STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
SIDAN REALTY CORP.	:	DECISION DTA No. 812314
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 Sidan Realty Corp., 8108 Avenue L, Brooklyn, New York 11236, and the Division of Taxation each filed an exception to the determination of the Administrative Law Judge issued on August 10, 1995. Petitioner appeared by Kestenbaum & Mark, Esqs. (Bernard S. Mark, Esq., of counsel). The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (Laura J. Witkowski, Esq., of counsel).

Petitioner filed a brief in support of its exception and in opposition to the Division of Taxation's exception. The Division of Taxation filed a reply brief which was received on November 28, 1995, and began the six-month period for issuance of this decision. Petitioner's request for oral argument was denied.

Commissioner Koenig delivered the decision of the Tax Appeals Tribunal. Commissioners Dugan and DeWitt concur.

ISSUES

I. Whether, for transfer gains tax purposes, the $1,500,000.00 purchase price for a swim club is included as part of the original purchase price for real property.

II. Whether expenses incurred prior to the sale of condominium units for glass breakage, brooms, paint and locksmith constitute capital improvement costs or maintenance and repair costs.

FINDINGS OF FACT

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

In 1986, Sidney Steinberg and Anthony Clemenza formed petitioner, Sidan Realty Corp., for the purpose of developing and constructing new housing. Mr. Clemenza and Mr. Steinberg each owned 50% of the business; Mr. Steinbergwas a director and president of the corporation and Mr. Clemenza held the offices of secretary and treasurer.

Petitioner negotiated with Abe Maibach, who represented 8060 Property Partnership and Brook Sun & Swim Club, Inc., for the sale of certain adjacent properties in Brooklyn. On January 2, 1986, petitioner entered into an agreement with Brook Sun & Swim Club, Inc. for the sale of "property and business located at premises 8102 Avenue L, Brooklyn, New York." In that agreement, the "property" sold was described as follows:

> "The swimming club, pool, recreation center and the business operated in connection therewith, including all of the structures, improvements and erections thereon, including pool, restaurant, locker rooms and showers, office building and auditorium located thereat and all machinery, fixtures and equipment which are part of the structures, improvements and erections at said premises, together with the good will and telephone service, excluding however the real property and all personal property and movable equipment utilized in connection with such operation, consisting of lockers, benches, chairs, tables, beach umbrellas, play and athletic equipment, beach chairs, chaise lounges, mats, office furniture, equipment and desks . . ." (emphasis added).

The contract was signed by Abe Maibach, as president of Brook Sun & Swim Club, Inc.

According to the agreement, the purchase price was $1,500,000.00 and the closing was to occur one week after Labor Day of 1986. A rider was attached to the agreement, signed on January 2, 1986 by Anthony Clemenza, representing Sidan Realty Corp., and Abe Maibach, individually and as president of Brook Sun & Swim Club, Inc. and general partner of 8060 Property Partnership. The supplemental rider referred to contracts and agreements among Brook Sun & Swim Club, Inc., Abe Maibach, 8060 Property Partnership and Sidan Realty Corp. Paragraph 12 of the rider read as follows:

> "The contacts [sic] and agreements referred to herein are a group of four (4) in number and cover three lots in Block 8058, seven lots in Block 8058 and one lot in Block 8060 . . . and the business of Brook Sun & Swim Club, Inc."

The rider further provided that the four contracts were each contingent on the other; that a default or breach of one contract would be deemed a default and breach of all four contracts; and that the purchaser was not required to take title unless it could take title under all four contracts.

The Division of Taxation ("Division") submitted into evidence three contracts for sale of property signed on September 10, 1986. One contract was between 8060 Property Partnership and Sidan Realty Corp. for the sale of one lot, upon which the Brook Sun & Swim Club was located, for the sum of $1,300,000.00. The contract was signed by Abe Maibach, as partner of 8060 Property Partnership. Schedule A attached to the contract described the location of the real property and included as part of the description of the property "the buildings and improvements thereon erected." A rider, also attached to that contract, provided that the seller could continue operation of the swim club through the 1986 summer season and that it could retain ownership of all personal property and equipment "utilized in connection with such operation, consisting of lockers, benches, chairs, tables, beach umbrellas, play and athletic equipment, beach chairs, deck chairs, chaise lounges, mats, etc. . . . ."[1]

Another contract involved the sale of three lots of unimproved real estate that had been operated as a parking lot. The seller was 8060 Property Partnership and the purchase price was

[1]Thereafter, Sun & Swim Club auctioned off the club furnishings including diving boards, slides, chlorinators and structural items such as the hurricane fencing and cyclone fence, gas pumps, air conditioners, storm windows and doors, lighting and turnstile gates.

$210,000.00. The third contract involved the sale of seven lots, also unimproved land operated as a parking lot, by Abe Maibach[2] to petitioner for $490,000.00.[3]

Petitioner purchased all the properties with the purpose of constructing new condominium housing. It had no intention of operating a swim club. It purchased the swim club with the intention of converting the land use to newly-constructed condominiums where the pool and recreation building could be retained for the use of condominium owners. The swim club property contained a recreational and office building, tennis courts, handball courts, and other structures. Petitioner constructed housing in the locations of the tennis and handball courts, kept the recreational building for the use of condominium owners and replaced the pool with a new pool in a slightly different location, which was more suitable under its construction plan.

Mr. Steinberg testified that in negotiating the price for the properties he concluded that the value of the improvements on the real estate of the Brook Sun & Swim Club was $1,250,000.00 and the value of the land plus improvements was $3,500,000.00. These improvements included the buildings and all the equipment and swimming pool. According to his testimony, the $1,500,000.00 purchase contract with Brook Sun & Swim Club was for the purchase of those improvements.

In a letter, dated May 30, 1991, responding to the auditor's inquiries, petitioner claimed that it purchased the swim club for the sole purpose of acquiring the land. It stated that after much negotiation the seller presented the four contracts asserting that the only way it would sell the property was in this manner. Petitioner claimed that it had to "accede to this method of

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[2]Abe Maibach was a nominee for nine other individuals in the sale of these seven lots. He was also a partner of 8060 Property Partnership, and a shareholder and president of the Brook Sun & Swim Club, Inc.

[3]The only deeds recorded with respect to these four transactions were the three contracts involving the purchase of the unimproved lots that had been used as parking lots and the purchase of the parcel upon which the swim club was located. There was no deed recorded concerning the $1,500,000.00 contract with Brook Sun & Swim Club, Inc.

purchase, even though all parties knew and understood that Sidan would demolish the existing structures immediately after taking title and had no intention of operating a swim club."

After the construction of the project and the sale of condominium units, petitioner filed a 50% update questionnaire dated September of 1989. The Division requested additional documents in the course of performing a desk audit.

The Division issued a Schedule of Adjustments, dated June 10, 1991, disallowing several items claimed by petitioner as part of its original purchase price. Because the desk audit took approximately two years to complete, the adjustments were based on a 75% update of units sold from February 3, 1988 through May 30, 1991. Among the items disallowed were the (1) $1,500,000.00 purchase price for Brook Sun & Swim Club on the ground that the amount was for the purchase of the goodwill of the business or the business itself and not for the purchase of real property, (2) the capitalization of real estate taxes of $10,662.00, (3) a mortgage commitment fee of $31,111.00 and mortgage broker fee of $15,972.00, and (4) an $18,500.00 cleaning fee and $139,980.00 expense that petitioner claimed were capital improvement expenses.

At the hearing held on September 13, 1994, the Division's auditor testified that she disallowed a mortgage commitment fee in the amount of $6,520.00 for nonsubstantiation. She also disallowed a mortgage commitment fee in the amount of $31,111.00 because that portion of the total $112,000.00 fee represented the $2,500,000.00 of a $9,000,000.00 loan from Dime Savings Bank used to refinance a loan from National Westminster Bank to acquire the property. She also disallowed a $15,972.00 mortgage broker fee on the same ground. She stated that because she had already allowed closing costs to borrow approximately $2,000,000.00 on the acquisition of the property in 1989, the disallowed broker fee and commitment fee were duplicative.

The closing statement concerning the four contracts indicates a bank loan from National Westminster Bank in the amount of $2,053,138.13 to petitioner for the acquisition of the

properties.[4] In January of 1987, Sidney Steinberg, Anthony Clemenza and James Clemenza took out an 18-month loan from Dime Savings Bank. Mr. Steinberg testified that the Dime Savings Bank loan was a $9,000,000.00 construction loan, only $2,500,000.00 of which petitioner actually drew down on. He stated that the $2,500,000.00 was collateralized by the land.

Dime Savings Bank sent to Messrs. Steinberg, Anthony Clemenza and James Clemenza a commitment letter, dated January 21, 1987, stating that it had approved their "request for a construction loan . . . secured by a first mortgage" on the premises. The premises were described in paragraph G and included the real property described in the three contracts. Paragraph H of the commitment letter described the purpose of the loan as follows:

> "Two Million Five Hundred Thousand Dollars ($2,500,000) shall be disbursed at the Closing and shall be applied for the acquisition of the Premises. All future advances will be based upon work completed and in place as further defined in the General Terms and Conditions."

The General Terms and Conditions provided that the loan was secured by a first mortgage lien on the premises.

Mr. Steinberg testified that the $2,500,000.00 was used for construction and that this loan was "the only way [they] were able to build the buildings." On cross-examination, Mr. Steinberg testified as follows:

> Q. "On the second page in paragraph H it states that 'the purpose of the loan, 2.5 million, shall be disbursed at closing and shall be applied for an acquisition of the premises.' What does that statement mean, then?"
>
> A. "What is the date on that?"
>
> Q. "January 21st, 1987."
>
> A. "When did we purchase the -- when did we close?"

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[4]The closing statement indicates a loan to petitioner from National Westminster Bank USA for $2,053,138.13 less $553,138.13 for the satisfaction of an existing mortgage. Of the balance, $215,000.00 was used to pay for the seven lots purchased for $490,000.00, and $1,285,000.00 was used for the purchase of the swim club. No other documentation of the loan was submitted into evidence. Therefore, the record is silent as to how this loan was secured and if or when it was paid off.

Q. "September 8th was the closing date."

A. "How could we borrow money three, four months later to pay for the land?"

Q. "That's what I am asking you."

A. "We already paid for the land. That's the way they just write it up in their commitment letter, but that has nothing to do with the acquisition. We already had the land, we already acquired it. They just used the land as collateral. It had nothing to do with the acquisition."

Q. "So, basically, you are stating in your testimony that this document means something other than what it says here?"

A. "Yes. They write it the way they want to sometimes. It had nothing to do with the acquisition."

Q. "What was the 2.5 million dollars used for?"

A. "That was construction. In the beginning we sold a lot of houses and we needed money for construction, and we took the 2 and a half million dollars toward construction." (Tr., pp. 160-162.)

When questioned by the Administrative Law Judge concerning the first loan on the properties, Mr. Steinberg testified as follows:

Q. "I just want a point of clarification on this. You took out a prior loan to purchase the property; is that true?"

A. "Yes."

Q. "So, you had a mortgage on the property?"

A. "We had no mortgage on the property."

Q. "You paid cash?"

A. "Right." (Tr., p. 163.)

Mr. Steinberg also testified that after the $9,000,000.00 loan was acquired, a second loan in the amount of $4,500,000.00 was obtained from National Westminster Bank and was collateralized with the assignment of sales contracts. Mr. Steinberg noted that this second financing was acquired in lieu of drawing down on the balance of the $9,000,000.00 loan

because the second loan avoided a mortgage tax, inspection fees and other expenses they would have incurred if they borrowed on the remainder of the Dime Savings Bank loan. Because the second loan was collateralized with the assignment of sales contracts and not with real property, petitioner saved money by avoiding the mortgage tax and inspection fees.

The Division's auditor disallowed two expenses as maintenance and repair expenses and rejected petitioner's claim that they represented capital improvement expenses. In response to the auditor's inquiries, petitioner identified an $18,500.00 expense for cleaning condo units prior to occupancy and a $139,980.00 expense for "glass breakage, brooms, paint and locksmith." Petitioner stated that the latter category included:

> "Vandalism Theft -- Appliances, Wiring, Plumbing, etc.
> Glass Breakage
> Punch list, paint touchup and general repairs
> Locksmith"

At hearing, Mr. Steinberg testified that these costs were incurred as part of the construction costs to prepare the units for sale. He stated that after units were constructed, the units were cleaned resulting in the $18,500.00 expense. He further testified that the $139,980.00 expense was incurred because of breakage and vandalism during the course of construction prior to the actual sale of the units. He testified that the units were not completely finished until prospective buyers obtained mortgage approval, at which point the units were completed according to a punch list that included touch-up paint, locksmith repairs, the installation of vanities and toilets, and repairs due to vandalism to walls, locks, wiring or glass in the units. This category also included the purchase of brooms to sweep the units.

The Division issued three notices of determination for the total amount of transfer gains tax due of $279,631.98, plus interest. One notice was dated August 22, 1991 for the tax periods ending February 3, 1988 through July 18, 1988 in the amount of $121,527.91, plus interest, for the total amount of $169,919.60. A second notice was dated October 15, 1991 for the tax periods ending July 19, 1988 through March 27, 1989 in the amount of $90,745.34, plus interest, for the

total amount of $122,714.05. A third notice was dated August 22, 1991 for the tax periods ending April 10, 1989 through May 30, 1991 in the amount of $67,358.73, plus interest, for the total amount of $75,355.73.

After a conciliation conference, the conferee issued a Conciliation Order, dated July 30, 1993, sustaining the statutory notices.

Sidan Realty Corp. filed a petition, dated October 18, 1993, asserting that it acquired the swim club for the purpose of acquiring the real property and not for the purpose of acquiring a swim club operation and that, therefore, the cost of the swim club should be allowed as part of the original purchase price. Petitioner also argued that the Division erred in disallowing "other various costs incurred which were attendant to the acquisition of petitioner's interest in real property (including the fees and costs to refinance the acquisition mortgage)."

The Division filed an answer, dated December 27, 1993, alleging, inter alia, that the costs to acquire the swim club were related to the purchase of an ongoing business and its goodwill and not to an interest in real property; and that petitioner had not met its burden of proving that the notices of determination were erroneous or improper.

Petitioner filed an amended petition, dated July 22, 1994, alleging overstatement of the consideration received. The Division filed an amended answer, dated August 11, 1994. By stipulation, dated September 13, 1994, the parties agreed that issues concerning the amount of consideration received that were raised in the amended petition were no longer being contested.

OPINION

In the determination below, the Administrative Law Judge visited Tax Law § 1441, Tax Law § 1440(3) which defines "gain" and reviewed the meaning under the statute of original purchase price along with the definition of real property, including 20 NYCRR 590.15, 590.16 and 590.17 which provide further descriptions and examples relating to "what constitutes acquisition costs and capital improvements that would reduce the 'gain' subject to tax" (Determination, conclusion of law "A").

The Administrative Law Judge then reviewed in great length:

(1) petitioner's contention that the sale contract makes it clear that the intent of the parties was to sell real property, including the pool, buildings and structures owned by the swim club, and not the business or goodwill; and

(2) the Division's contention that there were two contracts relating to the swim club, one providing for the sale of the land, including all buildings and improvements thereon, and a second contract providing for the sale of the business of the swim club.

As to these two contentions, the Administrative Law Judge, after discussing pertinent Tribunal decisions and court cases, held that:

(1) "it would have been helpful to have evidence concerning the relationship between the two apparently different but related sellers in these two contracts";

(2) "given the greater specificity of the swim club contract, which identified the improvements and structures sold, it would appear that part of the $1,500,000.00 purchase price was for real property related to the business";

(3) "there is insufficient evidence to draw any conclusion as to how to apportion the amount paid for the real property sold in the swim club contract (e.g., buildings, pool, etc.) and the amount paid for the business (including goodwill)";

(4) "[t]he swim club contract does not make any apportionments and Mr. Steinberg's testimony was insufficient to establish how this apportionment should be made";

(5) "[t]he $1,500,000.00 paid in accordance with the terms of the swim club contract included payment for the business which may not be included in the original purchase price"; and

(6) "[i]nasmuch as there is no basis upon which to determine the value of that business versus the value of any real property sold in that contract, no adjustment can be made to the $1,500,000.00 disallowance" (Determination, conclusion of law "A").

The Administrative Law Judge rejected petitioner's challenge relating to $10,662.00 in real estate taxes listed on the closing statements for the properties, holding that "there is no evidence in the record that the real estate taxes listed on the closing statement were unpaid taxes constituting a lien on the property or were reported as additional consideration to the seller" (Determination, conclusion of law "B").

The Administrative Law Judge, after reviewing the evidence before her, including case law, regulations, paragraph "H" of the commitment letter, as well as the testimony of Mr.

Steinberg, held that petitioner failed to carry its burden on the issue relating to a portion of petitioner's mortgage broker fee in the amount of $15,972.00 along with a mortgage commitment fee in the amount of $31,111.00 and, therefore, the Division was correct in disallowing these amounts on the ground that they were acquisition financing expenses.

With respect to petitioner's claim for an $18,500.00 cleaning expense and a $139,980.00 expense listed for "glass breakage, brooms, paint and locksmith," the Administrative Law Judge held that "[t]he Division correctly disallowed the cleaning expenses inasmuch as they do not relate to any capital improvements to the property (see, 20 NYCRR 590.17[b])," but held that "[a]t the hearing, Mr. Steinberg gave credible testimony to explain the nature of these expenses" and, therefore, "the $139,980.00 expenses are allowable inasmuch as they relate to capital improvements to the units prior to their initial transfer," and "they should be included as part of the original purchase price" (Determination, conclusion of law "D").

Both parties in the matter before us filed exceptions to the determination of the Administrative Law Judge.

On exception, petitioner, in requesting changes to the findings of fact and conclusions of law, argues that it should be entitled to include as part of the original purchase price for real property the $1,500,000.00 purchase price paid for the Brook Sun & Swim Club.

Petitioner also argues, in opposition to the Division's exception, that there is clear and convincing evidence to support the $139,980.00 in glass breakage, brooms, paint and locksmith expenses which should be allowed as capital improvement expenses.

The Division, while not filing a formal brief in opposition to petitioner's exception relating to the $1,500,000.00 issue, argues that the record fully supports the findings of fact and conclusions of law of the Administrative Law Judge on this issue and, as a result, the Division relies upon the determination of the Administrative Law Judge and its brief filed below.

The Division, on exception, also requested revisions to and additional findings of fact as well as revised conclusions of law relating to the $139,980.00 in expenses claimed by petitioner.

The Division argues that petitioner has failed to carry its burden of establishing that the $139,980.00 in expenses were associated with capital improvements and, further, under 20 NYCRR former 590.16(f), expenses which are incurred to repair and maintain the property in a condition of fitness, readiness and/or safety or to preserve such conditions are specifically excluded from original purchase price.

The Division argues that by their very nature the expenses for replacement of broken windows and locks constituted repair expenses which were clearly incurred to maintain the units in a condition of fitness, readiness and/or safety and since the regulations specifically exclude any expenses claimed for repainting, the "touch up" paint used to fix the "wear and tear" caused by vandals cannot be included in original purchase price.

The Division further argues that no evidence was presented to establish how the purchase of brooms qualifies as a capital improvement expense under the regulations and must, therefore, be excluded from original purchase price.

The Division also argues that petitioner has failed to provide any documentary substantiation for repairs to the walls and/or plumbing or to provide a breakdown of the $139,980.00 into its component parts and, thus, the entire amount must be disallowed. Since petitioner has also failed to provide any evidence which would indicate the proper apportionment of the $139,980.00 between sold and unsold units, the entire amount must be disallowed, even if some small amount of a valid capital improvement expense of the type above was included in it.

We first address petitioner's request for changes to the findings of fact and conclusions of law and its exception relating to the $1,500,000.00 paid in accordance with the terms of the swim club contract. We find that the Administrative Law Judge correctly analyzed and weighed all the evidence presented on this matter, accurately found the facts as established by the record and

correctly decided the issue. Therefore, we uphold the determination of the Administrative Law Judge on this issue for the reasons stated therein.

We next address the Division's request for revisions to and additional findings of fact along with a request for revised conclusions of law relating to the $139,980.00 in expenses (glass replacement, touch-up paint, brooms and locksmith repairs) claimed by petitioner. We reject such requests as the record supports those findings and conclusions reached by the Administrative Law Judge.

While the Division did not submit a brief on exception, a review of the Division's post-hearing response of January 6, 1995 states:

> "[i]n regard to the glass replacement, touch-up paint, brooms and locksmith repairs claimed by the petitioner, Mr. Steinberg testified that they were associated with fixing problems created by vandalism which occurred after the units had been constructed. (Tr. 143-44,172,173)" (Division's post-hearing response, p. 13).

The following is Mr. Steinberg's testimony on direct examination relative to the $139,980.00 in expenses:

> "Q. Now, you incurred during construction various types of expenses, and you heard testimony this morning on behalf of the Department relative to the disallowance of various types of expenses, and you were present for that testimony; weren't you?
>
> "A. Right.
>
> "Q. Annexed with part of the disallowance, there was a category of expenses called . . . glass breakage, brooms, touch-up paint, and locksmith repairs, $139,980. Now, could you delineate or could you explain what these expenses were and when they were incurred? What do they represent?
>
> "A. They were incurred during construction. Before people move in, we have to clean the apartments; and then due to building 184 units all at once, it takes time to build, and when you deliver some units, there is breakage and some vandalism, and you have to go back and fix it. It is all part of the cost of construction. It has nothing to do with maintenance, it's the cost of construction.
>
> "Q. How long did it take for you to build the 184 units, what period of time?

"A. Two, three years.

"Q. And during that time, if a unit that remained unsold, that they were building and remained fallowed, so to speak, offered for sale?

"A. Yes.

"Q. Were any complete, finished, and ready for sale, or was additional work necessary?

"A. No. We don't finish them completely. We sell them, we get people to get their mortgages approved, and then we go in and finish them.

"Q. When you described upon your submission to the Department in response to an inquiry of what was the $139,980 as glass breakage, brooms, touch-up paint and locksmith repairs --

"A. That's all part of the finishing of the units" (tr., pp. 143-145).

A review of the hearing transcript (pp. 172-173) relates to the Administrative Law Judge's questioning of Mr. Steinberg regarding the $139,980.00 in expenses, as well as a redirect examination wherein Mr. Steinberg testified that in getting the almost completed unit ready for sale they would also "paint it, to put the vanities in, the toilets in" (tr., p. 174). Further, the record is void of any examination of Mr. Steinberg by the Division regarding the $139,980.00 in expenses, either after his direct and redirect examination or even following his examination by the Administrative Law Judge.

On the issue of the $139,980.00 in expenses, we affirm the determination of the Administrative Law Judge who found that Mr. Steinberg gave credible testimony to explain the nature of the expenses. The credibility of witnesses is a determination within the domain of the trier of facts, the person who has the opportunity to view the witness first hand and evaluate the relevance and truthfulness of their testimony (see, Matter of Moss, Tax Appeals Tribunal, November 25, 1992; Matter of Jericho Delicatessen, Tax Appeals Tribunal, July 23, 1992; Matter of Spallina, Tax Appeals Tribunal, February 27, 1992). Although this Tribunal is not bound by the Administrative Law Judge's evaluation of a witness's credibility (Tax Law §

2006[7]; 20 NYCRR 3000.17[e][1]; Matter of Moss, supra; Matter of Jericho Delicatessen, supra), we find nothing in the record here which causes us to alter the determination of the Administrative Law Judge (cf., Matter of Wachsman, Tax Appeals Tribunal, November 30, 1995).

The Administrative Law Judge dealt fully and correctly with the issues and we affirm her determination for the reasons stated therein.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Sidan Realty Corp. is denied;

2. The exception of the Division of Taxation is denied;

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

4. The petition of Sidan Realty Corp. is granted as indicated in conclusions of law "D" and "E" of the determination of the Administrative Law Judge and is in all other respects denied; and

5. The three notices of determination dated August 22, 1991 and October 15, 1991, as modified by the Administrative Law Judge, are sustained.

DATED: Troy, New York
May 16, 1996

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

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

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