

STATE OF NEW YORK
TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
CHANDRU JAGWANI	:	DECISION
	:	DTA No. 813400
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 Chandru Jagwani, 35 Aldgate Drive East, North Hills, Manhasset, New York 11030, filed an exception to the determination of the Administrative Law Judge issued on July 18, 1996. Petitioner appeared by Robinson Brog Leinwand Greene Genovese & Gluck P.C. (Babcock MacLean, Esq., of counsel). The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (Herbert M. Friedman, Jr., Esq., of counsel).

Petitioner filed a brief in support of his exception and a reply brief. The Division of Taxation filed a brief in opposition. Petitioner's request for oral argument was denied.

Commissioner Jenkins delivered the decision of the Tax Appeals Tribunal. Commissioner Pinto concurs. Commissioner DeWitt took no part in the consideration of this decision.

ISSUES

I. Whether the Division of Taxation, in calculating consideration for the transfer of a certain interest in real property, properly included the face value of a purchase money mortgage despite the fact that the mortgage subsequently became valueless.

II. Whether the imposition of gains tax on petitioner, when he has not realized any economic gain, violates his constitutional rights to equal protection.

FINDINGS OF FACT

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

forth below.

On May 19, 1986, petitioner, Chandru Jagwani, as purchaser, contracted with Port Jeff Development Corp., as seller, for the purchase of real property located at Old Town Road, Route 347, in Port Jefferson Station, Suffolk County. Petitioner agreed to purchase this subdividable and apparently unimproved Long Island property at a purchase price of \$6,375,000.00. There is nothing in the record that discloses the names of the principals behind Port Jeff Development Corp. or to what extent this transaction was, in fact, at arm's length. Petitioner's contract with this entity was not made a part of the record.

More than a year later, rather than closing on the property, petitioner assigned his contract rights to an individual identified as Lawrence Hahn. According to a statement attached to the transferor's questionnaire dated October 20, 1987 filed by petitioner, which was marked into the record as the Division of Taxation's ("Division") Exhibit "I", petitioner "[o]n August 31, 1987 . . . executed a contract with Lawrence Hahn for the assignment of the contract for a total price of \$8,075,000.00." This contract of assignment also was not submitted for review. The statement attached to the questionnaire further disclosed that Mr. Hahn "assigned his contract for no consideration to Port Jeff Developers." Mr. Hahn's assignment of his contract with petitioner to Port Jeff Developers, in consideration of the sum of \$1.00, is attached to the transferee questionnaire dated October 8, 1987 of Port Jeff Developers, which was marked into the record as the Division's Exhibit "J". This transferee questionnaire discloses that Lawrence Hahn was a partner of Port Jeff Developers. Both the petitioner's transferor and Port Jeff Developers' transferee questionnaires report a date of anticipated transfer of December 15, 1987. However, the transfer apparently did not take place until February 1989. There is nothing in the record to explain this 14-month delay.

A real property transfer gains tax supplemental return dated February 14, 1989 filed by petitioner, which was marked into the record as the Division's Exhibit "K", reveals that Port Jeff Developers was a "co-partnership". Petitioner in an amendment to his agreement with

Lawrence Hahn, which is an attachment to this supplemental return, noted his consent to the assignment of his agreement with Mr. Hahn "to a partnership, one of whose partners shall be a corporation of which Lawrence Hahn and/or Robert Feldman and/or members of their immediate families, or their spouses, own all of the issued and outstanding stock."

On his transferor questionnaire dated October 20, 1987, petitioner reported anticipated real property transfer gains tax due of \$118,720.00 on a gain subject to tax of \$1,187,204.00, which was computed as follows:

Gross consideration to be paid for transfer by Port Jeff Developers, as transferee	\$8,075,000.00
Less: Brokerage fees to be paid by transferor	484,500.00
Consideration	<u>\$7,590,500.00</u>
Purchase price paid to acquire property	\$6,375,000.00
Other acquisition costs	10,000.00
Cost of capital improvements	3,296.00
Attorneys fees	<u>15,000.00</u>
Original purchase price	\$6,403,296.00
Gain subject to tax (Consideration less original purchase price)	\$1,187,204.00

Petitioner filed the real property transfer gains tax supplemental return dated February 14, 1989 in order to elect to pay the gains tax reported due of \$118,720.40 in installments on the basis that no part of the consideration to be received by petitioner, on or before the date of transfer of the real property, was cash consideration. As a result, petitioner chose to defer payment of the gains tax reported due of \$118,720.40. By a letter dated April 10, 1989, which was marked into the record as petitioner's Exhibit "8", petitioner's election to pay the gains tax due in installments was accepted by the Division.

Petitioner paid a first installment of \$39,573.46 of the total gains tax reported due of \$118,720.40 in February 1990, which was one year after the closing. Two years after the closing, in February 1991, petitioner paid a second installment of \$39,573.46.

Subsequently, the Division issued a Statement of Proposed Audit Changes dated May 4,

1992 against petitioner, which was marked into the record as petitioner's Exhibit "2", asserting gains tax due of \$39,573.46 plus penalty and interest for the following reason:

"Our records indicate that on 02/14/92 an installment of the gains tax was due under plan number I-878. Section 1442 of the Tax Law provides that 'if the transferor shall fail to pay any installment on the date on which it is due . . . the entire balance of the tax is due and owing'."

Petitioner responded quickly to the Division's Statement of Proposed Audit Adjustment by noting his disagreement with the assertion of tax due in his own statement dated May 13, 1992, which was attached to a payment document he filed with the Division, and which was marked into the record as petitioner's Exhibit "3". In this statement, petitioner requested a refund of the first two installment payments:¹

"The transaction relating to the above assessment closed on February 14, 1989 and concerned the assignment of a contract of sale by [petitioner] to Port Jeff Developers (which in turn assigned the contract to an entity known as House Beautiful at Port Jefferson).

The Tentative Assessment and Return originally provided for a Transfer Gains Tax of \$118,720.40. On the date of the closing a supplemental return . . . was completed and filed indicating that no payment was due on the closing date by reason of the amendment of the contract of sale providing for the major portion of the purchase price to be paid by way of a purchase money mortgage² in lieu of cash. On April 10, 1989, this was accepted by the Department, with a

¹The Division withdrew its contention, which was affirmatively asserted in its answer, that petitioner failed to file a timely refund claim.

A copy of this purchase money mortgage was not made a part of the record. Neither was a copy of the note, which was secured by the mortgage, made a part of the record. It is observed that in its answer, the Division affirmatively stated that "at the time of transfer of this property, a note secured by a purchase money mortgage in the face amount of \$1,500,000.00 was given by the transferee to the petitioner and formed part of the consideration received by the petitioner." Attached to the real property transfer gains tax supplemental return is a copy of an amendment dated November 30, 1988 to the agreement between petitioner as assignor and Port Jeff Developers as assignee which described how the "balance on closing of title" would be paid as follows:

"[B]y execution and delivery of a purchase money third mortgage payable three (3) years from the closing of title with interest at the rate of ten (10%) percent per annum payable quarterly. Said mortgage and note shall be drawn on the standard form of New York Board of Title Underwriters."

stipulation for payment of tax in installments over a period of not more than three years.

The first installment of the tax was paid one year after the closing, in February 1990, and the second two years after the closing, in February 1991. The payment requested at this time is for the third and final installment, together with interest [sic] and penalties.

Payment of this installment is strenuously objected to, since no money has been received on account of the principal balance of the mortgage at all. In fact, it is questionable as to whether [sic] any money will ever be received. By its terms, the mortgage principal was due and payable on February 14, 1992. It has not been paid. Moreover, it is subordinate to a first mortgage held by Port Jeff Development Corp. in the amount of \$3,360,000 which is in default and on which foreclosure proceedings have been instituted and are presently pending

In the circumstances I do not believe that I am responsible for the payment of any tax, which is a 'gains tax' since the circumstances are that I have made no gain on the assignment of the contract. In addition, the first two installment payments which I made should be refunded to me. . ." (emphasis in original).

In response to petitioner's statement of disagreement, the Division, by a letter dated June 19, 1992, which was marked into the record as petitioner's Exhibit "4", sent petitioner a form TP-165.8 for completion so he could formalize his refund claim. Petitioner completed the form to which he attached his statement of disagreement cited above, and eventually, by a letter dated May 4, 1993, which was marked into the record as the Division's Exhibit "G", the Division denied petitioner's refund claim because:

"No error was made at the time the tax was paid because the consideration paid or required to be paid was \$8,075,000.

The tax was properly calculated at that time.

Since the tax is due on the date of transfer, there was no erroneous payment made at the time the tax was paid. Therefore, the refund must be denied in its entirety" (emphasis in original).

In an affidavit of petitioner dated November 15, 1995, which was marked into the record as petitioner's Exhibit "7", petitioner explained that the transaction at issue soured:

"2. Due to the decline of the real estate market, the Property could not be developed successfully by Buyer [Port Jeff Developers].³ The Property was to consist of 170 residential units. However, only 10 units were partially completed by Buyer, and none were sold by Buyer. At the present time, the estimated fair market value of the Property is approximately 20% of its value at the time of the transfer by me to Buyer.

3. The second⁴ mortgage held by me was by its terms due and payable on February 14, 1992. It has not been paid. Moreover, it is subordinate to a first mortgage held by Port Jeff Development Corp. in the amount of \$3,360,000, which is in default and on which foreclosure proceedings were instituted. As the holder of the junior mortgage, I was named as a defendant in this action. . . . Subsequently, the Property has been foreclosed by the first mortgagee. The fair market value of the Property is less than the amount of the first mortgage. Therefore, there has not been and there will not be any payment made to me on account of my second mortgage. I have not realized and will not realize a gain on the transaction" (emphasis in original).

OPINION

In his determination, the Administrative Law Judge concluded that gains tax has been imposed in situations of speculative profit and in situations where real estate transactions have soured. The Administrative Law Judge noted that arguments similar to petitioner's were rejected in Matter of Brockman (Tax Appeals Tribunal, April 4, 1996). Further, the Appellate Division has sustained the conclusion that the amount of gains tax due is finally determined by the amount of consideration paid or required to be paid on the date of the transfer (see, Matter of Wanat v. Tax Appeals Tribunal, 224 AD2d 873, 638 NYS2d 251, lv denied 88 NY2d 803, 645 NYS2d 446, confirming Matter of Wanat, Tax Appeals Tribunal, September 15, 1994; Matter of South Suffolk Recreation Ventures v. Tax Appeals Tribunal, 224 AD2d 874, 638 NYS2d 515, lv denied 88 NY2d 803, 645 NYS2d 446, confirming Matter of South Suffolk

³It is unknown why petitioner referred to Port Jeff Developers as the entity which could not successfully develop the property at issue since, as noted above, the ultimate assignee of the contract to purchase the Port Jefferson Station property was House Beautiful at Port Jefferson.

⁴As noted above, petitioner held "a purchase money third mortgage" on the property. This discrepancy was not explained in the record.

Recreation Ventures, Tax Appeals Tribunal, November 3, 1994).

The Administrative Law Judge rejected petitioner's contention that the amendment of the gains tax law in 1993, which deemed "consideration" to be limited to the fair market value of the property transferred to a lender in foreclosure proceedings, means that gains tax may be imposed only on an actual gain. The Administrative Law Judge concluded that the Legislature has manifested no intent to ignore a transaction for purposes of gains tax due to subsequent events given the broad definition of "transfer of real property" in Tax Law § 1440(former [7]). The Administrative Law Judge found that while the real property transfer gains tax is not viewed as a stamp tax, but rather as a tax on income in the context of bankruptcy litigation, the fact that gains tax due is calculated at the time of transfer and may not be reduced by subsequent events does not mean that it is not "a tax on or measured by income or gross receipts." Finally, the Administrative Law Judge rejected petitioner's argument that, by holding him liable for gains tax on a transaction that later soured, his right to equal protection of the law is violated, relying again on the decision of this Tribunal in Matter of Brockman (*supra*).

On exception, petitioner argues that denying his refund claim "is contrary to the Tax Law and to basic principles of fairness and common sense" (Petitioner's Brief in Support, p. 1). According to petitioner, "the gains tax is imposed only upon actual economic gain" (Petitioner's Brief in Support, p. 8). He supports this statement by citing to "litigation in the bankruptcy context" where the gains tax has been viewed not as a stamp tax but rather as a tax measured by income, or a tax imposed on economic gain. He also cites to the amendment of the gains tax law in 1993 which deemed "consideration" to be limited to the fair market value of the property transferred to a lender in foreclosure proceedings or a transfer in lieu of foreclosure. Further, petitioner maintains that to tax a real estate transaction even where gain is not derived is defective under the Equal Protection Clause.

The Division, in opposition, argues that in computing consideration the face amount of a

mortgage at the time of transfer is properly used, citing the Tax Appeals Tribunal decision in Matter of Normandy Assocs. (Tax Appeals Tribunal, March 23, 1989). Subsequent events which may effect the transferor's actual receipt of a gain are irrelevant. The Division also points out that the Tax Appeals Tribunal rejected an equal protection argument, similar to the one made by petitioner, in Matter of Rapoport (Tax Appeals Tribunal, August 31, 1995, confirmed Matter of Rapoport v. Koenig, ___ AD2d ___ [Mar. 20, 1997]).

In his reply brief on exception, petitioner maintains that, in the cases cited by the Division in its brief, the Tax Appeals Tribunal did not address the situation where a seller of real property has been taxed on a gain which he did not receive because the purchase money mortgage he held was worthless.

We affirm the determination of the Administrative Law Judge. Each of the issues raised by petitioner on exception were presented to and considered by the Administrative Law Judge. After reviewing all the evidence presented in this case, we find that the Administrative Law Judge correctly and adequately addressed these issues in his determination and we affirm his determination for the reasons stated therein.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Chandru Jagwani is denied;
2. The determination of the Administrative Law Judge is affirmed;
3. The petition of Chandru Jagwani is denied; and

4. The refund denial, dated May 4, 1993, is sustained.

DATED: Troy, New York
April 17, 1997

/s/Carroll R. Jenkins
Carroll R. Jenkins
Commissioner

/s/Joseph W. Pinto, Jr.
Joseph W. Pinto, Jr.
Commissioner