STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
EVELYN REYNOLDS, PAUL BOGONI, CHARLOTTE KELLY AND THOMAS URICH	:	DETERMINATION DTA NO. 810628
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.	:	

Petitioners, Evelyn Reynolds, Paul Bogoni, Charlotte Kelly and Thomas Urich, 340 Riverside Drive, New York, New York 10025, filed a petition 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.

A hearing was held before Marilyn Mann Faulkner, Administrative Law Judge, at the offices of the Division of Tax Appeals, Riverfront Professional Tower, 500 Federal Street, Troy, New York, on March 24, 1993 at 1:15 P.M., with all briefs and documents due on October 12, 1993. Petitioners, represented by Solomon I. Glushak, Esq., filed a brief on August 3, 1993. The Division of Taxation, represented by William F. Collins, Esq. (Kenneth J. Schultz, Esq., of counsel), filed a brief on September 14, 1993 and petitioners filed a reply brief on October 12, 1993.

ISSUES

I. Whether the sales of shares pursuant to a cooperative conversion plan are subject to real property transfer gains tax when the building was conveyed to the cooperative housing corporation prior to the effective date of Article 31-B but the sales were made after the effective date of Article 31-B.

II. Whether the sales of shares pursuant to the cooperative conversion plan, prior to the 1984 amendments to Tax Law §§ 1440.7 and 1442 and prior to the 1984 promulgation of regulations, are subject to gains tax.

III. Whether the sales of shares are subject to gains tax when petitioners furnished a sworn statement that the cooperative conversion plan was not conceived for the purpose of avoiding gains tax.

IV. Whether the Division of Taxation erred in its calculation of "gain" by (a) failing to step-up the original purchase price to the value of the property at the time the building was conveyed to the cooperative corporation; (b) failing to use the value, rather than the face value, of a wraparound mortgage in computing consideration; (c) failing to follow its own guidelines in computing estimated consideration for unsold shares; (d) failing to include an estimated broker's fee of 6% on future sales in calculating estimated consideration; and (e) failing to include a flip tax paid by petitioners into the reserve fund.

V. Whether gains tax was due on the sale of shares with respect to four units on the ground that the sales contract did not provide for the transfer of shares until completion of installment payments in 1993.

VI. Whether penalties and interest should be disallowed because no regulations were in effect at the time of the transfers of certain shares.

FINDINGS OF FACT

In 1975, the four petitioners purchased as tenants in common an apartment building containing 63 apartments at 340 Riverside Drive, New York, New York. The respective ownership interests of petitioners were as follows:

Paul Bogoni - 56%
Evelyn Reynolds - 26%
Thomas Urich - 9%
Charlotte Kelly - 9%

As a result of litigation brought on by Evelyn Reynolds against the three other tenants in common, the parties agreed to settle their differences by selling the apartment building.

On January 20, 1983, petitioners conveyed the building to a cooperative corporation pursuant to a cooperative conversion plan the first offering of which occurred on March 31, 1981. Under the cooperative Offering Plan, a total of 79,990 shares[1] was allocated to the 63

[1]In the answer to petitioners' petition, the Division of Taxation ("Division") admitted that the total number of shares was 79,990. However, the Division's attachment sheet to the Notice of

apartments.

According to petitioners' petition, at the January 20, 1983 closing, 41 apartments and 51,110 shares were sold leaving 22 unsold apartments and 28,880 unsold shares. On or about August 1, 1983, petitioners entered into an agreement dividing their interests as sponsors of the cooperative plan in the unsold apartments and shares.

Petitioners sold apartments 2A and 12D on April 3, 1984 and March 20, 1984, respectively. Petitioners' respective interests in the two apartments at the time of the sales were as follows: Paul Bogoni, 56%; Evelyn Reynolds, 26%; Thomas Urich, 9%; and Charlotte Kelly, 9%. Petitioners Paul Bogoni and Thomas Urich sold apartment 6D on March 5, 1986. Paul Bogoni had an 86% interest and Thomas Urich had a 14% interest in that apartment. Apartments 13B, 11C, 14C and 10D, owned 100% by Evelyn Reynolds, were sold on January 1, 1985. Petitioners did not pay real property gains tax at the time of the sale of these seven apartments.

According to petitioners' petition, the seven apartments represented a total of 9,230 shares.

By letters dated October 21, 1988 to petitioners c/o Sonnenschein, Sherman and Deutsch and to petitioners' attorney, Solomon Glushak, the Division informed petitioners that the records at the New York Department of Law indicated that aggregate consideration in excess of $1,000,000.00 would be received for a cooperative conversion plan with respect to 340 Riverside Drive and that it had no record of receiving the statutory filing for such transfers. The Division requested petitioners to file the appropriate questionnaires and to provide a copy of the offering plan along with all amendments. The Division requested a reply within 20 days.

By letter dated December 14, 1988, the law offices of Sonnenschein, Sherman and Deutsch informed the Division that because the premises were converted to cooperative ownership prior to the effective date of the gains tax law, no filings were made at that time. The

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Determination at issue calculated tax based on the total project shares at 79,910. The Offering Plan contained a pencilled line through the typed amount of 79,910 shares over which was written in pencil the amount of 79,990. In their brief, petitioners state that the correct number of 79,990 shares is not in dispute.

letter also suggested that if the Division needed further information, it should contact Solomon Glushak, the attorney for the sponsor of the conversion.

By letter dated January 13, 1989, the Division advised Mr. Glushak that the transfer of shares pursuant to a cooperative plan triggers the payment of the gains tax rather than the transfer of the property to the cooperative corporation. The Division again requested that certain documents, including a list of all units contracted for and sold after March 28, 1983, be submitted to it within 20 days.

By letter dated February 27, 1989, the Division informed Mr. Glushak that it had not received the information requested in its January 13 letter. The Division advised as follows:

> "This letter is to advise you that interest and penalty continues to accrue on any tax due and that section 1444 of Article 31-B provides in part that when a form required by Article 31-B is not filed, the amount of tax due shall be determined by the Commissioner of Taxation and Finance from any records or information obtainable.
>
> "Accordingly, failure to reply to our letter within 10 days from the date of this letter may result in the issuance of a Proposed Statement of Audit Changes for any Real Property Gains Tax that might be due, together with full penalties and interest as authorized by Sections 1444 and 1446 of Article 31-B of the Tax Law."

By letter dated March 1, 1989, Mr. Glushak indicated that he enclosed copies of the offering plan, all 11 amendments and closing statement. He also stated the following:

> "It is my understanding that because this plan was consummated and the property conveyed prior to the effective date of the statute providing for the gains tax, that no gains tax is due."

The Division sent a Statement of Proposed Audit Adjustment, dated July 14, 1989, to petitioners asserting tax due in the amount of $1,719,200.00, plus $1,522,114.00 in interest and $601,720.00 in penalty, for the total amount of $3,843,034.00. The Division provided the following explanation of the adjustment:

> "Since you have failed to respond to our requests for additional information of January 13, 1989 and February 27, 1989, your Real Property Gains Tax liability has been computed based on the best information available at this time. Tax period beginning date: 3/29/83."

By letter dated July 19, 1989, Mr. Glushak contacted the Division and stated the following:

> "This letter is in response to your 'statement of proposed audit adjustment', which I received today -- as quite a surprise.

"Enclosed is a copy of my letter to your department of March 1, 1989, -- with which I mailed a copy of the offering plan, amendments and the closing statement prepared by the attorneys who handled the matter. My letter explained that the property concerned was sold on January 20, 1983 and, therefore, is not subject to the gains tax.

"I am again enclosing copies of the offering plan, the amendments and the closing statement.

"Please review the enclosures and get back to me so that this matter can be straightened out."

In response to the July 19 letter, the Division wrote a letter, dated August 3, 1989, to Mr. Glushak referring him to Tax Law § 1442 and section 590.33 of the tax regulations advising him as follows:

"If the aggregate cash consideration paid by the tenant/purchasers for the units contracted for after March 28, 1983, plus the amount of unpaid mortgage indebtedness apportioned to such units is $1,000,000 or more, transfer gains tax may be due.

"Based on these facts, if the consideration for the cooperative units within this project will equal $1,000,000 or more, the following information must be submitted:

"1) Copy of offering plan and all amendments.

"2) List of all units contracted for and sold after March 28, 1983, including closing dates and cash consideration.

"3) Completed DTF 700 forms, including contract of sales and closing statement for sponsors original acquisition and brokers statement.

"4) Transferors Employer Identification Number or Social Security Number."

The Division also stated that all referenced information must be submitted within 20 days of the date of the August 3 letter.

By letter dated November 1, 1989, the Division sent a copy of a Supreme Court decision, Matter of Mayblum v. Chu (Sup Ct, Queens County, May 11, 1984, Graci, J.), to Mr. Glushak. The Division noted that the case discussed the issue of when a taxable event occurred with respect to cooperative conversions. The letter also contained the following statement:

"Also enclosed is a copy of my August 3, 1989 letter outlining the items that must be submitted to this office. A submission of the 700 forms and schedules of all shares sold since 3/29/83 and a schedule of unsold shares is requested by November 24, 1989."

The Division sent to petitioners a Notice of Determination, dated June 25, 1990, asserting tax due for the period ended April 1, 1983 in the amount of $879,257.91, plus $958,499.04 in interest and $307,740.16 in penalties, for the total amount of $2,145,497.11; and tax due for the period ended March 5, 1986 in the amount of $34,951.49, plus $17,174.17 in interest and $12,232.89 in penalties, for the total amount of $64,358.55. Attached to the notice was the following explanation for the amount of tax due:

"The following figures have been used in calculating Gains Tax for the cooperative project located at 340 Riverside Drive, NYC.

Total project shares	79,910		
	22,150 - sold prior to 3/83		
	30,080 - sold post 3/83		
	27,680 - unsold		
Consideration (28,930 shrs @ $116 p/s)		$3,355,880	
(1,150 shrs @ $300 p/s)		345,000	
Estimated consideration (27,680 shrs @ $6500 p/s)		13,840,000	
Mortgage ($1,350,000 allocated to 57,760 shrs)		975,798	
			$18,516,678
Less: Reserve fund ($125,478)			(90,697)
Less: Original Purchase Price (alloc. to 57,760 shrs)			
Purch. Price to Acquire ($671,500)	$485,369		
Capital Improvements ($533,780)	385,823		(871,192)
Gain			$17,554,789
Tax			$1,755,478.90
Tax per share	$30.3926		
Tax on 30,080 shares		$914,209.40"	

By letter dated November 27, 1990, the Division recalculated the amount of tax due after discussions with Mr. Glushak. With respect to the sale of units 12D and 2A, the Division set forth the following calculations of tax due:

"Paul Bogoni	Evelyn Reynolds	Thomas Urich	Charlotte Kelly
56%	26%	9%	9%
Units	Shares	Consideration	
12D	1,330	$230,000	
2A	1,260	255,000	
	2,590	$485,000	

Consideration		$485,000
Mortgage $1,350,000 allocated to 2,590 shrs[2]		43,712
		528,712
Brokerage		(29,100)
Reserve fund $150,000 allocated to 2,590 shrs		(4,857)
OPP $1,199,419 allocated to 2,590 shrs	(38,835)	
Gain		$455,920
Tax due - 10%		$45,592
Tax per share $17.6030		

Paul Bogoni	- 56% interest =	$25,531.52
Evelyn Reynolds	- 26% interest =	$11,853.92
Thomas Urich	- 9% interest =	$4,103.28
Charlotte Kelly	- 9% interest =	$4,103.28
		$45,592.00"

With respect to the sale of units 10B[3] and 6D, the Division calculated the amount of tax due based on Paul Bogoni's and Thomas Urich's ownership interest in certain units as follows:

"Paul Bogoni 86%	Thomas Urich 14%	
Units	Shares	Consideration
9A	1,470	
14A	1,620	
10B	1,440	$535,000
11B	1,470	
6C	1,000	
8C	1,040	
12C	1,330	
15C	1,420	
1D	1,000	
11D	1,300	

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[2] The Division calculated the allocation based on the total number of shares in the cooperative building which totalled 79,990.

[3] Unit 10B was sold on November 18, 1990, subsequent to the issuance of the Notice of Determination. Therefore, the amount of tax calculated with respect to unit 10B ($18.5534 x 1,440 shares = $26,716.90) and the tax payment of $14,628.52 relates to a unit not covered by the notice challenged in this petition. However, the actual sale price of unit 10B does effect the tax per share due with respect to unit 6D.

14D	1,390	
15D	1,420	
6D	1,150	308,000
	17,050	$843,000

Consideration (2,590 shrs)	$843,000	
Estimated Consid - $843,000 / 2,590 x 50% x 14,460 shrs		2,353,239
Mortgage $1,350,000 allocated to 17,050 shrs		287,775
		3,483,994
Buyout		(15,000)
Brokerage		(18,000)
Reserve fund $150,000 allocated to 17,050 shrs		(31,973)
OPP $1,199,419 allocated to 17,050 shrs		(255,658)
Gain		$3,163,363
Tax		$316,336.30
Tax per share $18.5534		
Tax on 2,590 shares	$48,053.30	
Tax paid on Unit 10B	14,628.52	
Balance Due	33,424.78	

Paul Bogoni - 86% interest =	$28,745.31
Thomas Urich - 14% interest =	4,679.47
	$33,424.78"

In the letter, the Division explained the method used for calculating estimated consideration in the above calculations as follows:

> "The method used to compute estimated consideration is pursuant to procedures established by this Department for valuing unsold shares. This is further explained in the attached memo (TSB-M-86-(3)-R), Safe Harbor Estimate for Transfers Pursuant to Condominium and Cooperative Plans. Basically, in this particular case, the Department allows an estimate of 50% of vacant market value or 100% of the latest offering plan price. (For Bogoni and Urich, vacant sales have occurred, so it is possible to estimate the unsold shares at 50% vacant market value. For Reynolds and Kelly, vacant sales have not occurred, so 100% of the latest offering plan price has been used. The latest offering plan price is $500 per share, as stated in the Eleventh Amendment).
>
> "The taxpayers may elect to not file pursuant to safe harbor, in which case they may value the unsold shares based on their reasonable estimate. However, if the shares should actually be sold at higher than estimated, the taxpayer will be subject to penalty and interest. If the taxpayer chooses to not file pursuant to safe harbor, a written statement to that effect is to be provided to this department."

With respect to the sale of units 13B, 11C, 14C and 10D, the Division recalculated the amount of tax due as follows:

"Evelyn Reynolds
100%

Units	Shares	Consideration
13B	1,530 }	
11C	1,300 }	$467,200

14C	1,390 }	
10D	1,270 }	
13D	1,360	
	6,850	$467,200
Consideration	$467,200	
Estimated Consid - 1,360 shrs @ $500 per shr, per 11 Amend		$680,000
Mortgage $1,350,000 allocated to 6,850 shrs		115,608
		1,262,808
Brokerage		0.00
Reserve fund $150,000 allocated to 6,850 shrs		(12,845)
OPP $1,199,419 allocated to 6,850 shrs		(102,713)
Gain		$1,147,250
Tax		$114,725
Tax per share $16.7481		
Tax on 5,490 shares		$91,947.06"

Taking into account these recalculations, but excluding the tax on unit 10B ($26,716.90), which was not covered by the Notice of Determination, and excluding the tax paid on the sale of unit 10B ($14,628.52), the total amount of tax due for the units covered by the Notice of Determination was $158,875.47.

After a conciliation conference, the conferee issued a Conciliation Order, dated December 27, 1991, recomputing the tax deficiency to $138,564.00,[4] plus penalty and interest. In the order, it was noted that "[p]ayments totalling $116,745.00 have been applied to this assessment."

Petitioners filed a petition, dated March 22, 1992, arguing, inter alia, that (1) because the building was conveyed to the cooperative corporation prior to the effective date of Article 31-B, no gains tax was due on the sale of the units; that (2) no gains tax was due on units sold prior to September 24, 1985, which was the effective date of the regulations concerning the projected sales of unsold shares or their evaluation, because all sales prior to that date did not add up to $1,000,000.00; that (3) units sold prior to September 4, 1984, the date section 1440.7 was amended, are not subject to gains tax; that (4) the Division incorrectly determined the original purchase price to be $14.99 per share rather than $61.87 per share; and that (5) the Division

[4]This amount does not correspond to the Division's recalculation of tax due ($158,875.47) (see, Finding of Fact "16"). The record contains no explanation as to how the conferee recomputed the tax due.

failed to allow legal fees, closing fees and full contribution to reserve fund with respect to the sales of units 12D and 2A.

The Division filed an answer, dated June 16, 1992, affirmatively stating, inter alia, that the Division made available to the public Publication 588 which explained the treatment of transfers by a cooperative corporation; that the transactions in question were subject to gains tax; that the 1984 amendment merely amplified the Legislature's intent and did not change the taxability of transfers of cooperative shares; and that petitioners bear the burden of proving error on the part of the Division.

At the hearing held on March 24, 1993, the parties agreed that the case primarily involved legal issues and that they would submit the case on the evidence, without testimony, and attempt to reach a stipulated agreement on the facts. Petitioners also moved to amend their petition to provide recalculations of the gains tax due and to claim that "gains tax is not owed because the co-op plan was not designed as a scheme to evade gains tax." In support of this claim, petitioners attached to the amended petition an affirmation by their attorney, Solomon P. Glushak, stating that he was personally familiar with the cooperative plan and that "the purpose of the Plan conversion to a co-op was in no way intended by the petitioners or any of them as a scheme to avoid the New York State Real Property Gains Tax." Petitioners also made an oral motion to amend further their petition to recalculate the tax to include potential broker's commissions of 6% for selling unsold units in the future.

At the hearing, the parties were given until April 28, 1993 to review petitioners' proposed calculations and to submit a stipulation of facts. In the event the parties did not stipulate to facts, the record was left open until April 28, 1993 to submit any further documentation in support of their respective positions. The April 28, 1993 date was extended until May 28, 1993.

On May 28, 1993, the Division submitted to the Division of Tax Appeals amendments to the Offering Plan, Transferor/Transferee Questionnaires and attachments, and an affidavit by Peter Van Buren explaining the audit adjustments in the case. The Division's counsel also stated in the cover letter to the Division of Tax Appeals that on May 20, 1993 he faxed a copy

of Mr. Van Buren's affidavit to Mr. Glushak and requested that he send to the Division a proposed stipulation. The Division's counsel noted that as of May 28, 1993 he had not received a response to that request.

In his affidavit, Mr. Van Buren explained the Division's computation of consideration, estimated consideration, proportionate share of mortgage, reserve fund, and original purchase price as follows:

> "(a) The consideration figure used was the actual consideration received [see DTF-700 series and transferor/transferee questionnaires].
>
> "(b) Estimated consideration was computed by using the guidelines set forth in TSB-M-86-(3)-R.
>
> "(c) The proportionate share of the mortgage encumbering the property was computed by dividing the principal balance of the wraparound mortgage, $1,350,000, by the total number of shares, 79,990, and multiplying the resulting number by the number of shares sold [see p. 5, Third Amendment].
>
> "(d) The amount of the Reserve Fund apportioned to the unit sales, $150,000, was derived from the Seventh Amendment to the Offering Plan. The apportionment is computed by dividing the amount of the Reserve Fund, $150,000, by the total number of shares, 79,990, and multiplying the resulting number by the number of shares sold.
>
> "(e) The original purchase price, $1,199,419.00, was computed by adding the following component costs:
>
> - purchase price to acquire: $ 902,900.
> - acquisition: $ 3,646.
> - capital improvements: $ 82,190.
> - conversion: $ 210,683.
>
> Total OPP $1,199,419.00"

With respect to units 12D and 2A, Mr. Van Buren set forth the same calculations contained in the Division's recalculations contained in the November 27 letter (see, Finding of Fact "16"). Similarly, with respect to units 10B and 6D, owned by petitioners Bogoni and Urich, Mr. Van Buren explained the estimated consideration used to calculate the tax per share as follows:

> "Units 10B and 6D were transferred vacant. Accordingly, pursuant to TSB-M-86-(3)-R, the Safe Harbor estimate of consideration was computed at 50% of the vacant market value of the unsold units. The calculation is as follows:
>
> Actual consideration for sales of units 10B and 6D: $\frac{\$843,000.}{2,590} = 325.4826$
> Number of shares sold

325.4826 x 14,460 unsold shares x 50% = $2,353,239.00."

Mr. Van Buren's calculation of tax due by Evelyn Reynolds for the sale of units 13B, 11C, 14C and 10D differed from that contained in the Division's November 27, 1990 letter because he considered the actual sale price of unit 13D, which sold in March of 1992 for $325,000.00. Mr. Van Buren set forth the calculation for the five units owned 100% by Evelyn Reynolds as follows:

"Units 13B, 11C, 14C, 13D and 10D - 6850 shares

Consideration:	$792,200.00	
Mortgage:	$115,608.00	
Working Capital/Reserve	($12,845.00)	[150,000 x $\frac{6,850}{79,990}$]
OPP	($127,875.06)[5]	

5

Gain	$767,087.94
Gains Tax	$76,708.79"

From these calculations, the tax per share should be $11.19836, as opposed to the calculation of the tax per share ($16.7481) contained in the November 27, 1990 letter for units 13B, 11C, 14C and 10D.

On August 3, 1993, the Division of Tax Appeals received an application by petitioners to further amend their petition, inter alia:

> "to incorporate their revised determinations of taxes which were made, they claim, pursuant to the Tax Commission guidelines identified in its answer as the basis for the Tax Commission's determinations, . . . to allege that Evelyn Reynolds was not liable for any taxes on the sale of Apts. 13B, 11C, 14C and 10D prior to their transfer in 1993, . . . [and] to deny any gains tax liability because the Plan and apartment sales were not pursuant to an agreement or plan to avoid the gains tax."

Petitioners also requested:

> "a hearing, if it is necessary, to put in testimony and further evidence to support petitioners' claim that the Plan and apartment sales were not pursuant to an agreement or plan to avoid the gains tax."

SUMMARY OF THE PARTIES' POSITIONS

Petitioners argue that (1) because the purpose of the cooperative plan was to settle certain disputes among petitioners and not for the purpose of avoiding gains tax, the transfers pursuant to the plan are exempt from gains tax; (2) that no gains tax is due on transfers made prior to the 1984 amendments to Tax Law §§ 1440.7 and 1442 or prior to the effective date of the Division's regulations; (3) that the Division erred in calculating the amount due by (a) not following its own guidelines, (b) basing the original purchase price on the 1975 acquisition cost of the property rather than the value of the shares on January 20, 1983, (c) overstating the amount of mortgage includable as consideration received, (d) failing to include an estimated

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The OPP was calculated as follows:

$102,713.00	($1,199,419.00 x $\frac{6,850}{79,990}$)
$ 6,791.00	(legal fees incurred for 1st 4 units)
$ 8,230.00	(capital improvement to unit 13D)
$ 10,141.06	(additional legal fees)
$127,875.06	

broker's commission of 6% on future sales and (e) failing to include flip tax payments by petitioners into the reserve fund; that (4) no gains tax was due on transfers of units 13B, 11C, 14C and 10D because the sale contract provided for installment payments and delayed the actual transfer of the shares until 1993; and (5) that penalties and interest should be disallowed because no regulations were in effect at the time of the transfers.

The Division contends that whether the cooperative conversion plan was or was not devised for the purpose of avoiding gains tax is irrelevant; that the regulations promulgated in September 1985 were adopted from the Division's Publication 588 issued in August 1983; that the 1984 amendment to Tax Law § 1440.7 was a clarifying change and not a substantive change; that petitioners are not entitled to step-up the original purchase price based upon the value of the shares on January 20, 1983; that the Division did not err in using the face amount of the wraparound mortgage in computing consideration; that the Division accurately calculated the estimated consideration for units 10B and 6D; that petitioners are not entitled to reduce their gains tax liability by an estimate of future brokerage costs or the unsubstantiated "flip tax" payment; and that there is no proof that the transfer by Evelyn Reynolds of units 13B, 11C, 14C and 10D was not completed until 1993.

CONCLUSIONS OF LAW

A. Under Tax Law Article 31-B, section 1441 imposes a 10% tax on gains derived from the transfer of real property. Article 31-B became effective on March 28, 1983. Petitioners argue that because the real property in question was conveyed to the cooperative corporation on January 20, 1983, the subsequent transfer of shares in accordance with the cooperative conversion plan after March 28, 1983 was not subject to gains tax.

This interpretation of the tax has already been rejected by the Court of Appeals in Mayblum v. Chu (67 NY2d 1008, 503 NYS2d 316), wherein the court held that although the cooperative conversion itself is treated as a single transfer for purposes of computing the tax on the subsequent sale of shares, it is the subsequent transfer of the shares that is the taxable event. Thus, all sales of units made subsequent to the effective date of Article 31-B are subject to gains tax (see, Matter of Albe Realty Co. v. Tax Appeals Tribunal, 194 AD2d 838, 598 NYS2d 602,

603, lv denied 82 NY2d 657, 604 NYS2d 556; Matter of Normandy Associates, Tax Appeals Tribunal, March 23, 1989).

B. Petitioners argue that transfers of shares prior to the 1984 amendments to Tax Law §§ 1440.7 and 1442 were not subject to gains tax. In Mayblum v. Chu (supra), the Court of Appeals rejected a litigant's argument, which is identical to petitioners' claim -- that the amendment to Tax Law § 1440.7 which added the sentence, "[f]or purpose of this article,

transfers pursuant to a cooperative plan shall include all transfers of stock in a cooperative corporation which owns real property", indicated that prior to the amendment the transfer of shares was not a taxable event. The court determined that the amendment constituted a legislative amplification of its previous intent. In support of this determination, the court referred to the State Executive Department Memorandum which stated that the purpose of the bill amending the gains tax law was to clarify the gains tax treatment of cooperative conversions (id. at 317, citing 1984 McKinney's Session Laws of NY, at 3457).

Similarly, the 1984 amendments to Tax Law § 1442 constitute a clarification of the gains tax law (id.). Petitioners argue that prior to the 1984 amendment to section 1442, the Legislature did not intend to tax cooperative sales before an aggregate of $1,000,000.00 in sales had occurred.[6]

Question and answer 21.F in Publication 588, issued in August of 1983, discusses whether transfers pursuant to a cooperative plan are aggregated. In that discussion, the Division noted that transfers pursuant to a cooperative plan are aggregated under the aggregation clause of Tax Law § 1440.7. The aggregation clause of section 1440.7, which was also contained in the original 1983 version, stated that:

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[6]In their brief, petitioners assert that certain provisions did not appear in section 1442 prior to the 1984 amendment. Petitioners inaccurately described the additions to the statute. The following underlined language constitutes the 1984 additions to section 1442; the bracketed language indicates language in the 1983 version but deleted from the 1984 version:

> " . . . In the case of a transfer pursuant to a cooperative or condominium plan, the date of transfer shall be deemed to be the date on which each cooperative or condominium unit is transferred. In the case of partial or successive transfers which are treated in the aggregate pursuant to subdivision seven of section fourteen hundred forty of this article, the date of transfer shall be deemed to be the date on which each partial or successive transfer of the aggregated transfer is transferred. For purposes [the purpose] of calculating the amount of tax due in each such partial or successive transfer or transfer pursuant to a cooperative or condominium plan, an apportionment of the original purchase price of the real property and total consideration anticipated under such cooperative or condominium plan or such aggregated transfer shall be made for each such cooperative or condominium unit or partial or successive transfer."

> "Transfer of real property shall also include partial or successive transfers pursuant to an agreement or plan to effectuate by partial or successive transfers a transfer which would otherwise be included in the coverage of this article, provided that the subdividing of real property and the sale of such subdivided parcels improved with residences to transferees for use as their residences, other than transfers pursuant to a cooperative or condominium plan, shall not be deemed a single transfer of real property" (emphasis added).

The fact that a specific exclusion from the residential exemption was provided for cooperative plans indicates the Legislature's intent to aggregate the transfer of shares pursuant to a cooperative plan. This aggregation provision clearly indicates the Legislature's intent to tax each transfer pursuant to a cooperative plan even though the consideration received for each such sale by itself did not equal $1,000,000.00 or more. There is nothing in the legislative history of the 1984 amendments to the gains tax law to imply that such amendments imposed a new tax obligation, as contended by petitioners, that had not already been in place. Contrary to petitioners' claims, the amended language merely clarified the existing provisions under section 1442.

C. Without referring to any specific provision in the Division's regulations concerning gains tax, petitioners broadly argue that no gains tax was payable under Article 31-B until the effective date of the regulations in September of 1985. Petitioners assert that the regulations cannot be retroactively applied to the transactions in question.

Petitioners' claims are meritless. Tax imposed under a statute may be enforced prior to the promulgation of the Division's regulations concerning that statute. Petitioners have not identified which regulation was retroactively applied to their transfers. As noted above, the units in question were taxed in accordance with the statutory language concerning cooperative plans. In any event, regulations that merely codify or fill in the details of the statutory policy do not invoke a claim of impermissible retroactive application (see, SEC v. Chenery Corp., 332 US 194, 191 L Ed 1995; Sam v. U.S., 682 F2d 925, 932 [Ct Cl 1982], cert denied 459 US 1146, 74 L Ed 993 [1983]; see also, Matter of Sanjaylyn Co. v. State Tax Commn., 141 AD2d 916, 528 NYS2d 948, 950, appeal dismissed 72 NY2d 950, 533 NYS2d 55; Matter of Sterling Bancorp, Tax Appeals Tribunal, November 18, 1993). Petitioners have not demonstrated that any of the regulatory provisions exceeded the statutory grant of power to an agency to promulgate

regulations or that the provisions themselves did more than codify the policy embodied in the statutory language.

D. Petitioners argue that because they furnished a sworn statement that the cooperative plan was not entered into for the purpose of avoiding gains tax, the transfers were not subject to tax pursuant to Tax Law § 1440.7. Section 1440.7 states, in pertinent part, that:

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

As indicated by the above statutory language, a sworn statement that the transfers were not pursuant to a plan does not apply to transfers pursuant to a cooperative plan because such transfers are "otherwise" subject to tax in that provision. The next sentence following the above-quoted sentence cited by petitioners in section 1440.7 states:

> "For purposes of this article, transfers pursuant to a cooperative plan shall include all transfers of stock in a cooperative corporation which owns real property."

Moreover, a sworn statement that the cooperative plan was not entered into for the purpose of avoiding tax is not relevant. There is no statutory requirement that a tax avoidance purpose is necessary to trigger the aggregation rule under the statute (Matter of Cove Hollow Farm v. State of New York Tax Commn., 146 AD2d 49, 539 NYS2d 127, 129). As noted above, sections 1440.7 and 1442 clearly contemplate that partial or successive transfers pursuant to a cooperative plan are subject to gains tax. In light of this conclusion, I deny petitioner's request for a hearing to put in testimony and further evidence to suport its claim that the unit sales were not pursuant to an agreement or plan to avoid gains tax.

E. Petitioners argue that the "gain" calculated by the Division is erroneous because it underinflated the original purchase price and overinflated the consideration estimated and actually received on future sales for purposes of calculating the tax per share. Tax Law § 1440.3 defines "gain" as the difference between the consideration for the transfer of real property and the original purchase price. Under the statute, the original purchase price means the consideration paid or required to be paid by the transferor "to acquire the interest in real property" (Tax Law § 1440.5[a]). The statutory definition of "consideration" includes:

> "any price paid or required to be paid, whether expressed in a deed and whether paid or required to be paid by money, property, or any other thing of value" (Tax Law § 1440.1[a]).

The regulations further provide that consideration paid to acquire an interest in real property includes:

> "the amount of money, property or any other thing of value provided or given up to acquire the interest in real property including the amount of any mortgage, lien or other encumbrance on the real property which was assumed or taken subject to" (20 NYCRR 590.15[a]).

Relying on 20 NYCRR 590.35, petitioners contend that they are entitled to step-up the original purchase price paid in 1975 to the value of the shares (the insider's purchase price of $45.00 per share) at the time petitioners conveyed the building to the cooperative corporation on January 20, 1983. Specifically, petitioners rely on a statement in 20 NYCRR 590.35(f) which reads as follows:

> "Where the transfers to the owners of the realty transferor took place before March 29, 1983, the owners will have an original purchase price in the shares based on the value of the shares at the time of the transfers."

Petitioners' reliance on this statement for a step-up in basis is misplaced. This statement is the partial response to a question posed concerning whether gains tax should be paid on transfers by the realty transferor to its owners. The response to the question posed also states that transfers by the realty transferor to its owners are not subject to gains tax and that the owners hold the shares in the place of the realty transferor with an original purchase price equal to that of the realty transferor's immediately before the transfer. In contrast to the situations addressed by the regulation, the transfer that took place prior to March 29, 1983 was the transfer of the building by petitioners as owners to the cooperative corporation (realty transferor). Tax Law § 1443.5 exempts from gains tax a transfer of real property which involves "a mere change of identity or form of ownership or organization, where there is no change in beneficial ownership." The regulations further provide that where the transfer involves a mere change of identity or form of ownership and no change in beneficial interest, the transferee has a carryover original purchase price in real property (20 NYCRR 590.50). Petitioners have not demonstrated that there was a change in the beneficial interests of the owners of the cooperative corporation to justify a step-up in the original purchase price when the property was conveyed to the

corporation prior to March 29, 1983 (see, Matter of Schrier v. Tax Appeals Tribunal, ___ AD2d ___ [December 30, 1993]).

F. Petitioners also claim that "gain" was improperly calculated by overstating the amount of mortgage to be included in the consideration received on the sales of the shares. Petitioners contend that at the January 1983 closing, they took back a second "wrap-around" mortgage of $1,350,000.00 with the obligation to pay off the first mortgage from the proceeds of the wraparound mortgage and that, therefore, in calculating the consideration received on their sales, the pro-rata portion of the $1,350,000.00 mortgage should be reduced by the per-share obligation to pay the underlying first mortgage. Petitioners assert that the Division incorrectly used the full face value of the $1,350,000.00 wraparound mortgage in calculating the gain per share. Petitioners state that the Legislature intended that gain be determined by the value, and not the face amount, of a mortgage and that "[c]learly, the face amount of the first mortgage was not its value to the petitioners."

As noted by the Division, the Tax Appeals Tribunal has explicitly rejected arguments that the value, rather than the face amount, of a mortgage should be included in the consideration used to determine gain (Matter of River Terrace Associates, Tax Appeals Tribunal, October 22, 1992; Matter of Normandy Associates, supra). Therefore, petitioners' argument is rejected.

G. Petitioners contend that the Division has not followed its guidelines set forth in TSB-M-86-(3)-R in calculating safe harbor estimates on unsold shares. Prior to August of 1986, the Division permitted two methods, Option A and Option B, for calculating gains tax liability upon transfer of shares with respect to cooperative units when other shares in the cooperative plan remained unsold. Option A allowed gain to be computed based upon the actual consideration received on each unit less the amount of original purchase price apportioned to each unit in the plan, whereas Option B allowed gain to be computed on a per share basis taking into account the actual consideration received as well as the anticipated consideration on unsold shares less the amount of original purchase price apportioned to each share in the plan to determine the tax per share on units sold. After August 1986, the Option A method was eliminated and certain standards were established in TSB-M-86-(3)-R for estimating anticipated consideration under a

cooperative conversion plan. These standards are called the "Safe Harbor Estimates". In TSB-M-86-(3)-R, the safe harbor estimate for a:

> "non-eviction conversion plan will be calculated by taking the lower of
>
> "a) 100% of the total of the offering plan prices established for insiders for the unsold units, or
>
> "b) 50% of the total of the vacant market value for the unsold units. Vacant market value will be established based on the price of vacant units transferred at the initial closing. If there are insufficient contracts for vacant units to establish vacant market value, or if circumstances indicate that the vacant units are not being transferred at market value, then the transferor must use 100% of the insider offering plan price to calculate his Safe Harbor Estimate under (a) above."

As indicated in the affidavit of Peter Van Buren, the Division estimated consideration in computing gains tax with respect to units 10B and 6D only.[7] The Division claims that 50% of the vacant market value was used because there were existing sales of vacant units from which a reliable estimate could be computed. Citing Matter of Normandy Associates (supra), the Division argues that once a taxpayer fails to comply with the filing and payment provisions of the gains tax law, complaints that the Division should not use actual consideration figures to calculate estimates of future consideration are unwarranted.

The Division's calculation of estimated consideration with respect to units 6D and 10B was reasonable under the circumstances. The purpose of the safe harbor estimates is to allow the taxpayer to elect a method for estimating gain on the overall plan in the absence of actual sales on all the units such that, in the event of underpayments, there would be no imposition of penalty or interest on the underpayments. As noted by the Division in its November 27, 1990 letter to petitioners, taxpayers may elect not to file pursuant to the safe harbor estimates and

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[7]In its November 27, 1990 letter, the Division explained that it estimated consideration of unsold shares in calculating gain for units 6D and 10B at 50% vacant market value because vacant sales occurred and it was therefore possible to estimate unsold shares. The Division contrasted this treatment with its treatment of shares owned by petitioner Reynolds (units 13B, 11C, 14C and 10D). In the calculation of tax for the four units owned by petitioner Reynolds, the Division used 100% of the latest offering plan price of $500.00 per share with respect to the remaining unsold shares because vacant sales had not occurred. However, since this letter, Peter Van Buren recalculated the tax owed on the four units using the actual sale price of the fifth unit (see, Finding of Fact "24").

instead value unsold shares based on reasonable estimates; however, if those estimates are below the actual selling price, then the taxpayer is subject to penalty and interest. Here, petitioners did not timely file and pay gains tax. Thus, they are not entitled, after the fact, to compute the tax owed pursuant to the lower of the safe harbor estimates (see, Matter of Normandy Associates, supra).[8] Under these circumstances, it was reasonable for the Division to base the estimated consideration for the two vacant units on 50% of the actual sale price of the sold units inasmuch as that method reflects the potential sale price of future units. It should be noted that the Division's method in this case is more generous than using the actual sale price as permitted under Option A, which was available to petitioners Bogoni and Urich at the time of their sale of unit 6D on March 5, 1986.

Petitioners further argue that in determining estimated consideration, the Division incorrectly added the full face value of the mortgage obligation without reducing it by 50% as it did with the consideration received. This argument has no merit. All shares of the cooperative are pledged as security for repayment of the mortgage under the terms of the Offering Plan. This amount is a known entity and can be apportioned over the entire 79,990 shares of the cooperative as done in the Division's calculations. The purpose of taking 50% of the consideration already received as an estimate of future consideration recognizes the speculative nature of future sale prices. There is no speculation as to the amount of the mortgage obligation assumed by each share of the cooperative. Thus, petitioners' argument is rejected.

H. Petitioners next argue that the Division refused to reduce the "gain" by the flip tax contribution in the amount of $40,647.68, which was payable by petitioners to the reserve fund on the sales of unit 12D ($4,128.69), unit 2A ($5,045.48), unit 10B ($10,809.43), unit 6D ($5,955.77), and unit 13D ($7,296.81), and which is "anticipated" to be paid with respect to units 13B, 11C, 14C and 10D ($7,411.50). Petitioners assert that these payments represent

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[8]Because it is determined that the Division was not obligated to use the safe harbor estimates with respect to this issue, I will not address whether the Division correctly applied the standard set forth in TSB-M-86-(3)-R.

ongoing payments in addition to the $150,000.00 initial payment to the reserve fund which the Division did allow to reduce the gain.

In its brief, the Division stated that it will allow contributions to the reserve fund with respect to the transfers of unit 6D ($5,955.77) and unit 10B ($10,809.43) because those amounts are substantiated by closing statements. Thus, these two amounts should be considered in recomputing the tax per share owed with respect to unit 6D. However, the Division stated that it would not allow flip tax payments with respect to units 12D and 2A because the evidence submitted by petitioners did not substantiate that the payments were in fact made. The Division also stated that it declined to allow the amount for unit 13D because the Notice of Determination did not cover the transfer of shares with respect to that unit which occurred on May 21, 1992. Furthermore, the Division declined to allow the "estimated" flip tax asserted by petitioners as "anticipated" flip taxes on units 13B, 11C, 14C and 10D.

The evidence submitted by petitioners with respect to the payment to the reserve fund for units 12D and 2A consisted of letters by Mr. Glushak to an attorney indicating that the sponsor-sellers would make the contribution to the reserve fund at the closing of the respective sales. No affidavit or other documents, such as the closing statement itself, was submitted to substantiate that this payment was actually made. Therefore, until these payments and the payments with respect to units 13B, 11C, 14C and 10D can be documented, the Division did not err in not including these amounts.

However, contrary to the Division's disallowance with respect to the $7,296.81 payment into the reserve fund for the transfer of unit 13D,[9] this amount should be taken into account for recomputing the amount of tax per share owed by the other four units transferred by petitioner Reynolds. The Division contradicts itself by allowing the reserve fund payment with respect to unit 10B but not with respect to unit 13D inasmuch as unit 10B also was not covered by the Notice of Determination. It should be noted that, in his affidavit, Peter Van Buren recalculated the tax per share for units 13B, 11C, 14C and 10D by taking into account the actual

[9]Similar to units 6D and 10B, the payment into the reserve fund was substantiated by a closing statement. Therefore, there is no issue with respect to substantiation that this amount was paid.

consideration received for the transfer of unit 13D (see, Finding of Fact "24"), and also recomputed tax owed with respect to unit 6D by taking into account the sale of unit 10B even though unit 10B was not covered under the Notice of Determination. Thus, in recalculating the amount of tax per share owed with respect to units 6D, 13B, 11C, 14C and 10D, an adjustment should be made to reflect the contributions into the reserve fund with respect to units 6D, 10B and 13D.

I. Citing the Tribunal's decision in Matter of Normandy Associates (supra), petitioners argue that the Division erred in not including a 6% broker's commission in determining estimated consideration in calculating the tax per share. In Normandy Associates, the Tribunal held that because

the tax due on the transfers at issue is based on an allocation of the gain anticipated on the entire plan, future brokerage fees are also a necessary element to calculate this tax. Without addressing the Tribunal's holding in Normandy Associates, the Division argues that because petitioners did not produce any brokerage agreement indicating that commissions of 6% will be incurred on future sales, they are not entitled to deduct that amount from the anticipated consideration.

In Normandy Associates, the Tribunal noted that the Division did not object to the Administrative Law Judge's conclusion that a 6% brokerage fee was an allowable deduction. In the determination below, the Administrative Law Judge noted that there was no dispute that the brokerage fee on the units in question should be 6% of the anticipated sale price of the unit. However, in the present case, there is a dispute as to whether petitioner will incur a 6% brokerage fee on the sale of future units.

When petitioners raised this argument in an oral motion to amend the petition at the hearing held on March 24, 1993, they were given an opportunity to submit documents in support of their argument in the event the parties could not stipulate to the facts underlying their legal arguments. No further evidence was submitted by petitioners. Thus, based on the record, petitioners' claim for an estimated 6% broker's commission is rejected in these circumstances.

The 6% fee is not substantiated by a contract committing petitioners to a 6% fee on future sales nor can such amounts be anticipated based on broker's fees on sales already completed.[10] Thus, as indicated by the Division, there is no basis in the record upon which it can be assumed that petitioners will incur a broker's fee of 6% on future sales that should reduce the estimated consideration used in calculating gains tax per share for unit 6D.[11]

J. On August 3, 1993, petitioners applied to further amend their petition to include, for the first time, the claim that no taxes were owed on the transfer of shares with respect to units 13B, 11C, 14C and 10D because the sale contract for all four units did not provide for their transfers until 1993.[12] Petitioners' claim is rejected because they did not provide any evidence to substantiate the claim that the shares were not actually transferred to the purchasers until full payment of the purchase price under the sale contract (cf., Matter of Estate of Lever v. New York State Tax Commn., 144 AD2d 751, 535 NYS2d 158, 160 [a determination as to whether a contract is binding is based upon the objective intent of the parties as gathered from their expressed words in the contract and deeds]).

K. Finally, petitioners argue that penalties and interest should be abated because regulations concerning the gains tax were not promulgated until 1984. Tax Law § 1446.2(a) permits abatement or waiver of penalty if it can be determined that a taxpayer's failure to timely file and pay the gains tax was due to reasonable cause and not due to willful neglect. The reasonableness of a taxpayer's failure to pay the tax must be evaluated in light of the Division's

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[10]The Division used estimated consideration in computing gain only with respect to units 6D and 10B. The brokerage fee accepted by the Division in its calculation for the two units was $18,000.00, which constituted approximately 2% of the actual sale price of the 2,590 shares allocated to the two units. However, the closing statement for the sale of unit 6D reveals that the brokerage fee was $18,000.00 on the $308,000.00 sale (thus, 5.8% of the selling price) which, in turn, indicates that no brokerage fee was incurred for the sale of unit 10B.

[11]The Notice of Determination does not cover tax owed with respect to unit 10B.

[12]Although this claim affects the interest of petitioner Reynolds only, reference nonetheless will be made to all petitioners who filed one petition.

articulated policy (see, Matter of Benacquista, Polsinelli & Serafini Mgt. Corp. v. Commr. of Taxation & Fin. of the State of NY, 191 AD2d 80, 598 NYS2d 829, 832) and "the extent of the taxpayer's efforts to ascertain its tax liability" (Matter of KAL Associates, Tax Appeals Tribunal, October 17, 1991). Here, petitioners have offered no evidence that they made any efforts to determine their tax liability.

Petitioners' contention that they should not be held liable because the regulations were not issued until 1984 has no merit. The Division had issued in August of 1983 Publication 588, which was subsequently adopted as regulations. Moreover, the statutory language itself should have induced petitioners to make inquiries concerning their tax liability. Furthermore, the record reflects that even after the Division contacted petitioners in 1988 and informed them of their potential tax liability, the documents requested were not timely provided. Considering the total circumstances, petitioners have not demonstrated reasonable cause to waive penalties or interest penalties for failure to comply with the filing and payment provisions of the gains tax law (see, Matter of Benacquista, Polsinelli & Serafini Mgt. Corp. v. Commr. of Taxation & Fin. of the State of NY, supra; Matter of Brounstein, Tax Appeals Tribunal, January 30, 1992).

L. As noted in Findings of Fact "16" and "24", the amount of gains tax liability should be recomputed, as indicated in the Division's November 27, 1990 letter and in the affidavit of Peter Van Buren, which reflected the actual consideration received by Evelyn Reynolds for the sale of unit 13D in calculating the tax per share owed for units 13B, 11C, 14D and 10D.

M. The petition is granted to extent of Conclusion of Law "H" and is otherwise denied, and the Notice of Determination, dated June 25, 1990, is modified by the Conciliation Order and in accordance with Conclusion of Law "L", and is otherwise sustained.

DATED: Troy, New York
March 17, 1994

/s/ Marilyn Mann Faulkner
ADMINISTRATIVE LAW JUDGE