STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
CLINTON HILL EQUITIES GROUP	:	DECISION DTA No. 811804
for Revision of a Determination or for Refund of Tax on Gains Derived from Certain Real Property Transfers under Article 31-B of the Tax Law.	: :	

Petitioner Clinton Hill Equities Group, c/o Louis J. Polonkay, C.P.A., Time Equities, Inc., 55 Fifth Avenue, New York, New York 10003-4301, filed an exception to the determination of the Administrative Law Judge issued on June 29, 1995. Petitioner appeared by Ziegler, Sagal and Winters, P.C. (Stephen S. Ziegler, Lanny M. Sagal and Alan Winters, Esqs., of counsel). The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (Paul A. Lefebvre, Esq., of counsel).

Petitioner filed a brief in support of its exception. The Division of Taxation filed a brief in opposition. Petitioner's reply brief was received on December 15, 1995 and began the six-month time period for the issuance of this decision. Petitioner's request for oral argument was denied.

Commissioner DeWitt delivered the decision of the Tax Appeals Tribunal. Commissioner Koenig concurs. Commissioner Dugan dissents in a separate opinion.

ISSUE

Whether a "financing fee" consisting of a percentage of proceeds from the sale of cooperative apartment units constituted a customary, reasonable and necessary expense incurred to create ownership interests in property in cooperative form which was includible in petitioner's original purchase price pursuant to Tax Law § 1440(5)(a)(ii).

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge. These facts are set forth below.

1. Petitioner, Clinton Hill Equities Group, a New York general partnership, is the sponsor in the cooperative conversion of property located at 165 Clinton Avenue, Brooklyn, New York (the "property").

2. Francis Greenburger is the sole stockholder, chairman and chief executive of Time Equities, Inc. ("TEI"). He has been engaged in the cooperative conversion business for approximately 15 years and has participated in converting to cooperative ownership in excess of 50 projects involving approximately 100 buildings.

3. TEI provides the various professional services necessary to accomplish a cooperative conversion, including preparing the co-op plan, acting as the sales agent, and acting as the managing agent for the converted building.

4. Insofar as is relevant herein, there are two categories of financing that are used to achieve a cooperative conversion. One is the permanent or underlying mortgage financing that will be on the property when the co-op takes title. The second type of financing (sometimes referred to as "end loan" financing) is the financing for the individual purchasers to purchase their apartments.[1]

5. Prior to the recession of the mid-1970's, cooperatives had been common in the more affluent areas of New York City (the "City"), such as Park Avenue and Central Park West, but had been less common or relatively unknown in the middle-income and lower-income areas.

6. During the period when the Clinton Hill conversion was proceeding, the general market for cooperative financing was very limited.

---

[1]A third type of financing that is often utilized is known as unsold share financing, which would provide the sponsor with a loan against the units that he does not sell immediately upon the conversion.

7. In the 1981-1984 period, TEI undertook to convert some apartment buildings that were located in Greenwich Village, and had to get financing from a private mortgage company called BRT Realty Company ("BRT"). The interest rate that BRT charged was approximately five points over prime, plus a percentage of the income realized from the conversion. This kind of hybrid financing structure was relatively common.

8. In some cases, when TEI negotiated with sellers, it attempted to get them to provide the underlying mortgage portion of the financing or, on occasion, the unsold share financing and possibly even an end loan for the tenant-stockholders. Typically, for doing that, the lender would receive an incentive participation in the profits from the conversion (commonly known as an "equity kicker") of from 5% to 25%.

9. The Clinton Hill area had at one time been the location of the Brooklyn Navy yard, and the buildings making up the Clinton Hill project were originally built to house Navy personnel. When the Navy yard closed, the nature of the area changed and a new population moved in -- primarily low-income/minority families.

10. Many of the buildings in the area had suffered significant deferred maintenance, and many of them were vacant and had been boarded up.

11. In the years leading up to petitioner's acquisition, the property had suffered by virtue of the limited income it generated (because it was subject to rent control and rent stabilization). In general, there was a lot of deferred maintenance and the project was facing a crisis.

12. Mr. Greenburger initially entered into a contract of sale, dated January 30, 1981, with an unrelated party, Clinton Hill Associates ("CHA"), to purchase the property.

13. In the contract, the seller, CHA, acknowledged and indicated its understanding of Mr. Greenburger's intention:

> "to prepare a co-op plan and submit same for filing to the Attorney General's Office and seek acceptance for filing of said plan from the Attorney General during the term of this Agreement to offer said plan to the tenants in the premises and to enter into binders with prospective purchasers, in accordance with law."

The contract noted the seller's agreement to cooperate with the buyer by providing documentation and information as requested and to provide access to the premises. The contract further provided, however, that the "Seller shall have no liability and, Purchaser shall not be relieved of any of its obligations under this Agreement, if for any reason whatsoever said plan is not accepted for filing by the Attorney General's Office."

14. Following the execution of the January 30, 1981 contract of sale, Mr. Greenburger endeavored to present a plan of cooperative ownership to the tenants and see whether he could interest them in participating in the transition of the project from rental status to cooperative ownership.

15. Mr. Greenburger's first step was to approach the lender, which was The Equitable Life Insurance Company ("Equitable") -- whose mortgage on the property was to expire in two or three years -- and try to interest it in providing financing for the co-op. He even offered Equitable the possibility of some sort of equity participation. Equitable said it was not interested at all, that it was getting out of the residential lending business and that it just wanted to be paid.

16. Although Mr. Greenburger tried to explain that this was minority housing facing a crisis, the individuals at Equitable with whom he had been dealing were still not interested. It was only after several subsequent appeals to senior management that Mr. Greenburger eventually received a better hearing. At that point, the person with whom he was speaking indicated that although Equitable really did not want to be involved with the project, it would give Mr. Greenburger the following option. If Mr. Greenburger was successful in his efforts to find a new financing source, Equitable would discount its mortgage so that the new lender would have to provide a lower amount.

17. Once Mr. Greenburger accomplished that, he then began to search for a lender who would provide a permanent mortgage, as well as the end loan, because, in his judgment, there would be no co-op unless the tenants could finance the purchase of their apartments.

18. Mr. Greenburger approached approximately 100 financial institutions and had substantive discussions with approximately 20. The reaction of these institutions was uniformly negative for a variety of reasons, but most of all because of the nature of the project (i.e., its

location and tenant population), which most financial institutions perceived as being an untraditional market for cooperatives.

19. One of these financial institutions, Citibank (hereinafter sometimes referred to as the "bank"), had initially considered providing financing, but after some period of time turned it down.

20. Shortly thereafter, however, Mr. Greenburger received a telephone call advising him that if he wanted to appeal the bank's decision, he could present his case to one of the bank's senior lending officers, Len Druger. The first question Mr. Druger asked Mr. Greenburger was whether the planned conversion had political support in the area. Since prior to undertaking this project Mr. Greenburger had met with the various elected officials, he knew that the planned conversion had political support and he so informed Mr. Druger.

21. After Mr. Druger confirmed Mr. Greenburger's representations of political support, he called Mr. Greenburger and told him that the bank was interested in discussing the matter further, and very lengthy, arduous negotiations ensued.

22. Early on in the negotiations, Mr. Druger outlined for Mr. Greenburger what would be the broad parameters of the type of financing package the bank would consider. Although Mr. Druger was not prepared to commit to these terms, he wanted to know whether they would be acceptable to petitioner if the bank went ahead. One of the items that was on the list was a financing fee -- which was substantially higher than the one that was finally agreed to.

23. The bank wanted to make the loan only if it could get very favorable terms because it felt that it was going out of its way to make the loan; that the end loans would be difficult because they required a lot more paperwork than usual (due to many applications for SONYMA [government assisted] financing); there were small amounts involved and a much higher risk than usual. Although the bank was under political pressure to make more loans in the boroughs, it wanted to mitigate what it perceived as a heightened financial risk by better financial terms.

24. Initially, the bank proposed a fee of 15% of gross sales. Mr. Greenburger was able to negotiate the deduction of certain types of costs from the fee base, and also eventually achieved a reduction in the rate to 7%.

25. The overall negotiations with Citibank took over a year and were extremely difficult, with the bank contesting virtually every point raised by petitioner.

26. The overall negotiations between Mr. Greenburger and the bank involved both the fixed commitment fee and the financing fee at issue herein. Such negotiations ultimately resulted in the issuance by the bank of two separate commitment letters, both dated August 11, 1982, regarding the underlying mortgage financing (the Citibank refinancing) and the end-loan financing, respectively. The letter detailing the bank's commitment to the underlying mortgage financing set forth the details regarding both the fixed commitment fee (ultimately $252,000.00) and the financing fee at issue. The letter detailing the bank's commitment to end-loan financing indicated that the bank would make such financing available to individual unit purchasers and set forth the terms and conditions of such financing. This letter did not make any reference to the financing fee at issue herein.

27. In Mr. Greenburger's opinion, there was no possibility of doing the Clinton Hill conversion without an end-loan financing package.[2]

28. In Mr. Greenburger's opinion, at that time there was no other financing available that was remotely close to providing what Citibank provided. Thus, in his opinion, there was no alternative to the Citibank financing that he could have utilized.

29. On June 1, 1982, Francis Greenburger assigned his rights to acquire the property under the January 30, 1981 contract to petitioner (a general partnership of which Mr. Greenburger was the managing general partner), and petitioner purchased the property.

30. The purchase price paid at the closing was $12,300,000.00, consisting of the following:

---

[2]Individual unit purchasers were not obligated to utilize Citibank to finance their purchase. During the early part of the conversion period, most purchasers financed through Citibank. Later, more unit purchasers financed their purchase through other banks.

Purchase Money Mortgage	$ 4,758,855.00
Transferor taking subject to existing mortgage payable to Equitable (the "Equitable mortgage")	6,820,180.00
Cash and other consideration	720,965.00
Total Price	$12,300,000.00

31. The Citibank refinancing of the Equitable mortgage closed on December 23, 1982, with a $6,000,000.00 loan from Citibank (the "Citibank loan").

32. On April 24, 1984, the date of the transfer of the property to the cooperative housing corporation (the "CHC"), the Citibank loan had a balance of $5,985,793.00.

33. The Citibank mortgage contemplated that it could and would be assumed by the CHC upon conversion of the property to a cooperative. Thus paragraph 10(a) provided:

> "Mortgagor represents and warrants to Mortgagee, as an inducement to Mortgagee to enter into the transaction secured hereby, that Mortgagor shall use its efforts to convert the Premises to cooperative ownership lawfully established in accordance with the applicable laws and regulations of the State of New York. In connection therewith, Mortgagor has prepared and submitted an initial draft of the Offering Plan with the Attorney General."

34. Similarly, the Citibank mortgage (¶¶ 8[b]-[d]) provided the following affirmative covenants of petitioner:

> "(b) Comply with all other affirmative covenants set forth in the Commitment and/or the End Loan Commitment.
>
> "(c) Promptly furnish to the Bank preliminary and final copies of the Offering Plan and of all amendments thereto which are filed with the Attorney General, and copies of all correspondence, communications, notices and other writings of the Attorney General with respect to the Offering Plan.
>
> "(d) Use its efforts to effectuate and consummate the Offering Plan."

35. The Citibank mortgage (¶ 9[c]) provided as a negative covenant of petitioner that petitioner would not "voluntarily abandon the Offering Plan."

36. Pursuant to the Loan Agreement, the Citibank loan was also secured by a pledge of the proceeds of any cooperative conversion of the property.

37. The terms of the Citibank loan in regard to interest rate and maturity were less advantageous if the property was not converted to a cooperative by November 30, 1984; that is:

(a) Interest was payable at 1% over the Citibank "base rate" until the earlier of the date of conversion of the property to cooperative ownership or November 30, 1984.

(b) In the event the conversion occurred on or before November 30, 1984, then after such conversion, interest was payable at Citibank's individual cooperative 30-month loan rate plus 1½% per annum, adjustable after five years.

(c) In the event the conversion did not occur on or before November 30, 1984, from and after December 1, 1984 interest was payable at a rate equal to Citibank's individual cooperative 30-month loan rate plus 4½% per annum, with adjustments on June 1, 1987, December 1, 1989 and June 1, 1992.

(d) In the event that the interest payable during the period ending on the earlier of December 1, 1984 or the conversion was in excess of 15%, such excess would be accrued. Thereafter, interest in excess of 18% would be accrued. Accrued interest was to be carried forward to the first period in which the interest rate was less than the rate at which accrual was required.

(e) Amortization based on 30-year term.

(f) Balance due December 1, 1994 or 10 years from the end of the month of the conversion (later determined to be May 1, 1994).

38. At the time that Citibank agreed to refinance the Equitable mortgage, it also agreed to offer financing to purchasers of cooperative apartments in the conversion.

39. As set forth above, petitioner paid a financing fee to induce Citibank to make the Citibank loan.[3]

The Loan Agreement provides, in part:

> "A. Pursuant to a certain commitment letter dated August 11, 1982, as amended by letter agreements dated November 24, 1982 and December 21, 1982 (hereinafter the commitment, as amended, the 'Commitment'), the Bank undertook to make a loan (hereinafter the 'Loan') of up to $6,000,000 to the Borrower to be secured in part by a first mortgage lien (hereinafter the 'Mortgage') on certain property

[3]Petitioner alleges that it paid $1,174,513.00 of the financing fee. This amount has not been audited. If petitioner prevails, this fee would be allowed subject to verification by the Division of Taxation. Petitioner also paid a commitment fee of $252,000.00.

(hereinafter the 'Property') consisting of land and residential apartment buildings thereon located at 169, 185, 193, 201, 205, 209, 210, 325, 345, 355, 361 and 365 Clinton Avenue, Brooklyn, New York, recently acquired by the Borrower.

* * *

"J. To induce the Bank to make the Loan, the Borrower agrees to pay to the Bank from time to time the Financing Fee (as defined below) more particularly described in Section 4 hereof.

* * *

"4. Financing Fee

"(a) After an amount equal to the Reserve Requirements has been applied and received by the Bank and/or reimbursed to the Borrower out of the Gross Proceeds in accordance with the provisions of Section 3 of this Agreement, the Borrower shall pay to the Bank a fee (the 'Financing Fee') in an amount equal to seven percent (7%) of Adjusted Sales Proceeds received thereafter from time to time by the Borrower.

* * *

"(d) The obligation of the Borrower to pay the Financing Fee shall survive the satisfaction or prepayment of the Mortgage and/or release or application of all collateral held hereunder and shall remain the personal obligation of the Borrower notwithstanding (i) any one or more conveyance(s) of the Property whether to the Apartment Corporation or otherwise and/or (ii) any one or more sales or transfers of Unsold Shares to affiliated persons and/or to persons or entities that are not bona fide third party purchasers until the earlier of (i) September 30, 2032 or (ii) the sale of all of the Shares to bona fide third party purchasers who are not affiliated persons and the payment of the Financing Fee to the Bank."

40. For gains tax purposes, petitioner included the financing fee in original purchase price as a cost of the conversion of the property.

41. The Division of Taxation ("Division") disallowed the entire financing fee. The Division stated the basis for the disallowance of the financing fee as follows:

"Citibank Additional financing fees disallowed by Albany ($1,174,513) since not customary or normal and there is already a commitment fee."

42. On December 9, 1991, the Division issued to petitioner a Notice of Determination which asserted an additional gains tax liability of $43,957.00, plus interest, resulting from the disallowance of the financing fee.

43. Petitioner submitted proposed findings of fact numbered 1 through 40.

(a) Proposed findings of fact 1, 2, 4 through 10, 13, 14, 16 through 23, and 27 through 39 are accepted (and renumbered) herein as Findings of Fact "2", "3", "5" through "11", "15", "16", "18" through "25", and "29" through "41", respectively.

(b) Proposed finding of fact 3, renumbered as Finding of Fact "4" herein, has been modified by substituting "used" for "necessary". Proposed finding of fact 15, renumbered as Finding of Fact "17" herein, has been modified by substituting "in his judgment" for "obviously". Proposed finding of fact 25, renumbered as Finding of Fact "27" herein, has been modified by adding "In Mr. Greenburger's opinion", and by adding footnote "2". Proposed finding of fact 26, renumbered as Finding of Fact 28 herein, has been modified by adding "in Mr. Greenburger's opinion" to each of the sentences and by adding the word "other". All of the foregoing modifications have been made to better reflect the record.

(c) Proposed finding of fact 11 is rejected. Contrary to the assertion made therein, the January 30, 1981 contract was, by its terms, a contract of sale, not an option. Moreover, again contrary to the proposed finding, the language of the contract does not give the purchaser an extended period to effect the conversion.

(d) Proposed finding of fact 12 is rejected. The contract of sale contains no language providing the seller the right to accelerate the closing date if it received another offer to purchase the project.

(e) Proposed finding of fact 24 is rejected. There is insufficient evidence to conclude that, in the negotiations, the bank "never differentiated between the fixed commitment fee and the financing fee" as asserted therein. Moreover, the commitment letters (see, Finding of Fact "26") clearly distinguish between the commitment fee and the financing fee.

(f) Proposed finding of fact 40 is rejected. This proposed finding is in the nature of a conclusion of law rather than a finding of fact.

OPINION

Tax Law § 1440(5)(a) defines "original purchase price" as the consideration paid or required to be paid by the transferor to acquire the property and, insofar as is relevant herein, also includes:

> "those customary, reasonable and necessary expenses incurred to create ownership interests in property in cooperative or condominium form, as such fees and expenses are determined under rules and regulations prescribed by the commissioner" (Tax Law § 1440[5][a][ii]).

20 NYCRR former 590.39 (amended and renum 20 NYCRR § 590.40, eff November 9, 1994) provides that:

> "Question: What are the allowable costs of co-oping (or converting property to condominium form) if paid or required to be paid by realty transferor?
>
> "Answer: The following list illustrates costs that are includible in original purchase price as costs to convert property to cooperative or condominium form:
>
> -- legal, accounting and engineering fees incurred directly as a result of cooperative or condominium formation and transfer of title to the cooperative corporation
> -- filing and recording fees
> -- costs of printing offering plan
> -- title insurance
> -- New York City Real Property Transfer Tax paid as a result of conveyance of title to the cooperative corporation
> -- New York State Real Estate Transfer Tax paid as a result of conveyance to the cooperative corporation
> -- appraisal fees
> -- mortgage recording tax on mortgages created as a result of conveyance of title to the cooperative corporation
> -- mortgage commitment fees
> -- points paid to lender
> -- the cost of 'buying down' the interest rate on co-op loans to purchasers
> -- the cost of 'buying out' nonpurchasing tenants
> -- amounts paid to relocate nonpurchasing tenants"
>
> (20 NYCRR former 590.39).

In its exception, petitioner argues that because of the relationship between the contingent fee at issue and the cooperative conversion, the fee should be considered as relating to the conversion rather than to the acquisition of the property. Further, it argues that the fee was "customary," "reasonable" and "necessary" as required by Tax Law § 1440(5)(a)(ii) in that it was a cost of buying down the interest rate for the cooperative below the rate applicable to property in rental form. Finally, petitioner argues that disallowing the inclusion of the financing fee in original purchase price is contrary to the New York State public policy of encouraging the investment of private capital in low and moderate income housing.

In opposition, the Division argues that the Legislature has given special explicative powers to the Commissioner of Taxation to determine which costs of cooperative conversion are allowable as part of original purchase price. The Commissioner's regulation on this point (20 NYCRR former 590.39) is illustrative of costs incurred to create an ownership interest in property in cooperative form. The mortgage costs allowable apply to mortgages created as the result of conveyance of title to a cooperative corporation. In the present case, the purchase of the property was not conditioned on obtaining permission to convert the property to cooperative form. The loan at issue was a refinance of the acquisition loan. Therefore, the Division argues that the fees at issue were incurred by petitioner as a direct result of the purchase of the property and were not incurred to create an ownership interest in property in cooperative form.

These same arguments were presented by the parties to the Administrative Law Judge. After considering each of them, the Administrative Law Judge correctly applied the law to the facts in this case. In his determination, he concluded that:

> "[t]he cost in question, the financing fee, was incurred pursuant to the terms of the Citibank refinancing agreement . . . . The Citibank loan resulted from petitioner's acquisition of the property. The financing fee at issue was thus a cost to petitioner for a loan to finance its purchase of the property. Such fees are properly categorized as acquisition interest expenses and acquisition interest expenses are expressly disallowed under 20 NYCRR former 590.15(c) . . . .
>
> "That the financing fee was not a cost of converting the property is further evidenced by the fact that the contract of sale by which the property was transferred to petitioner was not conditioned on conversion and by the alternative terms of the Citibank loan in the event that the conversion did not occur. These two facts underscore that the financing fee at issue was a cost to petitioner as a result of its acquisition of the property and was not a cost of conversion, for even if the conversion had been unsuccessful, the contract still required transfer of the property to petitioner and the loan agreement remained in place, albeit under different repayment terms" (Determination, conclusion of law "D").

On exception, petitioner also argues that, based on our decision in Matter of Middle Island Assocs. (Tax Appeals Tribunal, September 21, 1995 [issued subsequent to the determination of the Administrative Law Judge herein]), the financing fee should be an allowable cost because there, as in the instant case, a fee paid on the sale of cooperative units was allowed as part of the original purchase price. In Middle Island, the allowed fee was required under the terms of a refinanced first mortgage entered into after the purchase but prior to the cooperative conversion.

The Division, in opposition, argues that the fee or "equity kicker" at issue is additional consideration paid to the lender for the loan and is in the nature of additional interest. As such, Middle Island disallows the inclusion of such interet in original purchase price. We agree with the position of the Division.

In Middle Island, fees were imposed by the terms of two separate mortgages. The taxpayer claimed each as part of its original purchase price. The First Mortgage required payments to be made to the mortgagee in the aggregate amount of $95,000.00 on the sale of cooperative units. These payments were not to be applied in reduction of the principal amount of the mortgage. The Second Mortgage required a payment of $10,000.00 for each cooperative unit sold which was designated as "additional interest" and was likewise not applied in reduction of the principal amount of the mortgage. We held that the fees imposed by the First Mortgage were includible as part of the transferor's original purchase price while those imposed by the Second Mortgage were not.

In considering the nature of the payment required by the First Mortgage, we held that:

> "[n]ot all cooperative conversion costs are includible as part of the transferor's original purchase price (see, Matter of Belhara Assocs. Ltd. Partnership, Tax Appeals Tribunal, January 26, 1995). For example, as we stated in Matter of 44 West 62nd St. Assocs. (Tax Appeals Tribunal, August 11, 1994), conversion period interest and conversion period real property taxes were not properly included in original purchase price because they:
>
> > '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. Commr. of Taxation & Fin., 170 AD2d 842, 566 NYS2d 957, lv denied 78 NY2d 859, 575 NYS2d 455] where we stated the test was whether the cost "can be characterized as an expense incurred to create ownership in the cooperative form"' (Matter of 44 West 62nd St. Assocs., supra).

"In the present case, paragraph 16.03 of the Consolidation and Extension Agreement, dated July 7, 1987, which resulted in the consolidated First Mortgage, generally prohibited the transfer of any interest in the mortgaged property. The transfer to a cooperative corporation was excepted from this general prohibition, provided that a number of conditions were satisfied. Among these conditions was the requirement that the lender receive and approve of the 'Borrower's agreement to pay Lender a fee as shares in the Cooperative Corporation are sold from time to time, such fee to be paid in installments upon the sale of each unit owned by the Cooperative Corporation' (Appendix A). Because petitioner was required to incur the obligation to pay the $95,000.00 in fees as a condition of transferring the real property to the cooperative corporation, this was a cost incurred to create ownership in the cooperative form.

"Although the fees were paid after the property was transferred to the cooperative corporation, this does not preclude their allowance . . . . There is nothing in the statute [Tax Law § 1440(5)(a)] that imposes a requirement that the costs incurred must be paid prior to the transfer to the cooperative corporation to be an element of original purchase price" (Matter of Middle Island Assocs., supra).

In considering the nature of the payment required by the Second Mortgage, we held that:

"[t]here is no evidence that these fees are 'customary, reasonable and necessary expenses incurred to create ownership interests in property in cooperative . . . form, as such fees and expenses are determined under rules and regulations prescribed by the tax commission' as required by section 1440(5)(a) and as such fees and expenses are illustrated by 20 NYCRR 590.39.

"In Matter of 1230 Park Assocs. (supra), we disallowed negative carrying costs as part of the transferor's original purchase price because they represented a cost of carrying the property in the cooperative ownership form, not creating it. In the present case, the release fees associated with the Second Mortgage were not expended to create ownership interests in property in a cooperative form but were incurred in order to sell property interests in a cooperative form of ownership.

* * *

"Unlike buy-out costs and relocation costs, the payment of the release fees by petitioner herein did not enhance petitioner's ownership interest in

> the cooperative shares and they are not a cost of creating cooperative ownership.
>
> ". . . It is clear from section 590.39 that the points and mortgage commitment fees included in original purchase price relate only to a mortgage given in connection with the creation of the ownership of the property in cooperative form. Here, the Second Mortgage was given prior to the conversion to cooperative form. The fees were contingent and might never be expended. If expended, they resulted from the sale of shares representing cooperative units after the financing was in place, not from the creation of cooperative ownership" (Matter of Middle Island Assocs., supra).

In Middle Island, the inclusion or exclusion of the fees at issue depended upon whether they were costs incurred to create ownership in the cooperative form. In the instant case, the Administrative Law Judge found that the fees at issue were clearly incurred to finance the purchase of the property (i.e., an acquisition interest expense) which costs are expressly disallowed under 20 NYCRR former 590.15(c). We agree with the Administrative Law Judge. The financing fee was not a cost to convert the property to cooperative form and was, therefore, properly excluded from the calculation of petitioner's original purchase price. As a result, we affirm the determination of the Administrative Law Judge.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Clinton Hill Equities Group is denied;

2. The determination of the Administrative Law Judge is affirmed;

3. The petition of Clinton Hill Equities Group is denied; and

4. The Notice of Determination, dated December 9, 1991, is sustained.

DATED: Troy, New York
June 13, 1996

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

/s/Donald C. DeWitt
Donald C. DeWitt
Commissioner

COMMISSIONER DUGAN dissenting:

I respectfully disagree with the opinion of the majority in this matter and would reverse the determination of the Administrative Law Judge.

The majority concludes, based on the analysis of the Administrative Law Judge before our decision in Matter of Middle Island Assocs. (Tax Appeals Tribunal, September 21, 1995), that the fees were incurred in connection with the acquisition of the property since they were paid as part of the refinancing of the Equitable Mortgage.

I disagree.

The fact that the fees were required under the terms of a refinanced first mortgage does not mean they were necessarily incurred in connection with the acquisition of the property. The test is whether the cost can be characterized as an expense incurred to create cooperative ownership to effectuate the cooperative conversion (Matter of 44 West 62nd St. Assocs., Tax Appeals Tribunal, August 11, 1994). In Middle Island, the fees we approved as part of the original purchase price were also incurred in connection with a refinancing. The key to our holding was the provision of the Consolidation and Extension Agreement which generally prohibited the transfer of any interest in the mortgaged property. There was an exception for transfer to a cooperative corporation provided the fee at issue was paid. Under the circumstances, we held that fees had to be paid "as a condition of transferring the real property to the cooperative corporation, this was a cost incurred to create ownership in the cooperative form" (Matter of Middle Island Assocs., supra).

In this case, it is also clear that the fees were paid as a necessary inducement to create ownership in the cooperative form notwithstanding the fact that they also flow from the refinancing of the Equitable Mortgage. Petitioner acquired the property subject to the Equitable Mortgage. It did not incur the Citibank loan to acquire the property. In order to convert the property to cooperative ownership, it was necessary for petitioner to find mortgage financing which could be assumed by the cooperative housing corporation. Equitable would not agree to any extension of its mortgage for that purpose. Equitable indicated, however, that if Mr. Greenburger was successful in his efforts to find a new financing source, that it would discount its mortgage so that the new lender would have to provide a lower amount. Mr. Greenburger approached approximately 100 financial institutions and had substantive discussions with approximately 20. Citibank, after confirming Mr. Greenburger's representation of political support for the project, agreed to discuss the matter further. Citibank indicated that the fee at issue here was a <u>necessary part</u> of any financing package it would consider for the project. The package finally agreed to included the underlying mortgage financing and the end-loan financing. The long and short of the matter is that petitioner could not have achieved a cooperative conversion for the Clinton Hill property without the Citibank financing package and petitioner could not obtain Citibank financing without the fees. As in <u>Middle Island</u>, the fact that the fees were required under a refinancing of the original acquisition indebtedness does not preclude inclusion of the fees in petitioner's original purchase price.

For the reasons stated above, I disagree with the opinion of the majority in this matter and would reverse the determination of the Administrative Law Judge.

DATED: Troy, New York
June 13, 1996

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