter at issue there was a single transferee, Kruger. As previously indicated, 20 NYCRR former 590.44(a) states that:

"... for purposes of the gains tax, in the case of a corporation which has an interest in real property, the acquisition of a controlling interest in the corporation occurs when a person or group of persons, acting in concert, acquires [*40] a total of 50 percent or more of the voting stock in such corporation."

The Administrative Law Judge concluded that since one person cannot act in concert, it follows that when a single transferee (such as Kruger in the present matter) acquires a controlling interest as he did upon acquiring the shares of Goldman and Schainman, his intent is entirely irrelevant.

We affirm the Administrative Law Judge on this issue.

When there was an acquisition of a controlling interest, it was the act of the transferee(s) which triggered the tax (20 NYCRR former 590.45[a]). If there were multiple transferees, then it had to be determined if they were acting in concert (20 NYCRR former 590.46[b]). The regulation specifically addressed when a group of persons was acting in concert, focusing on whether persons were "acting in concert," not whether they meant to acquire a controlling interest (20 NYCRR former 590.46[b]). With regard to the latter, the regulation stated that a transfer or acquisition of a control- ling interest in an entity with an interest in real property occurred when a person (or persons acting in concert) trans- ferred or acquired 50% or more of the voting stock (20 NYCRR former [*41] 590.45[a]). In the instant matter, it was the act of the acquisition of a controlling interest by Mr. Kruger which triggered the tax, not whether he meant to ac- quire a controlling interest. Arguably, the only time an analysis of intent arose out of the acquisition of a controlling interest was when transferees were said to have acted in concert and were considered to have acted as a single entity. In
the instant matter, there was one transferee and we do not reach the analysis attending circumstances with multiple transferees.

In Harris, we made the statement, in dicta, n12 that "in entity transactions the activities and intent of the transferee or transferees determine whether there is a taxable event, not those of the transferor or transferors" (Matter of Harris, supra). This statement was made in the decision immediately after we disagreed with both the Administrative Law Judge and the petitioner that the intent of the transferor needed to be established before the tax was triggered in a controlling interest acquisition and immediately before we cited the regulation at 20 NYCRR former 590.44, which stated that in controlling interest acquisitions it was the act of [\(^{42}\) the transferee which triggered the tax. The discussion of intent was necessary therein because the petitioner had argued that her transfer was not pursuant to a plan, a concept found in the regulations at 20 NYCRR former 590.44(a), which related to the aggregation of partial or successive transfers such that they are deemed a single transfer of real property. We decided that the correct analysis in controlling interest acquisitions was to determine the act of the transferees (actual acquisition of a controlling interest) (20 NYCRR former 590.45[a]) and whether the transferees' interests could be aggregated because they had acted in concert pursuant to 20 NYCRR former 590.45(b). Since no evidence was offered to disprove their acting in concert, the imposition of the tax was sustained.

n12 In Harris, there were three transferees which mandated the analysis of whether they were acting in concert. No such analysis would have been mandated with one transferee and the discussion, insofar as it addressed transactions with one transferee, was unnecessary to support the decision in Harris and, therefore, lacked binding precedential authority.

The use of the word "intent" in [\(^{43}\) Harris was unfortunate because it did not accurately characterize the plain meaning of 20 NYCRR former 590.44 or 590.45, which explicitly stated that it was the acts of the transferee(s) which triggered the tax and, if multiple transferees, their interests were aggregated if they were determined to have been acting in concert. The enumeration of some of the factors indicative of acting in concert, although inferring intent, was not meant to impose an "intent" standard on the act of the acquisition of a controlling interest when there was no provision or authority for doing so in the statute or regulations.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Estate of Morton J. Goldman is denied;
2. The determination of the Administrative Law Judge is affirmed;
3. The petitions of Estate of Morton J. Goldman are denied;
4. The two notices of determination, dated May 27, 1993, asserting gains tax of $ 34,160.97 each, plus interest, are sustained; and
5. The two notices of determination, dated May 27, 1993, asserting real estate transfer tax in the amount of $ 1,400.00 each, plus interest, are sustained.

Legal Topics:

For related research and practice materials, see the following legal topics:
STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

On October 2, 1991, a Petition for Advisory Opinion was received from Martin J. Walzer, Esq., 230 Park Avenue, New York, New York 10169.

The issue raised by Petitioner, Martin J. Walzer, Esq. is whether a transfer by Petitioner's client of her partnership interest will be aggregated with transfers by an unrelated transferor in determining whether a controlling interest is transferred for Real Property Transfer Gains Tax purposes (hereinafter the “gains tax”).

A New York general partnership (“P”) owns New York City real estate which is encumbered by a substantial mortgage. Record title to the real property is in the name of Holding Corp., but beneficial interest is, and has been, held at all times by the partners of the partnership.

The partnership comprises the following partners holding the following percentages in capital, profits and beneficial interest:

<table>
<thead>
<tr>
<th>Partner</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Holding corp. (“Corp”)</td>
<td>40%</td>
</tr>
<tr>
<td>Petitioner's client</td>
<td>40%</td>
</tr>
<tr>
<td>Unrelated individual, but related to Corp.</td>
<td>10%</td>
</tr>
<tr>
<td>Unrelated individual, but related to Corp.</td>
<td>100%</td>
</tr>
</tbody>
</table>

Petitioner's client is a woman over the age of 80. Petitioner's client intends to transfer all her interest in P to an amendable, revocable living trust under which she and her two daughters will be the trustees. Petitioner's client has already transferred substantially all her other assets to the trust. The trust provides that all of the income of the trust will be payable to Petitioner's client during her lifetime and on her death, the property will be distributed to her issue. Since the trust is amendable and revocable and provides for all the income to go to Petitioner's client, there are no gift tax consequences and, in fact, for federal income tax purposes, since Petitioner's client is a trustee, the trust will file income tax returns under the same tax ID number as Petitioner's client, i.e., Petitioner's clients’, social security number.

The sole shareholder of Corp., S, recently died and his estate now owns all of the stock in Corp. S's estate has advised Petitioner's client that it may be necessary for S's estate to sell the estate's interest in Corp., and if there is no sale, the interest will be distributed in accordance with
S’s will. This would probably occur within three years of the transfer to be made by Petitioner's client.

S and Petitioner's client are not related. Moreover, Petitioner's client has no interest in Corp. and Corp. and Petitioner's client have each held their 40% interest in P for a substantial number of years. Neither Petitioner's client nor her trust will purchase S’s interest in Corp.

Section 1440.7 of the Tax Law defines the term “transfer of real property”, in part, to mean the transfer or acquisition of a controlling interest in any entity with an interest in real property.

Section 1440.2 of the Tax Law provides as follows:

2. "Controlling interest" means (i) in the case of a corporation, either fifty percent or more if the total combined voting power of all classes of stock of such corporation, or fifty percent or more of the capital, profits or beneficial interest in such voting stock of such corporation, and (ii) in the case of a partnership, association, trust or other entity, fifty percent of more of the capital, profits or beneficial interest in such partnership, association, trust or other entity. (emphasis added)

Section 590.44 of the Gains Tax Regulations provides, in pertinent part, as follows:

(a) Question: How is the phrase "acquisition of a controlling interest in an entity with an interest in real property" applied.

Answer: . . . for purposes of the gains tax . . . In the case of a partnership, association, trust or other entity, the acquisition occurs when a group of persons, acting in concert, acquires a total of 50 percent or more of the capital, profits or beneficial interest in such entity. (emphasis added)

Section 590.45 of the Gains Tax Regulations provides, in part, as follows:

(b) Question: When is a group of persons acting in concert?

Answer: When the various purchasers have a relationship such that one purchaser influences or controls the actions of another. For example, if a parent and a wholly owned subsidiary each purchase a 25 percent interest in an entity, the two corporations will be considered to have acted in concert to acquire a controlling interest (i.e.. 50 percent) in the entity.
Where the individuals or entities are not commonly controlled or owned persons will be treated as acting, in concert only when the unity with which the purchasers have negotiated and will consummate the transfer of ownership interests supports a finding that they are acting as a single entity. If the acquisitions are completely independent, each purchaser buying without regard to the identity of other purchasers, then the acquisition will be treated as separate acquisitions. The transferees must provide affidavits swearing that they acquisitions are independent of each other.

Factors that will indicate whether persons are acting in concert include the following:

(1) The acquisitions are closely related in time.

(2) There are few purchasers.

(3) The contracts to purchase contain mutual terms.

(4) The purchasers have entered into an agreement in addition to the purchase contract binding themselves to a course of action with respect to the acquisition. (emphasis added)

Although the above regulation only sets forth the criteria of "acting in concert" for transferees, the criteria concerning "acting in concert" also applies to transferors. (See Section 575.6 of the Transfer Tax Regulations for similar treatment for transfer tax purposes.)

Accordingly, pursuant to Sections 590.44 and 590.45 of the Gains Tax Regulations, since Petitioner's client will transfer only a 40% interest in P and Petitioner's client and S are unrelated, Petitioner's client will not be deemed to have transferred or acted in concert to transfer a controlling interest pursuant to Sections 1440.2 and 1440.7 of the Tax Law. In addition, since the trust will only acquire a 40% in P from Petitioner's client and neither Petitioner's client nor the trust will acquire S's interest, pursuant to Sections 1440.2 and 1440.7 of the Tax Law the trust will not be deemed to have acquired a controlling interest.

DATED: December 31, 1991 

s/PAUL B. COBURN
Deputy Director
Taxpayer Services Division

NOTE: The opinions expressed in Advisory Opinions are limited to the facts set forth therein.
Application of Transfer Taxes

Determining the consideration to be taxed in a mezzanine foreclosure may have an impact on the decision whether to foreclose or continue negotiating a workout. The following examples apply the RPTT and the RETT to typical situations that may be seen in the context of mezzanine financing.29

**Example 1.** X is the owner of 100 percent of the limited liability company (LLC) interests in Y and Y is the owner of 100 percent of the LLC interests in Z. Z's only asset is a parcel of real property located in New York City. The fair market value of the real property is $2 million. The real property is encumbered by the lien of a mortgage having a current unpaid balance of $1.5 million, held by B Bank. X pledged its 100 percent LLC interest in Y to C bank as security for a mezzanine loan of $400,000, the current unpaid balance of which is $450,000, including accrued interest. There are no other outstanding loans.

C is presently enforcing its security interest in the LLC interest in Y, which results in both a transfer and acquisition of a controlling interest. Assume for purposes of Example 1 that C's successful bid at foreclosure is equal to the amount of the outstanding debt.

**RETT:** The consideration is computed as the lesser of:

1. (a) the $450,000 outstanding debt plus (b) the $1.5 million outstanding mortgage loan, equal to $1,950,000, or
2. fair market value (FMV) of the real property, which is $2 million.

The consideration is $1.95 million.

**RPTT:** The consideration is computed as (1) (a) the $450,000 successful bid plus (b) the $1.5 million outstanding mortgage loan.

The consideration is $1,950,000.

**Example 2.** Consider the same structure as in Example 1 above, however, Y has also pledged its LLC
interest in Z to D bank as collateral for a $300,000 senior mezzanine loan, which has an unpaid balance of $350,000, including unpaid interest. C bank is seeking to foreclose on X's pledge of its interest in Y. C is the successful bidder.

**RETT:** The consideration is computed as the lesser of

1. (a) the $450,000 outstanding debt plus (b) the outstanding senior loan debt of $350,000 plus (c) the $1.5 million outstanding mortgage loan, equal to $2.3 million, or

2. FMV of the real property, which is $2 million.

**The consideration is $2 million.**

**RPTT:** The consideration is computed as:

1. (a) the $450,000 successful bid plus (b) the outstanding senior loan debt of $350,000 plus (c) the $1.5 million outstanding mortgage loan, equal to $2.3 million.

**The consideration is $2.3 million. Note that the RPTT does not have an FMV cap.**

**Example 3.** Consider the structure outlined in Example 1 above; however, in C's foreclosure sale to enforce its security interest in X's shares of Y, a third party, E, is the winning bidder, with a bid of $300,000.

**RETT:** The consideration is (a) the $300,000 winning bid price and (b) the $1.5 million mortgage loan which represents the remaining senior liens or encumbrances on the real property after the conveyance.

**RPTT:** The RPTT does not distinguish between a foreclosure sale where the secured party is the winning bidder and where there is a third party bidder.

**The consideration for both taxes is $1.8 million.**

**Example 4.** Consider the structure outlined in Example 1 above; however, C enforces its security interest in X's shares of Y, by obtaining an assignment in lieu of foreclosure in its favor.
RETT: The consideration is the lesser of:

(1) (a) the $450,000 outstanding balance of the mezzanine loan and (b) the $1.5 million mortgage loan which represents the remaining senior liens or encumbrances on the real property after the conveyance or

(2) FMV of the real property, which is $2 million.

The consideration is $1.95 million.

RPTT: The consideration is

(1) (a) the $450,000 outstanding balance of the mezzanine loan and (b) the $1.5 million mortgage loan which represents the remaining senior liens or encumbrances on the real property after the conveyance.

The consideration is $1.95 million.

Example 5. S is the owner of 100 percent of the voting stock of K Corporation. K is the owner of 100 percent of the voting stock of L. L's assets consist of a parcel of real property located in New York City and other tangible assets. The FMV of the parcel of real property is $2.1 million and the FMV of the other assets is $300,000. The real property is encumbered by the lien of a mortgage having a current unpaid balance of $700,000. Also, L has other debts totaling $300,000. S pledged 100 percent of its stock in K to J as security for a $500,000 mezzanine loan, which has an unpaid balance of $550,000, including secured interest. J is presently enforcing its security interest in the voting stock owned by S, which results in both a transfer and an acquisition of a controlling interest with its winning bid at foreclosure of $550,000.

RETT: The consideration is the lesser of:

(1) the FMV of the real property, which is equal to $2.1 million, or

(2) the apportioned value of 30 (a) the $550,000 unpaid balance of the mezzanine loan, (b) the $700,000 outstanding mortgage debt plus (c) the $300,000 in other debt of the entity. The total amount to be apportioned is $1,550,000.
Apportionment is then calculated as follows:

The FMV of the real property, multiplied by the amount to be apportioned, divided by the FMV of all assets.

The apportioned amount is:

\[
\frac{1,550,000 \times 2,100,000}{2,400,000} = 1,356,250
\]

The consideration is $1,356,250.

RPTT:

The consideration should be computed as:

The apportioned value of (a) the $550,000 successful bid at foreclosure of the mezzanine loan, plus (b) the $700,000 outstanding mortgage debt plus (c) the $300,000 in other debt of the entity. The total amount to be apportioned is $1,550,000.

Apportionment is calculated as follows:

The FMV of the real property, divided by the FMV of all assets, multiplied by the consideration to be apportioned.

The apportioned amount is:

\[
\frac{1,550,000 \times 2,100,000}{2,400,000} = 1,356,250
\]

The consideration should be $1,356,250.

Example 6. Consider the same structure as Example 5, however, S only has a 60 percent interest in K, which it pledges to J as security for a debt of $500,000, with an outstanding balance of $550,000, including accrued interest.
**RETT:** The consideration is the lesser of:

(1) FMV of the real property multiplied by the equity interest being transferred, that is, $2.1 million x 60 percent = $1,260,000 or

(2) the apportioned value of (a) the $550,000 unpaid balance of the mezzanine loan, plus (b) the outstanding mortgage debt multiplied by the equity interest being transferred, that is, $700,000 x 60 percent = $420,000, plus (c) additional debt of the entity multiplied by the equity interest being transferred, that is, $300,000 x 60 percent = $180,000. The amount to be apportioned is $1,150,000.

Apportionment is calculated as follows:

\[ \frac{1,150,000 \times 2,100,000}{2,400,000} = 1,006,250 \]

The consideration is $1,006,250.

**RPTT:** The consideration should be:

the apportioned value of (a) the $550,000 successful bid at foreclosure of the mezzanine loan, plus (b) the $700,000 outstanding mortgage debt multiplied by the equity interest being transferred, that is, $700,000 x 60 percent = $420,000, plus (c) additional debt of the entity multiplied by the equity interest being transferred, that is, $300,000 x 60 percent = $180,000.

The amount to be apportioned is $1,150,000.

Apportionment is calculated as follows:

\[ \frac{1,150,000 \times 2,100,000}{2,400,000} = 1,006,250 \]

The consideration should be $1,006,250.
EXHIBIT I
STATEMENT OF AUDIT PROCEDURE

REAL PROPERTY TRANSFER TAX
TRANSFERS INTO AND OUT OF
CHARITABLE ORGANIZATIONS

A. Background

Generally, conveyances of property located in New York City, and economic interests in property in the City, are subject to the New York City Real Property Transfer Tax (“RPTT”). There are several exemptions from the RPTT, including transfers to or from charitable organizations. Specifically, conveyances to and from entities that are “organized and operated exclusively for religious, charitable or educational purposes” are exempt from the transfer tax. (See, the Rules of the City of New York, Title 19, Chapter 23, section 23-05(b)(2).)

This transfer tax exemption is very similar to the federal charitable exemption found in section 501(c)(3) of the Internal Revenue Code. Generally, when a charitable organization shows us that it is exempt from federal tax under IRC §501(c)(3), it is also exempt from the City’s transfer tax.

B. Scope

This statement alerts auditors and taxpayers to potentially abusive situations involving exempt entities, and outlines how we will treat these situations on audit.

The transactions covered by this procedure are illustrated by the following two examples, which are intended to be illustrative, and not all-inclusive.

1. The owner of real property in New York City transfers the property to an exempt charity. The charity then conveys the property to another party.

2. The 100% owner of a corporation that owns real property in the City transfers the property to an exempt charity. The corporation owner then transfers control of the corporation to someone else. The charity then transfers the property back to the corporation.
C. **Procedure**

If a charity is involved in a series of transactions where the end result is that the property, or an economic interest, is conveyed from one non-exempt party to another, we will look at the steps of the transaction to determine if the transaction should be taxable. This “step transaction doctrine” (where the steps of a transaction are linked to determine proper tax treatment) will be applied if:

1. the series of transactions was entered into pursuant to **binding agreements**, or
2. **evidence** exists that the series of **transactions** was entered into pursuant to a **plan**, even if there is no binding contract.

**Six Months**: If the series of transactions takes place within a period of six months, the transactions will be presumed to have taken place pursuant to a plan. This may be rebutted by evidence.

**Six Months to One Year**: If the series of transactions occurs within a period of six months to a year, the transactions will be audited to determine if the step transaction doctrine should be applied.

**More than One Year**: If a series of transactions takes place within a period of more than one year, all facts and circumstances will be considered to determine if the series of transactions should be audited.

D. **Discussion**

Courts regularly permit taxing authorities to look at the substance rather than the form of a transaction so that “mere formalisms” do not obscure the transaction’s true nature. The “step transaction doctrine” discussed above is an example of the use of the “form over substance” principle. The doctrine will be used to prevent the use of a charity as a means to avoid paying transfer tax on an otherwise taxable transfer or series of transfers.

Generally, a taxing authority may collapse the steps of a transaction to determine if it should be subject to tax when the criteria of any one of the following three tests are met:

- **End result test**: If the two transactions (owner to charity and then charity to new owner) were merely a means for the old owner to convey the property to a new owner, the “end result” test would be met. We will look at whether the parties intended to convey the property to a new owner, not whether the parties meant to avoid tax.

- **Interdependence test**: This test would be met if it were unlikely that either of the two transfers would have taken place except in contemplation of the other.

- **Binding Commitment test**: This test would be met if the two transactions took place pursuant to contracts entered into prior to the first transaction.
E. Review of Charitable Exemption

If Finance determines that the step transaction should be applied and the transactions are deemed taxable, this will also be treated as evidence that the charitable entity in question is not operating exclusively for religious, charitable or education purposes, and other City tax exemptions granted to the entity may be re-examined.

Even if we determine that the charitable exemption should not apply, the step transaction doctrine will still be applied so that a series of transactions will only be taxed once.
EXHIBIT J
STATEMENT OF AUDIT PROCEDURE

AUDITS OF PURPORTED “DUMMY/STRAWMAN” TRANSFERS IN CONNECTION WITH REAL ESTATE SYNDICATIONS

I. BACKGROUND

Investors use a variety of vehicles to acquire and finance the acquisition of real property in New York City. Frequently, one or more promoters will form a partnership or limited liability company to acquire a property. The promoters make an initial capital contribution to that entity (hereafter referred to as the “owner/principal”). Generally, the promoters then raise the money to acquire the property by selling interests in the owner/principal to investors using a public offering or private placement syndication. Additional funds may be obtained from lenders, usually on a short term unsecured basis to be repaid out of the proceeds of the syndication or replaced with permanent financing.

Generally the investors acquire a majority interest in the owner/principal through the syndication. If the syndication is completed or substantially completed before the owner/principal acquires the real property, the New York City Real Property Transfer Tax (“RPTT”) applies only to the purchase of the property by the owner/principal.

If the owner/principal purchases the property prior to the syndication, the RPTT would apply twice, first to purchase of the real property by the owner/principal and again to the transfer of a controlling economic interest in the owner/principal if the investors acquire a 50 percent¹ or greater ownership interest pursuant to the syndication.

¹The 50 percent ownership interest is measured by the fair market value or the combined voting power of the stock in a corporation or by the capital, profits or beneficial ownership in a partnership, trust or other entity. A transfer of a controlling interest can include the issuance of shares or interests in the entity. A series of transfers of ownership interests in an entity can constitute a controlling interest transfer if the transfers are pursuant to a plan. Transfers within three years are presumed to be pursuant to such a plan. Transfers pursuant to a syndication also are considered to be made pursuant to a plan. See Title 19 Rules of the City of New York §23-02, “Controlling interest”, par. (2), illustration (xiv).
Although syndication promoters try to time the transactions so as to avoid a double tax, occasionally they may not be able to do so. In those cases, the promoters will use another entity (hereafter referred to as the “nominee”) to acquire title to the property on behalf of the owner/principal. The nominee will hold title to the property only until the syndication can be completed or substantially completed, and will then transfer title to the property to the owner/principal. If properly structured and documented, the transfer of the property by the nominee to the owner/principal should qualify as a transfer from “a mere agent, dummy, straw man or conduit”[2] to its principal.

II. **SCOPE**

This Statement of Audit Procedure provides guidance to auditors examining a transaction for which the taxpayer has claimed the “dummy/strawman” exemption for a transfer from a nominee to an owner/principal as part of a real estate syndication as described above.

This Statement of Audit Procedure is not applicable in auditing a return relating to the acquisition of the property by the nominee.

This Statement of Audit Procedure shall apply to all open cases.

III. **PROCEDURES**

The auditor may accept as filed a return claiming the “dummy/strawman” exemption if all of the following conditions are met:

1. **Return.** The taxpayer must check condition (h) on the Form NYC-RPT and complete Schedule E claiming an exemption from the RPTT under the “dummy/strawman” exception.

2. **Documentation.** The auditor should request the following documents if not attached to the Form NYC-RPT:

   - nominee or agency agreement
   - formation documents for the nominee (the certificate of limited partnership, certificate of incorporation or articles of organization for a limited liability company)
   - syndication materials (the private placement or public offering materials sent to prospective investors)
   - loan agreements and other financing documents for financing the acquisition of the property by the nominee or the owner/principal
   - any other related documents

When reviewing the documents submitted, the auditor should look for the following:

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[2] The RPTT does not apply to:

- a deed, instrument or transaction conveying or transferring real property or an economic interest therein from a mere agent, dummy, straw man or conduit to his principal or a deed, instrument or transaction conveying or transferring real property or an economic interest therein from the principal to his agent, dummy, straw man or conduit.

Ad. Code §11-2108(b)(7).
A. **Nominee or agency agreement.**
   - The agreement must have been entered into prior to the transfer of the property to the nominee.
   - The agreement should identify the property and provide that the purpose of the agreement is to facilitate the acquisition of that property by the owner/principal.
   - The agreement should provide that the nominee is acting for and on behalf of the owner/principal.
   - The agreement should provide that the nominee must acquire, hold, dispose of and otherwise deal with the property solely as directed by the owner/principal.
   - The nominee should have no discretionary authority or responsibility for the property.
   - The owner/principal should indemnify the nominee for any losses, expenses or damages resulting from the nominee's actions under the agreement.
   - The agreement should terminate within one year after the acquisition of the property by the nominee and should provide that the property will be transferred to the owner/principal on termination of the agreement.

B. **Formation documents for nominee.** The organizational documents for the nominee must expressly provide that the nominee is being formed for the purpose of acquiring title to the property as a nominee for the owner/principal.

C. **Financing documents.** Documents relating to any financing provided by lenders in connection with the acquisition of the property by the nominee should acknowledge the beneficial ownership by the owner/principal. Any financing documents should provide that such financing is for the limited period of the syndication and that it will be repaid out of the proceeds of the syndication and/or any permanent financing following the transfer of the property from the nominee to the owner/principal.

D. **Syndication documents.** The syndication documents should describe the transaction, particularly the nominee arrangement, consistent with the provisions of the nominee or agency agreement and the characterization of the transaction as a “dummy/strawman” transaction.

E. **Other documents.** Any other documents executed in connection with the acquisition of the property and the syndication, such as the deed, the contract of sale or any assignment of the contract, should be consistent with the provisions in the nominee/agency agreement and the characterization of the transaction as a “dummy/strawman” transaction.

3. **Duration.** The nominee arrangement should be for a limited period of time. The transfer of the property from the nominee to the owner/principal should take place within one year after the acquisition by the nominee.
4. **Payment.** There should be no fee or other payment, other than a nominal amount not in excess of ten dollars, paid to the nominee for the conveyance of the property from the nominee to the owner/principal. The property should not be conveyed subject to any indebtedness.

If a taxpayer claims the “dummy/strawman” exemption for a transfer from a nominee to an owner/principal as part of a real estate syndication but the transfer **does not meet all of the above conditions**, for example, if some of the listed documents are not submitted or seem inconsistent with a nominee or agency arrangement, an auditor may not on his or her own accept the return as filed. Instead, the auditor will consult a supervisor who will review all of the facts and circumstances of the syndication and determine if the “dummy/strawman” exemption applies.
EXHIBIT K
Dear * * * *:

This is in response to your request for a ruling dated September 4, 2002 regarding the application of New York City Real Property Transfer Tax ("RPTT") to the conveyance of real property in connection with a "reverse" like-kind exchange under Internal Revenue Code ("IRC") section 1031. Additional information was received on October 30 and December 16, 2002 and January 7 and 13, 2003.

n1 For purposes of this ruling request, it is assumed that the transactions described below fall within the safe-harbor of Rev. Proc. 2000-37. The Department is not opinioning as to whether the transactions, do in fact, meet those requirements.

BACKGROUND

IRC section 1031 provides for nonrecognition of gain and loss on exchanges of like-kind properties. In a like-kind exchange, a taxpayer transfers one property (the "relinquished property") to a third party, and receives in exchange a like-kind property (the "replacement property"). In 2000, the Internal Revenue Service promulgated Revenue Procedure 2000-37, 2002-2 C.B. 308 (Sept. 18, 2000) ("Rev. Proc. 2000-37") setting forth criteria for a type of like-kind exchange, known as a "reverse exchange". In a reverse exchange, the taxpayer identifies and arranges for the acquisition of the replacement property by an accommodation titleholder before it has disposed of the relinquished property. To meet the requirements of Rev. Proc. 2000-37, the accommodation titleholder must have enough of the benefits and burdens of ownership with respect to the replacement property that the accommodation titleholder is treated as the owner for federal income tax purposes. The replacement property is then transferred either directly or indirectly through a qualified intermediary (as defined in Treas. Reg. 1.1031(k)-1(g)(4)) to the taxpayer. A qualified intermediary is a person who is not the taxpayer or a disqualified party (defined at Treas. Reg. § 1.1031(k)-1(k)) and who enters into a written agreement with the taxpayer (called the exchange agreement) under which the intermediary acquires the relinquished property from the taxpayer, transfers the relinquished property to a third party (the "Purchaser"), acquires the replacement property, and transfers the replacement property to the taxpayer. Treas. Reg. § 1.1031(k)-1(g)(4)(iii). The applicable Treasury Regulations provide that for the limited purposes of the like-kind exchange rules with respect to the relinquished property, the qualified intermediary is not considered the agent of the taxpayer. Treas. Reg. § 1.1031(k)-1(g)(4)(i).
FACTS

The facts presented are as follows:

Inc., an * * * * corporation ("Parent"), is in the business of serving as an accommodation titleholder for purposes of "reverse" like-kind exchanges under IRC section 1031. Parent intends to perform this service through one or more single member limited liability companies, each serving as an accommodation titleholder ("AT").

A sample reverse like-kind exchange within the scope of this ruling request would involve the transfer by the seller of the replacement property (the "Seller") of legal title to and federal tax ownership of the replacement property to the AT on day 1. Within 180 days thereafter:

(a) the AT would transfer federal tax ownership of the replacement property to the qualified intermediary (The qualified intermediary will be Corporation ("QI"), an entity related to the accommodation titleholder);
(b) the QI would transfer federal tax ownership of the replacement property to the taxpayer in exchange for the taxpayer's transfer of federal tax ownership of the relinquished property to the QI;
(c) the AT would convey legal title to the replacement property directly to the taxpayer;
(d) the QI would transfer federal tax ownership of the relinquished property to the Purchaser; and
(e) The taxpayer would convey title to the relinquished property directly to the Purchaser.

In support of your application for a letter ruling, you have submitted a sample Qualified Exchange Accommodation Agreement ("QEEA") intended to be used during the acquisition of the replacement property. The QEEA is designed and intended to be a QEEA as defined in Rev. Proc. 2000-37. Pursuant to Article 1.A of the QEEA, the AT will be assigned a contract for the acquisition of the replacement property pursuant to which it will acquire as quickly as practicable "qualified indicia of ownership" with respect to the replacement property. "Qualified indicia of ownership" are defined by the QEEA to mean (a) legal title, (b) other indicia of ownership that are treated as beneficial ownership under applicable principles of commercial law (e.g., a contract for deed), or (c) interests in an entity that is disregarded as an entity separate from its owner for federal income tax purposes (e.g., a single member limited liability company) and that holds either legal title to the property or such other indicia of ownership. QEEA, Art. 1.B. Pursuant to the QEEA, all funds needed to acquire the property are to be provided to the AT as one or more nonrecourse loans secured by the replacement property. QEEA, Art. 1.B.2. The AT will not be required or expected to advance or expend any of its own funds. Id. The QEEA requires that the AT and the taxpayer report the acquisition, holding and disposition of the replacement property as provided in Rev. Proc. 2000-37. The AT will be treated as the beneficial owner of all property that it holds pursuant to the QEEA for all federal income tax purposes and the taxpayer and the AT will report the federal income tax attributes of all property involved in the QEEA in a manner consistent with Rev. Proc. 2000-37. QEEA, Art. 2.C. In your letter dated December 13, 2002, you have also represented that the QEEA will be amended to specifically provide that the AT will receive only the fee set forth in Article 4D and reimbursement or indemnification in respect of costs and expenses incurred with respect to its legal ownership of the property and that the AT will transfer the property to the taxpayer at no profit or loss to the AT, other than the fee.

The QEEA provides further that the taxpayer is solely responsible for any and all activities, actions and decisions relating to the preservation and enhancement of the replacement property, including but not limited to, management, repairs, construction and payment of taxes, mortgage payments and similar items and the AT shall follow all reasonable written requests from the taxpayer and act as a conduit for payments and other matters. QEEA, Art. 3.A. Under the QEEA, the taxpayer wholly indemnifies the AT against any loss or liability arising directly or indirectly from the QEEA or the replacement property. QEEA, Art. 4.A. The taxpayer also indemnifies the AT and any related entities against any state and local taxes imposed or asserted with respect to the transactions, except that the AT will be solely responsible for all state and local taxes imposed on it with respect to the fees and interest income earned by the AT for its own account under the QEEA. QEEA, Art. 4.E. 1. To the extent any state and local taxes require the AT to conform to the federal income tax treatment of the transactions, the taxpayer must fully indemnify the AT and Parent for all state and local taxes incurred as result of the conformity. QEEA, Art. 4.E. 2. Article 6.S of the QEEA provides that the AT is acting solely as the taxpayer's agent for all purposes except for federal income tax purposes.

In accordance with Rev. Proc. 2000-37, within 180 days after the transfer of the "qualified indicia of ownership" of the replacement property to the AT, the replacement property will be transferred to the taxpayer through the QI. QEEA, Art. 2.D.
If for any reason, the AT is holding the "qualified indicia of ownership" of the replacement property at the end of the 180 day period, the AT shall have the immediate right to require the taxpayer to purchase the property (the "Put") and the taxpayer shall have the immediate right to require the AT to sell the property (the "Call"). However, pursuant to Rev. Proc. 2000-37, the Put and Call will not be effective for a period in excess of 185 days from the date on which the qualified indicia of ownership were acquired by the AT. QEAA, Art. 4.B. Attached to the QEAA will be a lease (the "Lease") executed contemporaneously with the QEAA, with the AT as lessor and the taxpayer as lessee with respect to the replacement property during the time that the AT is holding the property. QEAA, Art. 4C. The Lease is a net lease with the amount of the rent equal to the outstanding monthly obligation on the note and the mortgage on the property, payable in arrears. Lease §§ 3.1 and 3.2. As “additional rent”, the taxpayer is also responsible for all taxes, fees and other charges, including all utilities with respect to the property. Lease § 4. Under the Lease, the taxpayer has the right to construct any improvements on the leased premises without the consent of or notice to the AT. Lease § 5.1. You also have submitted a sample flow chart demonstrating that the AT’s cash flow with respect to the replacement property is designed to be a wash with the income equaling the expenses.

You have submitted a sample Exchange Agreement ("Exchange Agreement") in support of your application, subject to the modifications to Article 2D as proposed in your letter dated January 10, 2003. Under the Exchange Agreement, the relinquished property will be transferred from the taxpayer to the QI subject to the relinquished property contract between the taxpayer and the Purchaser of the relinquished property. Exchange Agreement, Art. 1A. You have represented that the Exchange Agreement will provide that the taxpayer will assign its rights (but not its obligations) under the QEAA with respect to the acquisition of the replacement property to the QI. The QI will be indemnified for any costs associated with the implementation of the Exchange Agreement. Exchange Agreement, Art. 5. The Exchange Agreement specifically provides that the QI is not liable for the debts or obligations of the taxpayer as a result of the provisions of the Exchange Agreement and the QI is acting solely as the taxpayer's agent for all purposes, except for federal and, as appropriate, state income tax purposes. Exchange Agreement, Art. 7F. In your letter dated January 10, 2003, you have represented that in the reverse exchange, the only profit derived by the QI is the Exchanger Fee prescribed under Article 21 of the Exchange Agreement.

ISSUES

You have requested the following rulings:

1. The transfer of the replacement property to the taxpayer from the Seller of the replacement property pursuant to the Exchange Agreement and the QEAA constitutes a single transfer of that property and is subject to the RPTT only once.
2. The transfer of the replacement property by the AT to the QI for the purpose of completing the Section 1031 exchange is not subject to the RPTT.
3. The transfer of the relinquished property by the taxpayer to the Purchaser of that property in accordance with the terms of Exchange Agreement constitutes a single transfer of that property and is subject to the RPTT only once.

DISCUSSION

In general the RPTT is imposed on each deed at the time of delivery by a grantor to a grantee when consideration for the real property and any improvement thereon exceeds $ 25,000. § 11-2102.a of the Administrative Code of the City of New York (the "Code"). The RPTT does not apply to a deed, instrument, or transaction conveying real property from a principal to an agent or a deed, instrument, or transaction conveying real property from an agent to a principal. Code § 11-2106.b(7).

Pursuant to Title 19 of the Rules of the City of New York section 23-05(b)(7)(i), a conveyance between a principal and an agent is exempt from tax provided:

. a written agreement is entered into at the time of the transaction establishing such a relationship with respect to the reality or economic interest therein,
. the purported agent functions as an agent with respect to the reality or economic interest therein for all purposes, and
the purported agent is held out as the agent and not the principal in all dealings with third parties relating to the realty or economic interest therein.

In re Goldman, Sachs & Co. v. Michael, 113 A.D.2d 326, 330 (1st Dept. 1985), the court stated that a transfer qualified for the exemption when "there was [a] prior agreement that the agent-entity would be created for a limited period and would serve a definite stated purpose and where the agent purchased the transferred property with funds provided by the principal".

Section 4.02(5) of Rev. Proc. 2000-37 requires that no later than 180 days after the transfer of qualified indicia of ownership to the accommodation titleholder the property must be transferred either directly or indirectly through a qualified intermediary to the taxpayer as replacement property; or (b) the property must be transferred to a person who is not the taxpayer or a disqualified person as relinquished property. Treas. Reg. section 1.1031(k)-1(g)(4) provides that in the case of a taxpayer's transfer of relinquished property involving a qualified intermediary, the qualified intermediary is not considered the agent of the taxpayer for the limited purposes of IRC section 1031(a). Under section 4.02(6) of Rev. Proc. 2000-37, the combined time period that the relinquished property and the replacement property are held in a "qualified exchange accommodation arrangement" may not exceed 180 days.

Notwithstanding the requirements of Rev. Proc. 2000-37, you argue that for purposes of the RPTT, the substance of the transaction is a single transfer of the replacement property from the seller to the taxpayer, with the AT and QI acting as the taxpayer's agents, and a single transfer of the relinquished property, with the QI functioning as the taxpayer's agent. Therefore, you contend, based on the substance of the transactions, the RPTT should be due only once on the transfer of the replacement property to the taxpayer and the RPTT should be due only once on the transfer of the relinquished property to the Purchaser.


The "exchange" requirement poses an analytical problem because it runs head-long into the familiar tax maxim that the substance of a transaction controls over form. In a sense, the substance of a transaction in which the taxpayer sells property and immediately reinvests the proceeds in like-kind property is not much different from the substance of a transaction in which two parcels are exchanged without cash... Yet, if the exchange requirement is to have any significance at all, the perhaps formalistic difference between the two types of transactions, must, at least on occasion, engender different results... (citations omitted.)

Where the taxpayer seeks to avoid the form of his own agreement, a higher level of proof, known as "the strong proof standard" is required. Coleman v. Commissioner, 87 T.C. 178, 201-203 (1986), aff'd, per curiam, 833 F.2d 303 (3rd Cir. 1987).

Recognizing that the form of the transaction in this case is particularly important for federal income tax purposes does not preclude an analysis of the substance of the transaction for purposes of applying the RPTT. Under general tax principles, the determination of ownership of an asset for tax purposes is to be based on an analysis of many different factors indicative of ownership, not always on the bare legal title. Bailey v. CIR., 912 F. 2d 44, 47 (2nd Cir. 1990). See, e.g., Helvering v. Clifford, 309 U.S. 331 (1940); Helvering v. F.& R. Lazarus Co., 308 U.S. 252 (1939). "Taxation is not so much concerned with the refinements of title as it is with actual command over the property taxed--the actual benefit for which the tax is paid." Corliss v. Bowers, 281 U.S. 376, 378 (1930).

In this case, in addition to holding legal title to the replacement property prior to its transfer to the taxpayer, the AT will also be reporting the income and expenses with respect to the property for federal income tax purposes. This federal tax treatment would normally indicate that the AT is the owner of the property. However, other factors militate strongly in
favor a determination that, for purposes of the RPTT, the AT is an agent of the taxpayer with respect to the property. For instance, the cash flow that the AT will be receiving as a result of the transaction is designed to be a wash, with the income equaling the expenses. Furthermore, the taxpayer will have provided the funds to purchase the replacement property and will have indemnified the AT for all possible expenses associated with the property. You have also represented that the QEAA will be amended to specifically provide that the AT will receive only the fee set forth in Article 4D and reimbursement or indemnification in respect of costs and expenses incurred with respect to its legal ownership of the property and that the AT will transfer the property to the taxpayer at no profit or loss to the AT, other than the fee. The Lease between the taxpayer and the AT is a net lease with the amount of the rent equal to the payments due on the note and mortgage secured by the property. Thus, the AT cannot profit or lose from the Lease. Furthermore, under the Lease, the taxpayer has the right to construct any improvements on the leased premises without the consent of or notice to the AT. The QEAA provides that the taxpayer is solely responsible for any and all activities, actions and decisions relating to the preservation and enhancement of the replacement property, including but not limited to, management, repairs, construction and payment of taxes, mortgage payments and similar items and the AT shall follow all reasonable written requests from the taxpayer and act as a conduit for payments and similar items.

The AT also will be holding the property for a limited time period. It is intended that the AT hold the replacement property for no more than 180 days. If at the end of 180 days, the AT is still holding the qualified indicia of ownership, the Put and Call will operate to terminate the AT’s involvement with the property. Finally, Article 6.S of the QEAA provides that the AT is acting solely as taxpayer’s agent for all purposes except for federal income tax purposes.

Based on all the facts, including the fact that the transaction was intended to meet the formalistic requirements of Rev. Proc. 2000-37, we have concluded that the AT is holding the replacement property as an agent for the taxpayer. Thus, only one RPTT will be due upon the transfer of the replacement property from the seller to the AT. The transfer of legal title to the replacement property from the AT to the QI and from the QI to the taxpayer will be exempt from the RPTT as transfers between agents and their principal.

Once the AT has acquired the replacement property, it will hold the property until the exchange for the relinquished property is effected. Prior to transferring legal title to the replacement property to the taxpayer, the AT will transfer federal tax ownership of the replacement property to the QI. The QI will hold the federal tax ownership for a brief time and then transfer it to the taxpayer. The QI will be completely indemnified for all costs associated with holding the replacement property. Article 7F or the Exchange Agreement provides that the QI is acting solely as the taxpayer’s agent for all purposes, except for federal and as, appropriate, state income tax purposes. You have represented that the only profit that the QI will derive from the transactions is the Exchanger Fee. Because of the brief time and limited purpose that the QI will be holding the replacement property and the fact that the transaction is intended to meet the criteria of Rev. Proc. 2000-37, we have determined that the QI also is functioning as the taxpayer’s agent for purposes of the RPTT. Consequently, any transfer of interests in the replacement property to the QI from the AT and from the QI to the taxpayer will not be subject to the RPTT. Similarly, the transfer to and the holding by the QI of the federal tax ownership of the relinquished property prior to its transfer to the Purchaser is of a limited purpose and duration and solely for the purpose of fulfilling the requirements of Rev. Proc. 2000-37.

Based on these facts, the transfer of these interests from the taxpayer to the QI will be exempt from the RPTT as a transfer from a principal to an agent.

The Department reserves the right to verify the facts submitted.

**Legal Topics:**

For related research and practice materials, see the following legal topics:
- Real Property Law
- Purchase & Sale
- Like-Kind Exchanges
- Tax Law
- Federal Income Tax
- Computation
- Sales & Exchanges
- Like-Kind Exchanges (IRC sec. 1031)
- Nonrecognition of Gains & Losses
- Tax Law
- Federal Income Tax Computation
- Sales & Exchanges
- Like-Kind Exchanges (IRC sec. 1031)
- Requirements
EXHIBIT L
8 of 69 DOCUMENTS

Re: Real Property Transfer Tax

FINANCE LETTER RULING 99

CITY OF NEW YORK-DEPARTMENT OF FINANCE

1999 N.Y. City Tax LEXIS 21; FLR 99-4745

[NO HEADING IN ORIGINAL]

June 30, 1999

Dear * * *

This letter is in response to your request, dated * * *, for a ruling regarding the application of the New York City Real Property Transfer Tax ("RPTT") to the transactions described below. Additional information was received on * * *.

FACTS

The facts presented are as follows:

The Taxpayer is a limited liability company ("Taxpayer") which has three members: * * * (the "unit owners").

The Taxpayer was recently designated by the * * * Corporation to develop the * * * site, located on * * * between * * * and * * *, New York, New York, Block * * *, Lot * * * (the "Project").

The Project will consist of three components: commercial/retail space, a senior housing facility, and a university faculty residence (the "Units"). The intention is that each member of the Taxpayer will own one of the units upon completion of the Project. However, because the Units will be physically and structurally integrated, it is necessary to develop the Project as a condominium regime. Due to restrictions imposed by the New York Condominium Act, the ownership of the property cannot be severed and each unit transferred to its owner prior to the substantial completion of all improvements. Therefore, the Taxpayer will take title to the property to facilitate the construction. Upon completion of the Project, the Taxpayer will submit the Property to the condominium regime and convey the three Units to their respective unit owners.

Each Unit Owner will separately fund the construction, development and improvement of its respective Unit. The Taxpayer's operating agreement separates the benefits and obligations regarding the Project from the outset, so that Each Unit Owner receives all benefits and bears all obligations of its own Unit, and has no beneficial interest in, or obligations with respect to, the other Units. Prior to conversion, all allocations of profit and loss, all cash distributions, and all capital contributions attributable to each Unit will be allocated to its respective Unit Owner, and each Unit Owner will have sole design discretion with respect to its Unit.

Further, the condominium declaration will provide that the Taxpayer is making the submission for the benefit of the three Unit Owners, and in effect will be acting in the capacity of a nominee, holding the property for the benefit of the three Unit Owners.

ISSUE
You have requested a ruling as to whether the conveyance of the units upon completion of the Project to their respective owners will be exempt from the RPTT.

CONCLUSIONS

Based on the facts presented and the representations submitted, we have determined that the conveyance is exempt under Code section 11-2106.7 of the Administrative Code of the City of New York (the "Code") as a transfer of real property from a conduit to its principal.

DISCUSSION

Code section 11-2102.b imposes a tax on the transfer of real property or an economic interest in real property when the consideration exceeds $25,000. However, Code section 11-2106 (b) (7) provides an exemption from the RPTT for conveyances "from a person acting as a mere agent, dummy, straw or conduit to his principal, or from the principal to such a person. . ."

In this instance, under the Taxpayer's Operating Agreement, the Taxpayer will purchase the property for the benefit of the Unit Owners with funds provided by them as capital contributions. The interest of each Unit Owner is limited to its interest in its Unit and the common areas adjacent thereto. The Taxpayer will then apply the Unit Owners' contributions to upgrade the Unit, submit a condominium declaration upon completion of the upgrade, and transfer the Units following approval by the Real Property Assessment Bureau. Finally, the Taxpayer will pay the transfer tax upon acquisition of the property, which will be allocated among the Unit Owners in the same proportion as their capital contributions. In sum, the Taxpayer will never derive any benefit from the property, nor incur any detriment. It will be acting merely as a conduit.

Based upon the facts and representations submitted we have determined that the distribution by the Taxpayer of the units upon completion of the Project to the respective unit owners will be exempt from RPTT as a transfer of real property from a conduit to its principal.

The Department of Finance reserves the right to verify the information submitted.

Legal Topics:

For related research and practice materials, see the following legal topics:
Real Property LawCommon Interest CommunitiesCondominiumsPurchase & SaleReal Property LawOwnership & TransferDeath & IncapacityTestamentary DispositionsTax LawState & Local TaxesReal Property TaxAssessment & ValuationGeneral Overview
Transfer Taxes
Who Owes What and How Much

Wayne Berkowitz, Esq. is both an attorney and an accountant and is a partner in Berdon LLP’s tax department. He heads the firm’s State and Local Tax Group, advising on the unique requirements of governments and municipalities across the nation, including realty transfer taxes in New York City and New York State.

Dealing with the ever-increasing complexity of state and local tax requirements, Mr. Berkowitz is a recognized expert in this challenging area. He advises a wide range of clients in an array of industries — including real estate — planning their tax strategies, assisting them in resolving controversies, and representing them in tax audits. As Berdon’s leader in directing state and local tax projects, Mr. Berkowitz monitors tax law in multiple states to anticipate and prepare for changes to ensure compliance and identify money saving opportunities. Mr. Berkowitz serves on a number of state accounting society and bar association committees. In this capacity, he is influential in state and local tax reform; analyzes the impact of new and proposed laws; and has helped develop ideas for new legislation. He has served on the New York City Commissioner’s Advisory Panel and has been a member of the state advisory panel.

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Sean Kanousis, Esq. is both an attorney and an accountant and is a principal in Berdon LLP’s State and Local Tax Group. In that role he stays on top of state and local tax law developments across all 50 states to help clients anticipate and prepare for change, realize tax credits, and stay compliant with constantly evolving regulations. Mr. Kanousis consults in all areas of state and local taxation including income and franchise taxes, as well as significant indirect taxes such as sales and use and realty transfer taxes. He has extensive experience advising clients on realty transfer taxes in New York City and New York State as well as across the country. Mr. Kanousis frequently consults on state and local tax law developments impacting real estate firms, REITs, and professional service firms, among others — identifying opportunities to ensure compliance and enhance bottom lines. Prior to joining Berdon, he served at a real estate and financial CPA firm where he was instrumental in establishing their state and local tax group.

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