STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
CALVERTON PROPERTY COMPANY	:	DETERMINATION DTA NO.810782
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, Calverton Property Company, c/o Keith H. Archer, Esq., Morton Weber & Associates, 534 Broad Hollow Road, Melville, New York 11747, 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.

On or about July 8, 1993, petitioner, by its duly appointed attorney and representative, Howard M. Koff, Esq., and the Division of Taxation, by William F. Collins, Esq. (Donald C. DeWitt, Esq., of counsel), signed a waiver of hearing and consented to have this matter determined upon the papers, including stipulated facts. The Division of Taxation filed its exhibits on July 20, 1993. Petitioner submitted no exhibits. The parties' stipulation of facts was submitted on or about September 20, 1993. The last scheduled day for filing briefs, i.e., petitioner's reply, was October 26, 1993. This was later extended, at petitioner's request, to December 15, 1993. After due consideration of the evidence and briefs filed herein, Carroll R. Jenkins, Administrative Law Judge, renders the following determination.

ISSUE

Whether the original purchase price of real property sold by petitioner must be stepped-up to reflect the consideration paid for the 1987 acquisition by two of the partners of less than a controlling interest in the partnership.

FINDINGS OF FACT

Petitioner, Calverton Property Company, c/o Keith H. Archer, Esq., Morton Weber &

Associates, 534 Broad Hollow Road, Melville, New York 11747 (hereinafter "petitioner" or "Calverton") is a co-partnership.

In July 1954, Jack Nelson, David Einbinder, Sidney Horowitz, Benjamin Spencer, Jay E. Rubinow and Stanley Bray entered into a syndication agreement for the purpose of purchasing certain real property in Suffolk County, New York.

On August 31, 1954, Jack Nelson, pursuant to the syndication agreement, purchased 405 acres of Suffolk County real property ("the property") for $263,250.00 ($650.00 per acre). On December 18, 1954, Nelson executed a declaration of trust whereby he agreed to hold the property as trustee for the other five members of the syndicate.

Under the trust agreement, Nelson, his heirs and assigns, were required, upon demand, to convey to any member of the syndicate his proportionate interest in the property. In the event the property was sold, the net proceeds would be paid to each of these individuals in proportion to his contributions.

There is no evidence in the record that Suffolk County ever approved a subdivision plan for the property and there is no evidence that any structures or capital improvements were ever placed on the property.

Between 1954 and 1974, some of the property was conveyed and some was taken by eminent domain.

On or about 1974, the then owners of a 76% interest in the property (i.e., Nelson, Spencer, Horowitz, Libman, etc., or their successors in interest) agreed to hold their interests as a partnership, i.e., Calverton Property Company,[1] and accordingly, on August 19, 1974, their 76% interest was jointly conveyed by deed to petitioner. From that point, the individuals comprising the Calverton partnership (owners of a 76% interest in the property) appear to have held the property as co-partners with Stanley Bray and Jay Rubinow or their successors (owners

[1]Apparently Stanley Bray and Jay Rubinow, decided to hold their interests in the property separately from Calverton.

of a 24% interest in the property).[2]

In 1987, Benjamin Spencer, a partner in petitioner, conveyed all of his 23.68% interest in the partnership to Alvin Gindel and Sidney Horowitz for $339,862.00. That same year, Morris Libman, also a partner, conveyed all of his 17.54% interest in petitioner to Gindel and Horowitz for $251,687.00. By these purchases, it is undisputed that Gindel and Horowitz acquired a 41% interest in the partnership.[3] Of the amounts

paid in 1987, the record does not show how much was paid by Gindel and how much was paid by Horowitz. Further, the record does not show what percentage of the partnership interests purchased in 1987 went to Horowitz and what percentage went to Gindel. The record is also silent with regard to whether Gindel and Horowitz, in making the 1987 purchases of interests in the partnership, were acting independently of each other or were acting in concert.

On December 5, 1991, Calverton, together with Stanley Bray, Judith Gartner, and David and Laurence Rubinow (then owners of the remaining 24% interest in the property) entered into an agreement to sell to Suffolk County, for $2,437,751.60, the remainder of the subject property, which consisted of 265 acres of vacant land.[4]

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[2]Jay Rubinow's interest was gifted to Judith Gartner, David Rubinow and Laurence Rubinow in 1983 and 1984.

[3]Since the parties have stipulated that it was Gindel and Horowitz that purchased this 41% interest in 1987, it has been adopted as a finding. However, it is noted that the question of "who received what" percentage of that 41% is not addressed in the record. It is also noted that the two agreements of sale in the record are only between Spencer and Gindel and Libman and Gindel. Horowitz is only mentioned in both agreements in the "hold harmless" clauses, not as a buyer or grantee.

[4]Actually, the purchase price appearing on the contract is $2,436,160.00. The contract provides that the per acre price is $9,200.00. The sellers warranted that the premises contained at least 264.8 acres. The parties agreed to adjust the price to the actual acreage after a survey had been conducted. That appears to account for the difference in purchase price appearing in the contract and that appearing in the transferee's questionnaire (TP-581[8/84]), i.e. $2,437,751.60. This latter figure was the actual selling price.

The County and petitioner, as seller,[5] duly filed real property gains tax transferor and transferee questionnaires with the Division of Taxation ("Division"). The transferor questionnaire filed by petitioner reported:

Gross consideration paid to petitioner:	$1,852,691.20
LESS:	
Purchase price to acquire the property:	668,481.00
Expenses of sale:	39,605.00
Total original purchase price:	$ (708,086.00)
Gain Subject to Tax:	$1,144,605.20
GAINS TAX DUE:	$ 114,460.00

Petitioner computed its "price to acquire the property", supra, by including the amounts paid by Gindel and Horowitz ($591,549.00) in 1987. Petitioner's computation was as follows:

265 Acres x $650.00 per acre[6]	= $ 172,250.00	
Calverton's allocated cost	x 76%	
	$ 130,910.00	
Adjust for 1987 partnership acquisitions (2)	x 41.233%	
	- 53,978.12	
	$ 76,931.88	
Add cost of 1987 acquisitions by Gindel and Horowitz	591,549.00	
Petitioner's "stepped-up" basis	$ 688,480.88	

Attached to petitioner's transferor questionnaire was a page detailing the claimed "Expenses of Sale". This page shows "legal fees" relating to the sale of the property totalling $31,993.00 for the period from May 3, 1990 to August 2, 1991. This page also showed engineering expenses of $12,680.00 incurred in 1989 relating to subdivision of the property. Reported legal fees for 1989 relating to subdivision of the property were $7,439.25. The total of these reported "Expenses of Sale" was $52,112.25, with petitioner's 76% allocation of these expenses being $39,605.31.

On or about December 30, 1991, the Division issued a Tentative Assessment and Return asserting real property transfer gains tax ("gains

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[5]From this point, this discussion relates only to petitioner and its 76% share.

[6]Price paid per acre in 1954.

tax") due based upon information contained in the filed transferor and transferee questionnaires. Attached to the Tentative Assessment and Return was a Schedule of Adjustments explaining the basis of the Division's recomputation of gains tax due.

The tentative return and statement of adjustments recomputed gains tax by disallowing petitioner's "stepped-up" price to acquire the property, and by disallowing petitioner's claimed selling expenses relating to legal and engineering fees associated with subdivision of the property.

These adjustments appear on the Statement of Adjustments as follows:

Purchase Price Paid to Acquire Real Property		
265 acres x $650.00/acre		$172,250.00
Petitioner's 76% interest		x 76%
Petitioner's price to acquire the property	$130,910.00	
Original purchase price claimed		668,481.00
Original purchase price allowed		-130,910.00
Resulting disallowed portion		$537,571.00
Allowable Selling Expenses		
"Section 1440.5(a) of the Tax Law limits allowable selling expenses to legal, engineering and architectural fees incurred in selling real property. Accordingly, the expenses claimed regarding the subdivision are being disallowed."		20,119.25
Total Disallowed:		$557,690.25

The Division computed the gains tax on the tentative assessment and return as follows:

Gain subject to tax as computed by petitioner:	$1,144,605.20
Total Amounts disallowed (Line 2)	557,690.25
Gain Subject to tax as adjusted:	$1,702,295.45
GAINS TAX DUE:	$ 170,229.55

Petitioner paid the adjusted gains tax asserted of $170,229.55 on January 22, 1992. Thereafter, petitioner filed a claim for refund with the Division in the amount of $70,808.57.

Petitioner's refund claim asserted that: (a) the legal ($7,439.25 x 76% = $5,653.83) and engineering expenses ($12,680.00 x 76% = $9,636.80) it incurred in obtaining subdivision approval should have been allowed as part of "selling expenses"; and (b) the consideration paid by Gindel and Horowitz ($591,549.00) in 1987 to acquire their interest in the partnership was improperly disallowed, and should have been included as a "step-up" in the partnership's cost to acquire the property.

By letter dated March 13, 1992, petitioner's application for refund was denied. Thereupon, petitioner filed the instant petition dated May 4, 1992.

SUMMARY OF THE PARTIES' POSITIONS

Petitioner argues that the $591,549.00 paid by Gindel and Horowitz to purchase a 41% interest in petitioner in 1987 should be allowed as a "step-up" in the partnership's purchase price to acquire the subject property.

Petitioner argues, in this regard, that to the extent that the Division's regulation (20 NYCRR 590.49[b]) purports to deny a step-up in original purchase price where, as here, less than a controlling interest is acquired, it is contrary to Tax Law § 1440(5)(a) "which, as a general rule, mandates a 'stepped-up' OPP" (Petitioner's brief, p. 2). For that reason, petitioner states, the regulation is invalid.

Next petitioner argues that 20 NYCRR 590.49(b) "ignores reality" and would tax "phantom gains".

Finally, petitioner urges that a "stepped-up" original purchase price is consistent with the "look through rule" (citing Matter of 307 McKibbon St. Realty Corp., Tax Appeals Tribunal, October 14, 1988). Under the look-through rule, petitioner says:

> "Gindel and Horowitz, the beneficial owners, are treated as the transferor. Hence, their acquisition costs must be utilized to ascertain taxable gain" (Petitioner's brief, p. 3; emphasis in original).

Petitioner offered no arguments or evidence in support of its claim that legal and engineering expenses incurred to obtain subdivision approval should have been allowed in computing original purchase price, even where the property was not subdivided.

The Division argued that the law permits a step-up in the original purchase price of real property owned by a partnership only where there has been an acquisition of a controlling interest in the partnership. Accordingly, the Division states, the amounts paid by Gindel and Horowitz for the purchase of less than a controlling interest in the partnership were properly disallowed in computing the original purchase price of the property.

CONCLUSIONS OF LAW

A. Petitioner does not take issue with the tax imposed on the gain derived from the transfer of real property herein, rather the computation of that gain and, more specifically, whether there should be an adjustment to the original purchase price of the real property, is the matter in dispute.

B. Tax Law § 1441 imposes a tax on gains derived from the transfer of real property within the State. In the case of a business entity, the "transfer of real property" is defined, in relevant part, as the "acquisition of a controlling interest in any entity with an interest in real property" (Tax Law § 1440[7]). With respect to a partnership, trust or association, a "controlling interest" means 50% or more of the capital, profits or beneficial interest in such entity (Tax Law § 1440[2][ii]; 20 NYCRR 590.44[a]).

C. "Gain" has been defined in the Tax Law as:

> "The difference between the consideration for the transfer of real property and the original purchase price of such property, where the consideration exceeds the original purchase price" (Tax Law § 1440[3]).

The "original purchase price" is defined in the same section as:

> "[T]he consideration paid or required to be paid by the transferor; (i) to acquire the interest in real property . . ." (Tax Law § 1440[5][a]).

The regulation promulgated pursuant to Tax Law § 1440(5) at 20 NYCRR 590.49 states, in part, as follows:

> "(a) Question: What is the original purchase price used by the transferor to calculate gain?
>
> "Answer: Generally, it is the original purchase price of the real property as held by the entity, apportioned to the interest the transferor is transferring."

Thus far there has been no mention either in the law or the regulations with regard to

stepping up the basis in the original purchase price. However, in subdivision (b) of the regulation at 20 NYCRR 590.49, the issue is first addressed as follows:

> "(b) Question: Is the original purchase price of the real property as held by the entity stepped-up upon the acquisition of a controlling interest?
>
> "Answer: Yes. In the case of an acquisition of a controlling interest, where the mere change exemption was not applied, the original purchase price in the real property as held by the entity may be stepped up to reflect the consideration recognized on the transfer of the ownership interest.
>
> "If less than a controlling interest were acquired, the entity may not step-up its original purchase price in the property" (emphasis added).

Thus, where a partner or partners acquire less than a controlling interest in a partnership, the entity (and thereby the individual partners) may not step-up its basis in the original purchase price of the real property.

D. Petitioner argues this is unfair, and urges that when Gindel and Horowitz purchased a 41% interest in the partnership from then partners Spencer and Libman in 1987, they paid Spencer and Libman their aliquot basis in the real property plus their share of the appreciation in the underlying real property. That being the case, according to petitioner, the partnership must be allowed to include the amounts paid in 1987 in computing the partnership's original purchase price of the property. To do otherwise, petitioner urges, would unfairly tax gains petitioner did not actually receive.

To some extent, anyone who has ever made a tax payment can sympathize with petitioner's "fairness" argument. However, petitioner has not demonstrated any unfairness here. Petitioner has not shown that the Division has treated it differently, in applying the gains tax law, from other similarly situated taxpayers. Further, petitioner has not alleged or proven that it has been confused by any vagueness in the statute. The fact is that the statute and applicable regulations clearly apprise a taxpayer, such as petitioner, as to what is required before a partnership is entitled to step-up its basis in partnership-owned real property for purposes of computing original purchase price.

Even if petitioner were correct that the gains tax, as computed here, is unfair (and that has not been shown), the Court of Appeals has stated:

> "[I]t seldom suffices, and is often immaterial, in the resolution of tax controversies to demonstrate that . . . a particular statute or regulation works even a flagrant unevenness . . . . That a fairer taxing formula might have been adopted is of no moment . . . . [I]t cannot be assumed that when the Legislature designed the particular statute it had either a specific or even a general desire to achieve a fair or balanced formula" (Matter of Long Island Lighting Company v. State Tax Commn., 45 NY2d 529, 535-536, 410 NYS2d 561, 564).

The crucial point here is that while petitioner argues that it should be taxed only on its "actual economic gain", it cites no legal authority that would permit it. Without applicable New York statutes, regulations or case law to support its position, there is no legal basis for allowing Calverton to step-up its original purchase price of the property based on the purchase by Gindel and Horowitz of less than a controlling interest in the partnership.

E. As noted earlier, the term "controlling interest", as defined in Tax Law § 1440(2)(ii), in the case of a partnership, association, trust or other entity, is 50 percent or more of the capital, profits or beneficial interest in such partnership, association, trust or other entity. The same provision is found in the regulations at 20 NYCRR 590.44. The regulation enhances the statute by providing that the acquisition occurs "when a person or group of persons, acting in concert, acquires a total of 50 percent or more of the capital, profits or beneficial interests in such entity." The regulations also provide that a group of persons is acting in concert when various purchasers have a relationship such that one purchaser influences or controls the actions of another (20 NYCRR 590.45).

Although it is undisputed that Gindel and Horowitz each purchased an interest in the partnership in 1987, there is nothing in the record to indicate whether they did so separately or were acting in concert with each other. In either event, the insurmountable and undisputed fact is, whether acting together or separately, Gindel and Horowitz failed to acquire a controlling interest in the partnership.

F. Petitioner argues that permitting it to "step-up" its original purchase price would be "consistent with the look through rule" (citing Matter of 307 McKibbon St. Realty Corp., supra). Under that rule, according to petitioner, Gindel and Horowitz, as beneficial owners, would be treated as the transferors, and as such, "their acquisition costs must be utilized to

ascertain taxable gain." Petitioner's citing of McKibbon is inapposite, since that case has no bearing on the facts presented here. McKibbon involved the question of whether the consideration received by one corporate petitioner could properly be aggregated with the consideration received by another corporation upon the simultaneous transfer by the two corporations of two contiguous properties. Here, we are not concerned with the tax treatment of two corporations, nor does this case involve an "aggregation" issue or the tax treatment arising from the transfer of two contiguous parcels. Accordingly, this argument is rejected.

G. Petitioner's arguments in this case (with the exception of McKibbon, supra) are similar to those raised and decided in Matter of SKS Associates (Tax Appeals Tribunal, September 12, 1991). In SKS, a one-third owner in a cooperative sold his interest in the partnership to the two remaining partners. SKS argued that: (1) it was entitled to a step-up in original purchase price for purposes of computing its gain derived from the transfer of real property; and (2) the intent of the gains tax enacted as Tax Law Article 31-B was to tax the "actual economic gain" realized by a taxpayer upon certain transfers of real property.

The Tax Appeals Tribunal in SKS sustained the determination below, which held that since the two partners had not acquired a controlling interest in the partnership,[7] SKS could not step-up its basis for purposes of computing the original purchase price of the property. There, as in this case, acquisition of a controlling interest was a prerequisite to allowing a step-up in the original purchase price of the property in question. In the instant matter, since Gindel and Horowitz did not acquire a controlling interest in the partnership, petitioner is not entitled to a step-up in the original purchase price (see, Matter of SKS Associates, supra; 20 NYCRR 590.49).

H. "Original purchase price" as defined in the Tax Law, includes "amounts paid by the transferor for any customary, reasonable and necessary legal, engineering and architectural fees incurred to sell the property . . ." (Tax Law § 1440[5][a]). Petitioner alleged in its petition that the Division improperly disallowed its legal and engineering fees attributable to subdivision of

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[7]Although not for the same reasons as presented here.

the property.

However, it does not appear from the record that the property was ever subdivided. In addition, petitioner has offered no evidence, or arguments in its brief, to support its claim that the subject fees were "customary, reasonable and necessary" or that they were "incurred to sell the property". Since petitioner failed to offer either evidence or argument in support of this claim, it is deemed abandoned.

I. The petition of Calverton Property Company is in all respects denied, and the denial of refund dated March 13, 1992 is sustained.

DATED: Troy, New York
April 14, 1994

/s/ Carroll R. Jenkins
ADMINISTRATIVE LAW JUDGE