STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
BELHARA ASSOCIATES LIMITED PARTNERSHIP for Revision of a Determination or for Refund of Taxes on Gains Derived from Certain Real Property Transfers under Article 31-B of the Tax Law.	:	DECISION DTA No. 809542

Petitioner Belhara Associates Limited Partnership, c/o Parkview Associates, Inc., 708 Third Avenue, New York, New York 10017, filed an exception to the determination of the Administrative Law Judge issued on March 10, 1994. Petitioner appeared by Margolin, Winer and Evens (James L. Tenzer, Esq., of counsel). The Division of Taxation appeared by William F. Collins, Esq. (Andrew J. Zalewski, Esq., of counsel).

Petitioner filed a brief in support of its exception. The Division of Taxation resubmitted its hearing brief in opposition. Petitioner's reply letter brief was received on June 29, 1994, which date began the six-month period for the issuance of this decision. Neither party requested oral argument.

The Tax Appeals Tribunal renders the following decision per curiam.

ISSUES

I. Whether the Division of Taxation erroneously calculated the "original purchase price" of the property transferred by petitioner to the cooperative housing cooperation when it refused to "step-up" petitioner's acquisition cost to the fair market value of the property on the date of transfer.

II. Whether a purchase money mortgage received by petitioner at the time of closing should have been excluded from the calculation of consideration on the ground that the sales

contract between petitioner and the cooperative housing corporation was executed before the effective date of article 31-B.

III. Whether the Division of Taxation's refusal to step up petitioner's original purchase price to fair market value and its inclusion of the purchase money mortgage in consideration violate petitioner's constitutional right to equal protection of the law.

IV. Whether petitioner should be allowed to include in original purchase price certain expenses it describes as "conversion period interest" and "conversion period real property taxes."

V. Whether the Division of Taxation properly computed the taxable gain on petitioner's transfer of cooperative units.

VI. Whether the Division of Taxation properly computed interest on the asserted deficiency.

VII. Whether petitioner demonstrated reasonable cause to abate penalties imposed under Tax Law § 1446.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge except for findings of fact "6," "7," "8," "10," "11," "12," "14," "15," "16," "17" and "18" which have been modified. The Administrative Law Judge's findings of fact and the modified findings of fact are set forth below.

The Division of Taxation ("Division") issued to petitioner, Belhara Associates Limited Partnership ("Belhara"), a Notice of Determination dated March 3, 1989, assessing real property gains tax for the period ended October 1, 1984 of $53,782.00 plus interest. No penalties were imposed on the tax due. The notice also assessed tax for the period ended February 8, 1986 of $4,681.00 plus penalty and interest.

Belhara was the sponsor of a plan to convert the premises located at 350 East 77th Street, New York, New York to cooperative ownership. On June 15, 1982, Belhara entered into an

Agreement of Sale to acquire all of the partnership interests of 350 East 77th Street Associates, a general partnership. The principal asset of 350 East 77th Street Associates was the real property located at 350 East 77th Street. Paragraph 2 of the Agreement of Sale states: "Sellers hereby agree to sell to Buyer and Buyer hereby agrees to purchase from Sellers all of the Partnership Interests on the Closing Date for an aggregate purchase price of $3,048,000.00."

Also on June 15, 1982, Belhara entered into a contract for the sale of 350 East 77th Street to 350 East 77th Street Corporation, a cooperative housing corporation. The contract of sale contains the following provisions:

> "3. (a) The consideration to be paid by Buyer to Seller is as follows:
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> "(i) an amount equal to the aggregate cash proceeds obtained by the Buyer through the sale of its shares under the Plan, less $50,000, the Working Capital Fund to be retained by the Seller (increased or decreased by closing adjustments) as set forth in paragraph 7;
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> "(ii) an amount equal to any money forfeited by defaulting subscribers under the Plan;
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> "(iii) an amount equal to the sum of $1,100,000, to be paid by Buyer executing and delivering to Seller a Purchase Money Note in the amount which shall be secured by the Purchase Money Mortgage as described in Section L of the Plan.
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> "(b) In addition to the net cash proceeds to be paid to Seller by Buyer pursuant to subparagraph (a), Buyer shall transfer to Seller the Following:
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> (i) the shares of the Buyer allocated to apartments under the Plan which have not been purchased or paid for as of the Closing Date under the Plan, which shares shall be duly issued to Seller or Seller's designee(s), and the proprietary leases appurtenant thereto;
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> (ii) by Buyer taking title subject to the wraparound mortgage to be in effect on the Closing Date as described in Section L of the Plan, in the amounts then outstanding on the closing Date."

In October 1982, 350 East 77th Street Corporation submitted a cooperative conversion plan to the office of the Attorney General. The original Cooperative Offering Plan (the "Plan") called for the sale of 84 units by transfer of 14,909 shares of stock. As amended the final Plan called for the sale of 86 units by the transfer of 15,334 shares of stock. The Plan was approved and declared effective as of January 11, 1984.

On or about March 15, 1984, Belhara transferred its partnership interests in 350 East 77th Street Associates to 350 East 77th Street Corporation. The purchase price paid to Belhara by the cooperative housing corporation, included the following:

> "(a) the aggregate cash proceeds obtained by the Apartment Corporation in connection with the sale of its shares to individual purchasers as of March 15, 1984 pursuant to individual subscription agreements (5,701 shares sold for a total of $1,054,535) less the $287,500 working capital fund retained at the closing by the Apartment Corporation (the "Working Capital Fund"), and less additional offering expenses incurred in connection with the sales and closing (including printing and advertising expenses, professional and legal fees, offering plan registration fees, broker's fees, gains tax and transfer tax expenses, marketing fees and title expenses), as provided for in the Contract of Exchange between Sponsor and Apartment Corporation dated as of June 15, 1982 and as amended by Supplemental Agreement dated as of March 15, 1984 (the "Contract") and
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> "(b) the Unsold Shares (9,633 shares valued at $1,733,940) and their appurtenant proprietary leases; and
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> "(c) the Apartment Corporation taking subject to a purchase money mortgage on the closing date with Sponsor in the principal amount of $1,100,000 ('the Mortgage')."

The Division submitted in evidence a set of transferor and transferee questionnaires filed by Belhara and 350 East 77th Street Corporation upon the transfer of the real property by Belhara to the cooperative housing corporation and a second transferor questionnaire filed by Belhara. The date of filing of these questionnaires is not known, but it is assumed that they were timely filed as there is no evidence in the record to the contrary. Belhara's transferor questionnaire included sales of cooperative units made under purchase agreements signed through January 29, 1984.

We modify the Administrative Law Judge's finding of fact "6" to read as follows:

> Attached to Belhara's transferor questionnaire were a number of schedules (denominated by Belhara as Exhibits A through I), showing the method used by Belhara to calculate the gain subject to tax, using the Option B method of filing to calculate tax due.[1] Gross consideration as

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[1] Prior to approximately August of 1986, the Division had allowed two acceptable methods of calculating gains tax liability upon transfers of cooperative apartment units. These two methods, known as Option A and Option B, may summarily be described as follows:

> Option A: Gain is computed based upon the actual consideration received on each unit transfer less the amount of total original purchase price apportioned to each such unit

reported by Belhara consisted of (1) the total "anticipated cash portion of purchase price for shares" (Exhibit F) in the amount of $3,333,855.00 plus the amount of the purchase money mortgage, $1,100,000.00, yielding gross consideration of $4,433,855.00.[2]

We modify the Administrative Law Judge's finding of fact "7" to read as follows:

Belhara calculated the purchase price paid to acquire the property as follows:

PURCHASE PRICE PAID TO ACQUIRE REAL PROPERTY:	
Acquisition Price	$ 3,048,000
Mortgage Costs and Fees	17,143
Attorneys' Fees	36,046
Title Costs and Fees	15,000
Filing and Registration Fees	6,784
Appraisal, Etc. Fees	3,000
Real Property Transfer Tax	60,960
Mortgage Recording Tax	24,750
Total Purchase Price	$ 3,211,683[3]

(including actual brokerage fees, advertising expenses, vacancy preparation costs and other selling expenses incurred). An update of the figures was required on four specific occasions (being respectively when 25%, 50%, 75% and 100% of the units had been transferred), or more frequently if requested by the Division.

Option B: Gain is computed based upon the total anticipated (i.e., actual plus estimated future) consideration as apportioned to each unit less the total (i.e., actual plus estimated future) original purchase price apportioned to each unit. This method essentially allowed an apportionment of anticipated gain to each unit. Updates were required at the same sellout plateaus (or more frequently upon Division request) as for Option A.

Commencing in or about August of 1986, the Division eliminated Option A as an acceptable method of calculation. In addition, new filing procedures were established whereunder standards were set for estimating anticipated consideration under a cooperative conversion plan. These standards for estimation, when applied, would result in a so-called "safe harbor" estimate of anticipated consideration and treatment as though the transferor's estimate of consideration exactly equalled the actual consideration ultimately received. In ultimate effect, compliance with the "safe harbor" method would avoid imposition of penalty and interest on any underpayment of gains tax on unit transfers (to the extent such underpayment represented the excess of actual consideration over the safe harbor estimate of consideration). This August 1986 change resulted, in essence, in the only acceptable method of computation being a modified Option B computation including guidelines for computing the safe harbor amounts. Updating was optional at the 25% plateau, and was required at the 50%, 75% and 100% plateaus (see generally, TSB-M-83-[2]-R, TSB-M-86-[2]-R and TSB-M-86-[3]-R).

[2] We modify finding of fact "6" of the Administrative Law Judge's determination by changing the reference from Exhibit "D" to Exhibit "F" to more accurately reflect the record.

[3] We modify finding of fact "7" of the Administrative Law Judge's determination by changing the phrase "original purchase price of the property" to read "purchase price paid to acquire the property" to reflect the record in greater

We modify the Administrative Law Judge's finding of fact "8" to read as follows:

> Belhara attached to the questionnaire a statement of brokerage fees "anticipated under the plan" amounting to $200,031.00. This was signed by Martin J. Raynes, the president of the brokerage firm acting as selling agent for the cooperative housing corporation. MR Gold Associates Limited Partnership and Parkview Belhara Associates Limited Partnership are the general partners of Belhara. Mr. Raynes is a general partner of MR Gold Associates Limited Partnership.[4]

Belhara calculated the total anticipated gain subject to tax as follows:

Gross Consideration	$4,433,855.00	
Brokerage fees	(200,031.00)	
Total consideration		4,233,031.00
Purchase price to acquire	3,211,683.00	
Capital improvements	476,907.00	
Original purchase price		(3,688,590.00)
Gain subject to tax		$ 545,234.00

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

> Exhibit A of Belhara's filing reported the transfer of 46 units as of the date the questionnaire was filed (on or about March 15, 1984) and that six of such units (the "grandfathered units") were transferred pursuant to binding agreements executed before March 28, 1983, the effective date of the gains tax law. Belhara apportioned the total consideration and purchase price to each of the 46 units based on a formula which it described as follows:
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> "The method of apportionment utilizing a fixed common denominator is based upon fair market value (FMV).
>
> "FMV is based upon the actual sales prices of units for which purchase agreements have been executed and accepted and current prices for unsold units.
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> "The . . . FMV factors for each individual unit [are] based upon a fraction the numerator of which is the FMV

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detail.

[4] We modify finding of fact "8" of the Administrative Law Judge's determination by deleting the last sentence of said finding of fact which stated "Mr. Raynes was also a general partner of Belhara," and by adding the last two sentences to the modified finding of fact to more accurately reflect the record.

> of such unit and the fixed common denominator of which is the aggregate FMV of all the units."[5]

We modify the Administrative Law Judge's finding of fact "11" to read as follows:

> The calculation described above yielded what Belhara described as a "percentage of interest" for each unit. The total percentage of interest of all units sold as of the initial filing (excluding the grandfathered units) was .376861. The application of this figure yielded the following computation of gains tax due on units sold as of the date the questionnaire was filed (i.e., on or about March 15, 1984):

Gross consideration to transferor	$ 1,670,947.00
Brokerage fees	(75,384.00)
Consideration	1,595,563.00
Original purchase price	(1,390,086.00)
Gain subject to tax	205,477.00
Anticipated tax due	20,548.00[6]

We modify the Administrative Law Judge's finding of fact "12" to read as follows:

> Exhibit "H" attached to Belhara's gains tax questionnaire sets forth Belhara's estimate of the fair market value of each of the 86 units located at the property, with the total fair market value of all 86 units shown as $3,333,855.00. Of the 46 units that were reported as transferred on the questionnaire, 45 were listed on Exhibit "H" at a price of $180.00 per share, the price to tenants as established by the Fourth Amendment to the Offering Plan. The 46th unit, Apartment 3B, was listed at a price of $428.728 per share. These 46 units represented

7,975 shares of stock. The remaining 40 unsold units, representing 7,359 shares, were valued at $254.1106 per share to determine the fair market value per unit as shown on Exhibit "H" of the questionnaire. Consideration for the 46 transferred units totaled $1,463,855.00 and when added to the estimated fair market value of the unsold units of $1,870,000.00 (7,359 shares x $254.1106 per share) resulted in total anticipated consideration on the sale of the 86 units of

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[5] We modify finding of fact "10" of the Administrative Law Judge's determination by deleting the first two sentences of such finding of fact which indicated that the 46 units were transferred through the end of January 1984 and that the six grandfathered units were transferred before March 28, 1983, and by substituting the first sentence of the modified finding of fact to more accurately reflect the record.

[6] We modify finding of fact "11" of the Administrative Law Judge's determination by changing the third sentence which read "[t]he application of this figure yielded the following computation of gains tax due on units sold as of the end of January 1984:" to reflect that the initial 46 units were transferred on or about March 15, 1984 and not as of the end of January 1984.

$3,333,855.00. Belhara did not offer the basis for its estimate of the fair market value of $254.1106 per share for the unsold units.[7]

The Division began an audit of the cooperative conversion in February 1987. The audit was completed in about September of 1988. Based on the records made available to it by Belhara's representatives, the Division calculated the original purchase price of the property as follows:

Cost to acquire real property		$3,048,000.00
Other acquisition costs:		
Legal fees	33,906.00	
End loan commitment	17,143.00	
sub-total		51,049.00
Capital improvements:		
Accounting fees	16,970.00	
Developer's fees	42,286.00	
Engineer	3,013.00	
Renovations (through 1986)	14,139.00	
sub-total		76,408.00
Conversion costs		
Legal fees	60,545.00	
Filing fees	6,790.00	
Printing	11,655.00	
sub-total		78,990.00
Original Purchase Price		$3,254,447.00

We modify the Administrative Law Judge's finding of fact "14" to read as follows:

> The Division determined that there were 86 units in the cooperative conversion plan and 15,344 shares of stock attributable to all units. When the Division commenced its audit of Belhara in February 1987, all shares of the cooperative housing corporation had been transferred. On audit, the Division determined that 7,744 shares, representing 45 units, were transferred by April 10, 1984 at a purchase

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[7] The Administrative Law Judge's finding of fact "12" read as follows:

> "Belhara did not offer the basis for its estimate of the fair market value of each unit. However, it is noted that the Fifth Amendment to the Plan lists the units sold as of the Plan's effective date. The actual purchase prices of those units, 31 in all, correspond to the fair market value of the same units as shown in Exhibit "H" of Belhara's filing. On the other hand, the purchase prices shown in the original Plan are consistently higher than the fair market values estimated by Belhara. For example, Unit number 6H is shown in the offering plan with a purchase price to rent controlled tenants of $38,200.00 and to nontenants of $87,860.00. The fair market value of 6H was estimated as $34,380.00. Unit 6H is not one of those sold as of the Fifth Amendment to the Plan."

We have modified said finding of fact to reflect the record in greater detail.

price of $1,422,275.00 (these are the same units that were reported as transferred by Belhara on its questionnaire filed on or about March 15, 1984). It was also found that on December 28, 1984, a bulk transfer of 7,165 shares was made to an investor. The purchase price for the bulk transfer was $2,589,925.00 and this sale was apparently made on an installment basis. On February 8, 1986, the 425 shares representing the last two units of the project, Apartments GR-1 and GR-2, were sold for $76,500.00. The consideration for all units was determined to be $4,088,700.00 ($1,422,275.00 and $2,589,925.00 and $76,500.00). The six grandfathered units represented 955 shares of stock, or 6.4888 percent of the total shares. Consideration received on these units was determined to be $207,455.00; thus, the total consideration from the sale of cooperative units subject to gains tax was determined to be $3,881,245.00 ($4,088,700.00 - $207,455.00). The Division added to this $1,028,623.00, representing the purchase money mortgage received by Belhara, adjusted to reflect the amount of the mortgage apportioned to the grandfathered units. This yielded gross consideration on taxable units of $4,909,868.00, an amount that was then reduced by $2,274.00 representing lost rents. Total gross consideration on taxable units was thus determined to be $4,907,594.00 (compared to petitioner's estimate of $4,157,951.00 [$4,433,855.00 - $275,904.00] as reported on Exhibit "A" of its questionnaire).

The Division reduced the gross consideration on the taxable units by brokerage fees in the amount of $16,238.00 and a capital reserve fund of $268,845.00 (again, adjustments were made to account for the pre-gains tax units), resulting in net consideration on taxable units of $4,622,511.00. The original purchase price of $3,254,447.00 (see above) was adjusted to reflect the transfer of units not subject to gains tax, resulting in an original purchaseprice of $3,043,272.00. The original purchase price was subtracted from net consideration on taxable units to calculate gain subject to the gains tax of $1,579,239.00 and anticipated tax of $157,924.00. The tax was divided by total number of shares subject to gains tax to calculate tax per share of $11.0136.[8]

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[8] The Administrative Law Judge's finding of fact "14" read as follows:

We modify the Administrative Law Judge's finding of fact "15" to read as follows:

> The total number of shares applicable to taxable units sold through the period ended October 1, 1984 was determined to be 6,749 (44% of the total shares), with a tax due on the transfers of $74,330.00 based on tax of $11.0136 per share. Tax paid by Belhara as shown on its questionnaire was subtracted from tax due to determine additional tax due for the period ended October 1, 1984 of $53,782.00. The Division determined that an additional 425 shares of stock were sold as of February 8, 1986, with a tax due on these transfers of $4,681.00 plus penalty and interest calculated from February 8, 1986. The Division issued to Belhara a Statement of Proposed Audit Adjustment dated August 19, 1988, showing this determination of tax due.[9]

We modify finding of fact "16" of the Administrative Law Judge's determination to read as

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> "The Division determined that there were 86 units in the cooperative conversion plan and 15,344 shares of stock attributable to all units. The total anticipated consideration for all units was determined to be $4,088,700.00. The basis for this figure is not clear from the record. It was apparently based on a review of Belhara's own records; however, there are no documents in the record showing exactly which records were reviewed, although there is evidence that the auditor reviewed records provided by Belhara's representative. A worksheet submitted by the Division shows the sale of 47 units subject to gains tax through the period ended February 8, 1986 at a total purchase price of $1,498,775.00. The price for each unit corresponds to the fair market values and prices shown in Belhara's transferor questionnaire. The anticipated consideration for 7,165 unsold shares is shown as $2,589,992.00, but the basis for this figure is unknown. The six grandfathered units represented 955 shares of stock, or 6.4888 percent of the total shares. Consideration received on these units was determined to be $207,455.00; thus, the total anticipated consideration from the sale of cooperative units subject to gains tax was determined to be $3,881,245.00 (compared to petitioner's estimate of $3,333,855.00 based on the fair market values). The Division added to this $1,028,623.00, representing the purchase money mortgage received by Belhara, adjusted to reflect the amount of the mortgage apportioned to the grandfathered units. This yielded gross consideration of $4,909,868.00, an amount that was then reduced by $2,274.00 representing lost rents. Total gross consideration was thus determined to be $4,907,594.00.
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> "The Division reduced the gross consideration by brokerage fees in the amount of $16,238.00 and a capital reserve fund of $268,845.00 (again, adjustments were made to account for the pre-gains tax units), resulting in net consideration of $4,622,511.00. The original purchase price of $3,254,447.00 (Finding of Fact "13") was adjusted to reflect the transfer of units not subject to gains tax, resulting in an original purchase price of $3,043,272.00. The original purchase price was subtracted from net consideration to calculate gain subject to the gains tax of $1,579,239.00 and anticipated tax of $157,924.00. The tax was divided by total number of shares subject to gains tax to calculate tax per share of $11.0136."

We have modified said finding of fact to reflect the record in greater detail.

[9] We modify finding of fact "15" of the Administrative Law Judge's determination by adding the words "applicable to taxable units" in the first sentence and the words "as shown on its questionnaire" in the second sentence to reflect the fact that the 6,749 shares applied to the taxable units sold and to also reflect that the tax paid by Belhara was the amount as reported on its questionnaire.

follows:

> An audit summary prepared by the Division contains the following statement: "Taxpayer requested that the tax be paid in installments. See AU200 attached." A handwritten statement which appears in the same summary indicates that the Division calculated additional tax due on "Sales To investor" and amounts due under an installment method of payment. The Division issued to Belhara a Statement of Proposed Audit Adjustment showing that calculation. This statement shows total tax due on "Sales [of] Bulk Shares" of $78,912.00, based on the sale of 7,165 such shares with a tax due of $11.0136 per share. The same statement indicates that four payments totalling $62,192.00 were made
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> on February 13, 1985, January 3, 1986, January 3, 1987 and January 1988. It further indicates that four installment payments remained owing, together totalling $16,720.00. There is no evidence in the record that an assessment was issued with respect to the installment payments shown as due on this statement. Any tax due from the bulk transfer of the 7,165 shares is not a subject of this proceeding. The bulk transfer of the 7,165 shares is involved in this proceeding to the extent that the $2,589,925.00 sales price of said shares was utilized by the Division in calculating total consideration and, ultimately, the tax due per share of $11.0136.[10]

We modify the Administrative Law Judge's finding of fact "17" to read as follows:

> To summarize, the Division's audit resulted in the following adjustments and disallowances:
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> (1) Two updates were made to Belhara's original filing. The Division calculated gains tax due on units sold as of April 10, 1984. As a result, the Division determined tax due on the transfer of 45 units (39 of which were taxable), while Belhara's filing calculated tax due on the transfer of 46 units (40 of which were taxable). The Division calculated interest from October 1, 1984. The Division also determined tax due on the transfer of two additional units on February 8, 1986 and calculated interest from that date. It imposed penalties on the tax assessed on the sale of these two units. There is no evidence in the record that Belhara updated its original filing to report the transfer of these units.
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> (2) The Division determined that the cash consideration on the sale of all units was $4,088,700.00. Thus, Belhara's estimate of gross consideration from the sale of units, $3,333,855.00, was increased by $754,845.00.
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> (3) The Division reduced brokerage fees claimed by Belhara from $200,031.00 to $17,365.00.

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[10] We modify finding of fact "16" of the Administrative Law Judge's determination by deleting the last sentence of said finding of fact which read: "[t]he transfer of these 7,165 shares is not a subject of this proceeding" and by adding the last two sentences to the modified finding of fact to reflect the fact that any tax due on the 7,165 shares was not at issue but that the consideration received for such shares was used in calculating the tax due per share.

(4) The Division disallowed the following acquisition costs as claimed by Belhara:

Title Insurance	$ 9,482.00
State real property transfer tax	3,353.00
City real property transfer tax	70,249.00
Mortgage recording tax	14,299.00
Title searches	322.00
Survey	79.00
Recording fees	200.00
Legal fees	11,302.00
Total	$109,286.00

(5) The Division disallowed three items included by Belhara in its computation of the cost of capital improvements: conversion period interest in the amount of $83,992.00, conversion period taxes in the amount of $9,865.00, and selling expenses in the amount of $5,198.00.

(6) With respect to conversion costs claimed by Belhara, the Division disallowed legal fees of $20,182.00 and a market survey of $3,226.00.[11]

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

The Division issued a Conciliation Order dated February 8, 1991, reducing the total tax deficiency asserted to $56,839.37. The reduction was based on additional documentation provided by Belhara. As the result of the additional documentation, the Division increased original purchase price by $34,710.00, which amount consisted of additional legal fees of $31,484.00 ($11,302.00 and $20,182.00) and the cost of a market survey in the sum of $3,226.00. The additional $34,710.00 of costs allowed was reduced by $2,252.00, to $32,458.00, to reflect the portion of said costs apportioned to the six grandfathered units.

As the result of this adjustment, the Division reduced the gain on the sale of taxable units from $1,579,239.00 to $1,546,781.00, which reduced the tax due to $154,678.10 and the tax due per share to $10.7872.[12]

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[11] We modify finding of fact "17" of the Administrative Law Judge's determination by substituting the third sentence of item "(1)" which read:

> "As a result, the Division determined tax due on the transfer of 45 units, while Belhara's filing calculated tax due on the transfer of 40 units."

Also, in the first sentence of item "(2)" we deleted the word "anticipated" from the phrase "the anticipated cash consideration" to reflect that the $4,088,700.00 was actual cash received from the sale of the 86 units and, thus, was not an anticipated amount.

[12] We modify finding of fact "18" of the Administrative Law Judge's determination by adding the last three sentences to reflect the record in greater detail.

OPINION

The Administrative Law Judge concluded Belhara was not entitled to step up its original purchase price to the fair market value at the time of transfer to the cooperative housing corporation because under Mayblum v. Chu (67 NY2d 1008, 503 NYS2d 316), Article 31-B of the Tax Law was designed to treat a cooperative conversion as a single transaction for purposes of applying the gains tax. The Administrative Law Judge recognized that petitioner's step-up in original purchase price would require that the conversion be viewed as two separate transactions and that this construction is contrary to the existing case law.

Second, the Administrative Law Judge declined to treat a mortgage created pursuant to a binding written agreement executed prior to the effective date of the gains tax in the same way as a bargain lease created prior to the effective date of the gains tax in determining consideration for the sale of stock in the cooperative housing corporation. The Administrative Law Judge, relying on Matter of Birchwood Assocs. (Tax Appeals Tribunal, July 27, 1989), held that the Division properly treated a portion of a mortgage given by the cooperative housing corporation to petitioner pursuant to a binding written agreement executed prior to the enactment of the gains tax law as consideration to petitioner on the subsequent sale of stock to unit purchasers even though no portion of the value of a bargain lease created prior to the effective date of the gains tax would be treated as taxable consideration by the Division. The Administrative Law Judge held that the bargain lease and mortgage were distinguishable in that the consideration from a bargain lease is received by the sponsor at the time the lease is executed, while a mortgage involves payments received over the term of the mortgage.

Third, the Administrative Law Judge addressed the constitutionality of (i) treating transfers of property to a cooperative corporation different from transfers to non-cooperative corporations and (ii) the Division's refusal to "grandfather" mortgages placed on the real property pursuant to a binding written agreement executed before the effective date of the gains tax in determining petitioner's consideration. The Administrative Law Judge rejected petitioner's constitutional arguments stating the Court of Appeals already addressed these issues in Trump v. Chu (65

NY2d 20, 489 NYS2d 455, appeal dismissed 474 US 915), and held that the disparate treatment accorded cooperative corporations and non-cooperative corporations was constitutional.

Fourth, the Administrative Law Judge upheld the Division's disallowance of conversion period interest and conversion period real property taxes in the calculation of original purchase price. The Administrative Law Judge held that the record was devoid of any evidence explaining and documenting the claimed expenses for conversion period interest and conversion period real property taxes and that the Division's disallowance of same was, therefore, proper.

Fifth, the Administrative Law Judge concluded that the Division properly calculated the gains tax due; that it properly apportioned the gain to each unit and that petitioner failed to establish that the Division's calculation and apportionment methods were erroneous.

Sixth, the Administrative Law Judge found that the Division correctly imposed interest from October 1, 1984 based on the number of shares sold as of said date and that interest was also properly calculated on the 425 shares sold on February 8, 1986.

Finally, the Administrative Law Judge refused to abate penalties and penalty interest which were imposed only on the tax assessed for the period ended February 8, 1986 because petitioner failed to establish reasonable cause.

On exception, petitioner asserts that: (1) The Division must use the fair market value of the property on the date it was sold by petitioner to the cooperative housing corporation in computing the original purchase price because the Division would do so if the real property had been transferred to an entity other than a cooperative housing corporation prior to March 28, 1983; (2) the Division must treat mortgages created pursuant to a binding written agreement executed prior to March 28, 1983 the same way bargain leases created prior to March 28, 1983 are treated when determining consideration on the subsequent sale of stock in the cooperative housing corporation; (3) the Division's refusal to (i) step-up the original purchase price to fair market value on the date of the transfer to the cooperative housing corporation and (ii) treat mortgages the same as bargain leases in determining consideration, is violative of both the United States and New York State Constitutions; (4) since under Mayblum v. Chu (supra), the

cooperative conversion is treated as a single transaction for gains tax purposes, the overall project gain should be allocated on a per-share basis for determining gain subject to tax under Option B; (5) conversion period interest and conversion period real property taxes are customary, reasonable and necessary expenses incurred to create ownership interests in cooperative form, and as such, are properly includable in original purchase price; (6) the Division incorrectly charged interest on units sold as of October 1, 1984 since the tax due as determined by the Division is based on the difference between the actual consideration received versus the consideration as originally estimated and pursuant to Option B no interest or penalty can be charged prior to the required update filing; and (7) penalties and penalty interest should be abated because (i) it voluntarily and timely filed the questionnaire reporting the 46 unit transfers in connection with the conversion of the property; (ii) its computation of gains tax due as reported on its questionnaire was made in good faith and was based upon a reasonable interpretation of the Tax Law; and (iii) its representative had periodic discussions with Division personnel concerning gains tax filings and it was reasonable for petitioner to rely on its representative's comments and direction.

In this proceeding, petitioner asserts that there was an overall project loss of $131,563.00, which amount was computed as follows:

Gross Consideration

Grandfathered units	$ 207,455.00
Taxable units	3,881,245.00
Subtotal	4,088,700.00
Purchase money mortgage - exempt	-0-
Subtotal	4,088,700.00
Less: Brokerage commissions	(18,492.00)
Reserve fund	(287,500.00)
Total Consideration	$3,782,708.00

Original Purchase Price

OPP as determined by Division		$3,254,447.00
Add: Difference between consideration received by petitioner on sale to cooperative housing corporation ($3,888,475.00) less purchase price paid by petitioner to acquire ($3,048,000.00)		840,475.00

Conversion period interest	83,992.00
Conversion period real property taxes	9,865.00
Legal fees	31,484.00
Total Original Purchase	$4,220,263.00

By subtracting total original purchase price ($4,220,263.00) from total consideration ($3,782,708.00) petitioner arrives at a loss of $131,563.00 (Petitioner's brief on exception, p. 8). Petitioner's computation is in error since $3,782,708.00 less $4,220,263.00 produces a loss of $437,555.00 and not a loss of $131,563.00 as reported by petitioner. Belhara argues that since the overall project resulted in a loss, it is entitled to a refund of the $120,373.00 of gains tax paid to date, plus interest.

We affirm the determination of the Administrative Law Judge.

We first address the issue of whether the Division must step-up the original purchase price of the property to its fair market value at the time of its transfer to the cooperative housing corporation.

Petitioner argues that the Division must use the fair market value of the property on the date it was sold by petitioner to the cooperative housing corporation in computing the original purchase price because the Division would do so if the property had been transferred to an entity other than a cooperative housing corporation prior to March 28, 1983. We reject petitioner's contentions.

To begin with, it is well settled that a cooperative conversion is treated as a single transaction for purposes of applying the gains tax (Mayblum v. Chu, 109 AD2d 782, 486 NYS2d 89, mod 67 NY2d 1008, 503 NYS2d 316; Matter of 1230 Park Assocs. v. Commissioner of Taxation & Fin., 170 AD2d 842, 566 NYS2d 957, lv denied 78 NY2d 859, 575 NYS2d 455). Allowing petitioner to step-up its original purchase price of the property to its fair market value at the time of transfer would have the effect of treating the cooperative conversion as two transactions, i.e., the transfer to the cooperative housing corporation and the transfers of shares to individual unit purchasers, instead of one (Matter of 470 Newport Assocs., Tax Appeals Tribunal, September 2, 1993). Furthermore, it is of no significance that the property was transferred to the cooperative housing corporation pursuant to a contract entered into prior to March 28, 1983

(the effective date of the gains tax), for it is the transfer of shares to unit purchasers which is the taxable event, and not the transfer to the cooperative housing corporation (Mayblum v. Chu, supra, 503 NYS2d 316, 317).

We have already considered and rejected the argument that the Division is required to tax transfers to cooperative housing corporations in the same manner as transfers to other types of entities. In Matter of 61 East 86th St. Equities Group (Tax Appeals Tribunal, January 21, 1993), we stated:

> "[a]s we noted in 1230 Park, Article 31-B has a number of provisions that single out transfers pursuant to a cooperative or condominium plan for treatment different from that applied to other types of transfers. In our view, these provisions, contained in former sections 1440(7), 1442, and section 1443(6), provide ample support for the Division's decision to tax transfers pursuant to a cooperative plan like transfers pursuant to a condominium plan and, as a result, to treat cooperative corporations differently from non-cooperative corporations" (Matter of 61 East 86th St. Equities Group, supra; see also, Matter of 470 Newport Assocs., supra).

Next, petitioner argues that the Division must treat mortgages created pursuant to a binding written agreement executed prior to March 28, 1983 the same way it treats bargain leases created prior to such date when determining consideration on the subsequent sale of the stock. Petitioner contends that since it received the mortgage pursuant to a binding agreement executed prior to March 28, 1983, the consideration attributable to such mortgage should be grandfathered. We disagree.

A mortgage, whether created prior or subsequent to the effective date of the gains tax, is treated by the Division as consideration only on that portion of the mortgage allocated to shares sold after the effective date of the gains tax, pursuant to contracts entered into after such date. This treatment of a mortgage as consideration was sustained by the Court in Matter of 1230 Park Assocs. v. Commissioner of Taxation & Fin. (supra).

We find no merit to petitioner's contention that the Division must treat pre-gains tax mortgages the same as pre-gains tax bargain leases. The Division's decision to treat no portion of a pre-gains tax bargain lease as taxable consideration is not inconsistent with the Division's treatment of mortgages because they are two very different types of encumbrances (Matter of

470 Newport Assocs., supra), and the Division's treatment reflects these differences. Among the differences is the fact that a mortgage encumbers each individual unit while a bargain lease does not.

Furthermore, even if petitioner were to persuade us that bargain leases and mortgages were to be treated the same, i.e., allocated to all units, petitioner has not attempted to explain why the pre-gains tax mortgage should be treated like the pre-gains tax bargain lease, instead of vice versa.

Petitioner next argues that the Division's refusal to step-up original purchase price to fair market value on the date of transfer to the cooperative housing corporation and its different treatment of mortgages as compared to bargain leases violates the Equal Protection Clause of both the United States and New York State Constitutions. We disagree.

With respect to petitioner's constitutional challenges regarding cooperative corporations as compared to other entities, as we noted earlier, Article 31-B of the Tax Law was designed to treat cooperative housing corporations differently than other entities (Matter of 61 East 86th St. Equities Group, supra). The different tax treatment accorded cooperative housing corporations:

> "enjoys a presumption of constitutionality which 'can only be overcome by the most explicit demonstration that [the] classification is a hostile and oppressive discrimination against particular persons and classes. The burden is on the one attacking the legislative arrangement to negative every conceivable basis which might support it' [citations omitted]" (Trump v. Chu, supra, 489 NYS2d 455, 458-459).

Petitioner has not carried its burden in light of the Court of Appeals' decision upholding the different gains tax treatment of cooperative and condominium developments compared to subdivided realty in Trump v. Chu (supra).

Turning next to petitioner's equal protection argument concerning the Division's different treatment of mortgages and bargain leases, we find no merit to petitioner's assertion that the distinction drawn by the Division between mortgages and bargain leases violates the Equal Protection Clause of either the New York State or United States Constitution (see, Matter of National Elevator Indus. v. New York State Tax Commn., 49 NY2d 538, 427 NYS2d 586).

We next address whether the Division properly calculated gain and tax due on audit. On audit, the Division calculated gain and tax due using the actual consideration received on the units subject to tax plus the pro-rata portion of the mortgage allocated to such units minus the pro-rata portion of the original purchase price allocated to the taxable units. Petitioner argues that since the gains tax treats the cooperative conversion as a single transaction, the overall project gain should be allocated on a per-share basis for determining gain subject to tax under Option B. In essence, petitioner asserts that all unit transfers, including grandfathered transfers, be counted in calculating gain per share and the gain per share be multiplied by the number of shares subject to tax. We disagree.

Prior to August 1986, there were two methods of calculating gains tax liability upon transfers of cooperative apartment units, Option A and Option B (see, TSB-M-83-[2]-R). Under Option A, gain was computed based on the actual consideration received less the pro-rata portion of original purchase price allocated to each unit. Under Option B, a taxpayer can elect, prior to the time it starts making taxable sales, to estimate the consideration to be received on all future sales. Although petitioner properly elected to compute its gains tax liability under Option B, it has not provided us with any support for the proposition that under Option B, gain per share is computed based on the total project gain (net of grandfathered and non-grandfathered shares) and then allocated to the non-grandfathered shares to compute tax due. We find that the Division's computational method which includes only the consideration received on taxable units is reasonable. Such method is in harmony with determining whether the cooperative conversion is taxable based on whether consideration anticipated on taxable units along reaches the $1,000,000.00 threshold.

Petitioner's next argument concerns whether conversion period real property taxes and conversion period interest are includible in original purchase price. Petitioner argues that both costs, pursuant to Tax Law § 1440(5)(a), are customary, reasonable, and necessary expenses incurred to create ownership interests in cooperative form. We disagree.

We addressed this same argument in Matter of 44 West 62nd St. Assocs. (Tax Appeals Tribunal, August 11, 1994) where we held that:

> "conversion period interest and conversion period real property taxes are not costs incurred to create ownership interests in cooperative form. These costs are merely expenses incurred to carry the property and not incurred to create ownership interests in the property (Matter of Mattone v. State Dept. of Taxation & Fin., 144 AD2d 150, 534 NYS2d 478). We direct petitioner's attention to our decision in Matter of 1230 Park Assocs. (Tax Appeals Tribunal, July 27, 1989, affd Matter of 1230 Park Assocs. v. Commissioner of Taxation & Fin., 170 AD2d 842, 566 NYS2d 957) where we stated the test was whether the cost 'can be characterized as an expense incurred to create ownership in the cooperative form.'"

Whether petitioner has provided documentation substantiating the claimed expenses for conversion period interest and conversion period real property taxes and whether original purchase price should be computed under the provisions of Tax Law former § 1440(5) or pursuant to Tax Law § 1440(5)(a) as amended by the Laws of 1984 (ch 900, § 3, eff September 4, 1984) is of no consequence to our decision since, as discussed, conversion period interest and conversion period real property taxes are not expenses properly includible in original purchase price for purposes of calculating the gains tax.

With respect to its argument that the Division incorrectly computed interest, petitioner states that:

> "the additional Gains Tax, if any, is attributable solely to units sold after the seventy-five percent (75%) project sellout. Also, pursuant to 'Option B,' no interest or penalty can be computed on the units sold prior to a required update filing based upon any difference between the actual 'consideration' received and the originally estimated 'consideration.' Accordingly, since Respondent has recomputed the Gains Tax all the units sold, which results in an erroneous assessment of additional tax on such transfers, and has computed interest on such additional Gains Tax amount, any interest amount ultimately determined to be due must be recomputed" (Petitioner's brief on exception, pp. 35, 36).

Petitioner's initial gains tax questionnaire reported that 7,975 shares, representing 52% of total shares, were transferred on or about March 15, 1984. It is undisputed that there was a bulk sale of 7,165 shares on or about December 28, 1984, thus, making the project 98.7% sold out. When the last two units were transferred on February 8, 1986, the project was completely sold out, thus, petitioner was required to file a project update upon the bulk transfer since said sale

pushed it beyond the 75% sellout plateau and it was also required to file a final update upon the sale of the last two units on February 8, 1986, when it reached 100% sellout. Petitioner is incorrect when it asserts that the tax due "is attributable solely to units sold after the seventy-five percent (75%) project sellout." Only two units, apartments GR-1 and GR-2, were transferred after the 75% sellout plateau.

The following table sets forth the amounts attributable to the taxable units as reported by petitioner on its questionnaire and as computed by the Division on audit after the adjustments made at conference:

	Petitioner	Division
Gross consideration	$4,157,951.00	$4,907,594.00
Less: broker's fees	<187,584.00>	<16,238.00>
purchase price	<3,011,830.00>	<3,075,730.00>
cost of improvement	<447,231.00>	<268,845.00>
Taxable gain	$ 511,306.00	$1,546,781.00

As can be seen from this chart, the taxable gain, and ultimately the tax due per share, was increased as the result of (1) an increase of $749,643.00 in taxable consideration due to the fact that petitioner's estimate of the fair market value of the unsold shares as reported on its questionnaire of $254.1106 was substantially lower than the actual selling price per share of $361.4689 as received from the bulk sale and (2) a net decrease of $285,832.00 in expenses claimed by petitioner for broker's fees, acquisition costs and cost of improvements. This analysis shows that the tax due at issue is not derived solely from an increase in consideration with respect to units sold after the 75% project sellout as asserted by petitioner.

Tax Law § 1446 provides that if it is determined that the tax has been underpaid, the person liable for the tax due shall pay interest. Tax Law former § 1442 provides that the tax due shall be paid on the date of transfer and that the date of a transfer pursuant to a cooperative plan is the date that each cooperative unit is transferred.

Here, it was proper for the Division to assert interest against petitioner considering that a portion of the tax due comes from disallowed expenses and also that petitioner's questionnaire, as filed, was incorrect and insufficient. Pursuant to TSB-M-83[2]-R, a taxpayer, when electing to report its gain under Option B, can apportion the gain pursuant to three methods acceptable to

the Division and it must submit a statement setting forth the basis of determining total gross consideration. Petitioner, on its questionnaire, did not use any of the three approved apportionment methods (it used as a fixed common denominator fair market value) and there is no evidence to show that the Division was requested to or approved of the use of this alternative apportionment method. Furthermore, there is no evidence to show how petitioner determined the fair market value of $254.1106 per share for all unsold units. Accordingly, it was proper for the Division to assert interest against petitioner.

Finally, we address whether petitioner has established reasonable cause for abatement of the penalties and penalty interest which were assessed only on the last two transfers made on February 8, 1986.

Tax Law § 1446(2)(a) authorizes imposition of a penalty and penalty interest for failure to pay over tax in a timely manner. These charges may be cancelled if the failure was due to reasonable cause, and not due to willful neglect (Tax Law § 1446[2][a]). We agree with the Administrative Law Judge's conclusion that (1) most of petitioner's arguments concerning reasonable cause are irrelevant; (2) there is no evidence to support that petitioner reported the sale of these last two units to the Division; and (3) petitioner did not establish reasonable cause for its failure to pay over the tax in a timely fashion. Therefore, we find no basis to abate the penalties.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Belhara Associates Limited Partnership is denied;
2. The determination of the Administrative Law Judge is affirmed;
3. The petition of Belhara Associates Limited Partnership is denied; and

4. The Notice of Determination dated March 3, 1989, as modified by the Conciliation Order, is sustained.

DATED: Troy, New York
December 15, 1994

/s/John P. Dugan
John P. Dugan
President

/s/Francis R. Koenig
Francis R. Koenig
Commissioner