STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
MONTCLAIR SPONSOR CORPORATION	:	DETERMINATION DTA NO. 815551
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, Montclair Sponsor Corporation, c/o Millennium III Real Estate, 228 East 45th Street, 18th floor, New York, New York 10017, 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 October 10, 1997 and October 17, 1997, respectively, petitioner, by its representative, Margolin, Winer & Evens LLP (Wayne M. Olson, Esq., of counsel), and the Division of Taxation appearing by Steven U. Teitelbaum, Esq. (Michael J. Glannon, Esq., of counsel) waived a hearing and agreed to submit the matter for determination based on documents and briefs to be submitted by July 31, 1998, which date commenced the six-month period for the issuance of this determination. After review of the evidence and arguments presented, Winifred M. Maloney, Administrative Law Judge, renders the following determination.

ISSUES

I. Whether the Division of Taxation timely issued the Notice of Determination in this matter.

II. Whether the Division of Taxation properly disallowed, in the computation of original purchase price, certain costs which petitioner contends were acquisition costs or costs of capital improvements.

III. Whether a settlement payment made by petitioner to resolve litigation with the condominium association is properly included in the computation of original purchase price for purposes of applying the real property transfer gains tax.

IV. Whether legal fees associated with petitioner's litigation with the condominium association are properly included in the computation of original purchase price for purposes of applying the real property transfer gains tax.

V. Whether the Division of Taxation properly computed the interest due on any unpaid gains tax determined to be due.

VI. Whether the penalty imposed pursuant to Tax Law § 1446 should be abated.

FINDINGS OF FACT

1. On March 27, 1995, the Division of Taxation ("Division") issued to petitioner, Montclair Sponsor Corporation, a Notice of Determination assessing additional tax due under Article 31-B of the Tax Law ("gains tax") in the amount of $148,755.00, plus penalty and interest. The Notice of Determination was based upon a field audit pertaining to property located at Alpine Drive, Wappingers Falls, New York.

2. Petitioner is the sponsor of a plan to convert property located at Montclair Townhouses, Alpine Drive, Wappingers Falls, New York (the "property") to condominium ownership. The

property consists of 37 buildings containing 296 residential apartment units, a pool house, sewer plant, water shed, and maintenance garage. As sponsor, petitioner offered for sale as condominium units all 296 residential apartment units along with each unit's undivided percentage interest in the common elements at the property.

3. Petitioner acquired the property from Fishkill-Montclair Associates, a limited partnership, which transfer qualified as a partial "mere change of identity or form of ownership."[1] The original purchase price ("OPP") reported by petitioner and accepted by the Division was $8,771,369.00, the calculation of which follows:

Purchase Price- Land and Building	$6,700,000
Other Acquisition Costs	296,848
Real Property Capital Improvements Costs	723,859
	$7,720,707
"Taxable" Gain from Transfer	1,050,662
Total Purchase Price Paid to Acquire Real Property	$8,771,369

4. The shareholders of petitioner are Herbert Somekh, Raymond Bernstein, Harold Bernstein, Jay Bernstein, Gene Bernstein, Donita Williams, Gerard Cerchio, Tony Providenti, Milton Askinas, Arthur Zelniker and Andrew Garr.

5. The offering plan, an eviction plan, became effective July 23, 1987. The record only includes 27 pages of the offering plan, and the condominium offering plan's second amendment dated July 23, 1987.

6. Review of the offering plan's table of contents reveals that sections H, I, J and K discuss the rights of tenants, including "eligible senior citizens and eligible disabled person," interim leases, as well as the obligations of unit owners occupied by nonpurchasing tenants. None of these sections are part of the record. According to the section entitled "Special Risks"

[1]The exact date of the transfer is not part of the record. The record also does not include any documents related to that transfer.

(page iv of the offering plan), a nonpurchasing tenant could be evicted at the expiration of his lease and did not have any right to an extension of the term of his lease or any right to remain in possession of his apartment subsequent to the expiration of his lease.

The offering plan's table of contents also contains sections concerning unit closing costs and adjustments (section P), rights and obligations of the sponsor (section Q), management and other contractual agreements (section Z) and sponsor's profit (section Z-2). None of these sections are part of the record.

7. Both the cover page and page 108 of the offering plan list the selling agents as "Innovative Properties Corp." ("Innovative") and "Robert-Mark Realty Inc. and Robert-Mark Agency Inc." ("RM Agency"). According to the offering plan, the RM Agency, an institutional broker, has extensive experience in the marketing of condominium units. It described Innovative as "a licensed real estate broker in the State of New York" whose shareholders are Herbert Somekh and Andrew Garr.

The record includes a copy of the brokerage agreement between petitioner and the RM Agency. Pursuant to the RM Agency agreement, petitioner retained the RM Agency as agent to sell 246 ("selling agent units") of the 296 units. However, the RM Agency was not authorized to sell the remaining 50 units ("sponsor units"). The RM Agency was to receive commissions equal to: (a) 4% of the gross sales price of each selling agent unit sold ("commission") and (b) 1½% of the gross sales price of each sponsor unit sold ("total commission"). The brokerage agreement also stated that the RM Agency was to be the exclusive sales agent with respect to the selling agent's units except that petitioner could also designate Innovative as an additional sales agent. However, even if Innovative brought about any sale, the RM Agency was still entitled to receive the full commission and added commission, as applicable. Petitioner was to pay any commission

due and owing Innovative. The record does not include a copy of any brokerage agreement which may have existed between petitioner and Innovative.

8. By mid 1989, 295 units had been sold and transferred.[2]

9. On November 16, 1989 and December 26, 1989, the Division requested petitioner to file a complete project update for the property.

10. On or about May 1, 1990, petitioner filed transferor questionnaires, forms DTF-700 (9/85), DTF-701 (6/85) and DTF-703 (6/85), with attachments, including a schedule of gains tax paid by unit, for the project update.[3] According to the project update documents, 295 units were sold having 99.56306% of the common interest. In the update filing, petitioner reported total anticipated gross consideration in the amount of $18,974,832.00 (consisting of $18,888,086.00 in actual consideration and $86,746.00 in estimated additional consideration). Petitioner computed the total anticipated gross consideration "using the actual selling prices for units for which contracts of sale have been executed and 'safe harbor' estimate for the unsold unit (i.e., 100% of selling prices set forth in the Offering Plan)." Petitioner reported total anticipated brokerage fees of $1,609,368.00 (consisting of $1,602,456.00 of actual to date and $6,912.00 of estimated additional) broken down as follows: $858,148.00 to RM Agency and $751,220.00 to Innovative. It reported total anticipated OPP in the amount of $10,062,550.00, composed of: (A) Capital improvements totaling $305,325.00 which consisted of: architectural fees of $5,161.00; construction material of $19,500.00; consideration paid to contractors to make capital improvements of $165,791.00; built-in appliances of $10,801.00; landscaping and site planning of $1,600.00; initial painting of new buildings, structures, or additions of $47,355.00; appraisal

[2]The 295th unit was sold on or about June 7, 1989 .

[3]The accompanying cover letter specifically refers to the filing as a "Project Update."

fees of $500.00 and additional capital improvements (i.e., carpentry, electrical, plumbing, tile, carpeting and windows) in the total amount of $54,617.00. (B) Conversion costs totaling $981,411.00 consisting of legal, accounting and engineering fees of $156,290.00; filing and recording fees of $5,860.00; offering plan printing expenses of $24,261.00 and developer's fee of $795,000.00. (C) Total anticipated allowable selling expenses (legal) of $4,445.00 (consisting of $4,195.00 actual to date and $250.00 estimated additional). The project update reported a total anticipated gain subject to tax in the amount of $7,302,914.00.

11. At some point in 1989, the Board of Managers of Montclair Townhouse Condominium commenced an action against petitioner, Innovative, the architect and 13 individuals. Sometime in 1990, Millennium III Real Estate Corporation commenced an action for breach of a management agreement against the Montclair Townhouse Association and the five members of the condominium association board of managers. The record does not include copies of the complaints filed in either of these matters.

On March 12, 1992, the parties to both actions, "to avoid the expense and continuation of litigation and without acknowledging liability of any party," entered into a "Settlement and Release Agreement" ("agreement"). Under the terms of the agreement, petitioner agreed to pay to the condominium board of managers the sum or value of $108,000.00 "in full satisfaction of all claims, payable as follows:" the sale of unit #14A, at the property, at a sale price of $90,000.00 and upon acceptance of the deed to unit #14A, the payment of $18,000.00. According to paragraph 1 of the agreement, the agreement constituted a contract of sale for unit #14A.

12. Prior to the anticipated date of transfer of unit #14A, April 30, 1992, the required transferee questionnaire was filed. On this questionnaire, the transferee is listed as The Board of

Managers of Montclair Townhouse Condominium, the transferor is listed as Fishkill-Montclair Associates and the consideration to be paid for unit #14A is $90,000.00. While not part of the record, it appears that petitioner also filed the required transferor questionnaire. On April 28, 1992, the Division issued to petitioner a Form TP-582 "Tentative Assessment and Return" for the unit reporting the tentative assessment of tax due in the amount of $3,198.63.

13. After a field audit, the Division issued a Statement of Proposed Audit Adjustment ("statement") dated February 13, 1995 against petitioner asserting real property transfer gains tax due of $148,755.00, for various transfers. This amount of gains tax asserted due was based upon the Division's calculation of a total gains tax due of $885,295.00 less prior payments of $736,540.00, for a balance due of $148,755.00, plus interest (from October 15, 1989 through March 13, 1995) in the amount of $92,683.00 and a 10% penalty in the amount of $14,875.00.

14. Attached to the Statement of Proposed Audit Adjustment is the auditor's computation of the gains tax due and supporting schedules of proposed adjustments. The auditor determined anticipated gain to be $8,852,947.00, by subtracting a total of $10,167,999.00 (consisting of Reserve Fund of $30,000.00; Working Fund of $10,000.00; Brokerage fees of $1,041,202.00 and OPP in the amount of $9,086,797.00) from actual consideration of $19,020,946.00.

The auditor's computation was based upon adjustments to brokerage fee, capital improvements and conversion costs. According to the statement's supporting brokerage schedule, using a commission rate of 5.5%, per the RM Agency agreement, for all sales except the last unit's transfer, "as it was transferred as a result of a lawsuit," the auditor allowed brokerage fees totaling $1,041,202.00 ([19,020,946.00 – 90,000.00] x .055 = $1,041,202.00). This schedule also contains a notation that, on audit, petitioner claimed only $1,562,008.00 in brokerage fees. Review of the capital improvements schedule reveals that, of $305,325.00 in

total capital improvements claimed on audit, the auditor disallowed $143,771.00, composed of $132,970.00 in consideration to contractors and $10,801.00 for built-in appliances. The disallowed figure represented amounts claimed for "lost rents, furniture & fixtures and appliances." Of the $981,411.00 in conversion costs claimed on audit, the auditor allowed only $149,429.00. She disallowed $36,982.00 of "refinancing, accounting & litigation fees" and an unsubstantiated developer's fee in the amount of $795,000.00.

15. On March 11, 1995, petitioner's representative sent a letter to the auditor stating that petitioner disagreed with all of the proposed audit adjustments including the computation of interest and the imposition of a penalty and requested a conference. In the same letter, petitioner claimed that the $108,000.00 litigation settlement should be included in OPP as a "cost to create ownership interests in . . . condominium form." It also claimed additional legal fees of $9,500.00 "relating to the settlement and transfer of the last condominium unit."

16. Petitioner did not receive a response to its March 11, 1995 letter, nor was the requested conference ever held. As noted in Finding of Fact "1," on March 27, 1995 the Division issued the Notice of Determination asserting additional gains tax due, plus interest and penalty.

17. In its request for conciliation conference, petitioner disagreed with the audit adjustments which resulted in the additional tax, interest and penalty asserted in the Notice of Determination. It also claimed that the $108,000.00 settlement with the condominium association and an additional $9,500.00 in legal fees relating to the settlement are includible in OPP. Petitioner also claimed that the statute of limitations had expired on either June 7, 1992, or, in the alternative, no later than May 1, 1993, long before the Notice of Determination was

issued in this matter. After a conciliation conference, the conferee issued a Conciliation Order (CMS No. 148436), dated September 13, 1996, sustaining the Notice of Determination.

18. In its petition, petitioner asserts that the Division made the following errors, among others in its computation of gain: (1) Arbitrarily computed brokerage fees; (2) Improperly excluded the following amounts from OPP: "consideration paid to contractors" in the amount of $132,970.00; the entire cost of new built-in appliances in the amount of $10,801.00; legal, accounting and engineering fees in the amount of $36,982.00; and developer and supervisory fees in the amount of $795,000.00; (3) Failed to include the "$108,000 of 'settlement payments' made to the condominium association in order to resolve certain claims by the association relating to improvements to the property" in OPP; (4) Improperly used October 15, 1989 as the starting date for the computation of interest on any additional gains tax due; (5) Assessed penalties which are not applicable in this matter. In the alternative failed to abate the penalties for "reasonable cause"; (6) Issued the Notice of Determination after the statute of limitations had expired.

19. The record includes invoices from two law firms. The first is an invoice dated August 30, 1989 from petitioner's New York City law firm which shows a total balance due in the amount of $25,342.66 for professional services rendered in connection with "Millennium/Montclair Litigation." This invoice reflects balances from prior statements totaling $25,194.66. The second is an invoice dated June 1, 1992 from a New Paltz law firm for professional services rendered with respect to "Millennium III Real Estate Corp. v. Montclair Townhouse Condo." and "Board of Managers of Montclair Townhouse Condo. v. Montclair Sponsor Corp., *et al*." The legal fee of $9,500.00 was for

> [a]ll services rendered, including Court attendance, review of Offering Plan, preparation of pleadings, preparation of Demand for Bill of Particulars, conduct extensive settlement negotiations, preparation of RJI and Trial Term Note of

Issue, motion practice, agreement, preparation of deed and attendance at closing of title, all correspondence and telephone communications (including telefax) with client and opposing counsel.

SUMMARY OF PETITIONER'S POSITION

20. Petitioner argues that the Division has arbitrarily determined that the amount of brokerage fees allowable should be limited to 5.5% of the units' sales prices. It asserts that it incurred a total of $1,609,368.00 in brokerage fees and commissions to the RM Agency and Innovative, the selling agents pursuant to the offering plan, in connection with the sale of the units at the property. Petitioner maintains that the entire amount ($1,609,368.00) is a proper reduction in "gross consideration" in the determination of "consideration." In support of its contention that it incurred $1,609,368.00 in brokerage fees, petitioner submitted a schedule of "Brokerage Commissions" which contains a list of payments made to both RM Agency and Innovative, along with supporting documentation in the form of canceled checks and accounting work papers. Review of the schedule reveals that some form of payment documentation has been submitted for $1,562,008.00 in claimed brokerage fees.

21. Petitioner asserts that $165,791.00 was paid in connection with the renovation and rehabilitation of the units and that the Division improperly disallowed consideration paid to contractors in the amount of $132,970.00. The disallowed amounts consist of $100,170.00 for "lost rents" paid to the prior owner of the property and $33,000.00 for furniture and fixtures - "Models (86 & 87)."[4]

Petitioner argues that the "lost rent" amount represents an additional cost of the improvements to the property and an economic cost to it for the conversion of the property to

[4]The discrepancy between the amount disallowed and the amount claimed with respect to models 86 and 87 has not been explained by either party.

condominium ownership. It avers that the amount was paid to the prior owner so that improvements could be made and the conversion could proceed when units became available. Petitioner contends that the $100,170.00 is includible in OPP as either a cost to improve the property, or a cost incurred to create ownership interests in cooperative or condominium form. It also argues that since the amount was paid to the prior owner as a reimbursement for costs associated with the units during the period between the contract date and the date of transfer, the amount is also includible in OPP as an other acquisition cost.

With respect to the reference "furniture and fixtures," petitioner contends that the $33,000.00 amount "represents amounts incurred to renovate the model units." (Petitioner's brief, p. 10.) Petitioner did not explain the nature of the renovations made to the model units. However, it averred that the model units were sold "as is." Petitioner argues that, if the cost of the renovations included some amount for furniture and fixtures, "the cost thereof was a cost of the units sold and must be included in OPP." (Petitioner's brief, p. 10.) As an alternative argument, petitioner asserts that, if "amounts are deemed to represent payment for items that are tangible personal property and are not included in OPP," a portion of the sales price of the respective model unit must be allocated to such items (Petitioner's brief, p. 10). Petitioner further argues that any amount allocated to those items would not be consideration for real property and therefore would reduce the amount of consideration.

Petitioner did not submit any documentary evidence showing that it had paid either of the above disputed amounts to contractors.

22. Petitioner maintains that the auditor improperly disallowed $10,801.00 which it incurred for the purchase and installation of built-in appliances. Other than some general references to stoves and dishwashers, petitioner did not submit any evidence concerning the type,

cost or installation of any appliances. Alternatively, petitioner argues that if it is determined that some or all of the $10,801.00 amount was incurred for the purchase of tangible personal property and is not a cost of capital improvements, then a portion of the sale price for the respective unit equal to the cost of the appliances must be allocated to such items and be removed from consideration.

23. As part of the conversion costs, petitioner claimed $156,790.00 in "legal, accounting and engineering fees," of which $36,982.00 was disallowed by the Division. Petitioner concedes that documentation no longer exists for $6,201.00 incurred in 1988 for legal fees and therefore the Division properly disallowed that amount. Of the $5,490.00 which was disallowed because it represented refinancing, petitioner argues that it was not involved in any refinancing. It maintains that the amounts relate "to making funds available to purchasers so that they would be able to purchase, and Petitioner would be able to sell the Units" and as such are allowable conversion costs (Petitioner's brief, p. 13). Petitioner claims that, in 1989, it incurred legal fees, with respect to the litigation discussed in Finding of Fact "11," in the amount of $25,342.00 and additional legal fees relating to that litigation in the amount of $9,500.00. It argues that since these legal fees relate to claims made by the Montclair Townhouse Condominium board of managers, "which claims were directly associated with the Offering Plan and the Property," they are includible in OPP (Petitioner's brief, p. 13).

24. Petitioner contends that the $795,000.00 disallowed by the Division (***see,*** Finding of Fact "14") was paid to the developer for development and supervisory services rendered in connection with the renovation and rehabilitation of the units and therefore is an allowable conversion cost. It asserts that the services rendered included supervising

> the improvements made to the property and the units, assisting the sponsor in the assessment of the feasibility of the conversion, supervision of and coordination among the various professionals and consultants in the areas of market analysis, regulatory compliance and filings with the municipalities and the Attorney General's Office, coordination with the Condominium and overall supervision of the conversion process. (Petitioner's brief, p. 14.)

The record includes a copy of a check dated November 11, 1992 payable to Fishkill-Montclair Associates in the amount of $795,000.00. There are no explanatory notations on this check. The record does not include any agreements between Fishkill-Montclair Associates and petitioner, nor are there any bills from Fishkill-Montclair Associates.

25. Petitioner asserts that the $108,000.00 settlement payment to the condominium board of managers should be includible in OPP as a cost to create ownership interests in condominium form. It maintains that the litigation concerned the conversion of the property and the representations made in the offering plan concerning the condition of the property and improvements thereon.

26. Petitioner asserts that the Division incorrectly concluded that interest should be computed from October 15, 1989. It contends that the interest on the additional gains tax, if any, must be computed pursuant to the provisions of Technical Services memorandum TSB-M-86(3)R.

Petitioner also argues that the penalty for late payment should be abated. It maintains that, since it timely filed all gains tax forms and questionnaires, received and timely filed for each unit sold a Form TP-582 and timely paid the amount of gains tax reported on each unit's tentative assessment and return, the penalty provisions of Tax Law § 1446 do not apply. Petitioner further argues that there is no unpaid gains tax and, in fact, it has overpaid the gains tax due in this

matter. Notwithstanding that contention, petitioner maintains that any unpaid gains tax results from reasonable cause and not from willful neglect.

27. Lastly, petitioner maintains that the Notice of Determination in this matter was issued after the statute of limitations had expired. It argues that it sold the last unit on June 7, 1989. Petitioner maintains that at that point, it held the sole remaining unit which it did not intend to sell. It contends that it allowed the offering plan to become stale on December 13, 1991, and it was no longer effective after that date. Petitioner further maintains that, at the Division's request, on May 1, 1990, it filed its "project sell out" (i.e., the final update) in accordance with TSB-M-86(2)R. Petitioner argues that "[since] the last sale pursuant to the Plan occurred on June 7, 1989 and the required 'Tentative Assessment and Return' was timely filed and the gains tax reported thereon timely and properly paid;" the period for assessment of any additional gains tax and any related interest and penalty expired on June 7, 1992. (Petitioner's brief, pp. 18 - 19.) Alternatively, petitioner argues that since the final update was filed on May 1, 1990, the final date for assessment cannot be later than May 1, 1993. In its reply brief, petitioner also contended that the transfer took place on March 12, 1992 pursuant to the settlement agreement. It also argues that the transfer was clearly not made pursuant to the offering plan per se inasmuch as the board of managers could not occupy the unit. Furthermore, it maintains that the transfer was made pursuant to a litigation settlement, not by purchase and therefore is not a transfer for purposes of determining the three-year assessment period.

CONCLUSIONS OF LAW

A. Tax Law former § 1444[5] provides, as relevant:

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[5]The real property transfer gains tax imposed by Article 31-B of the Tax Law was repealed on July 13, 1996. The repeal applies to transfers of real property that occur on or after June 15, 1996. (***See,*** sections 171 through 180 of chapter 309 of the Laws of 1996.)

> (1) If a form required by this article is not filed, or if a form when filed is incorrect or insufficient, the amount of tax due shall be determined by the commissioner of taxation and finance from such records as may be obtainable . . . .
>
> * * *
>
> (3)(a) Statute of limitations. (1) General. No assessment of additional tax under this article shall be made after the expiration of three years from the date of transfer, or in the case of a transfer pursuant to a condominium or a cooperative plan or an aggregated transfer, after the expiration of three years from the date of the last transfer made pursuant to such plan or aggregated transfer . . . .

The first issue to be addressed is whether the Division's Notice of Determination is barred by the three-year statute of limitations set forth in Tax Law former § 1444(3)(a). The Division contends that the final transfer pursuant to the offering plan took place on April 30, 1992 when petitioner transferred unit #14A to the condominium association board of managers and, therefore, the Notice of Determination issued on March 27, 1995 was timely issued. Petitioner argues that the last sale pursuant to the offering plan took place on June 7, 1989 and, at that point, it held the sole remaining unit which it did not plan on selling. It avers that it allowed the offering plan to become stale. Petitioner further contends that it filed the final project update on May 1, 1990 and that the statute of limitations expired no later than May 1, 1993, long before the notice in question was issued. Alternatively, petitioner argues that the transfer of unit #14A took place on March 12, 1992 pursuant to a litigation settlement, not on April 30, 1992 as the Division contends. It asserts that the transfer was clearly not made pursuant to the offering plan inasmuch as the condominium board of managers could not occupy the unit. It further argues that because the transfer was made pursuant to a litigation settlement, not by a purchase, it should not be considered a transfer for purposes of determining the three-year assessment period.

For the following reasons, I find that the Notice of Determination is not barred by the statute of limitations.

B. Tax Law former § 1441, which became effective March 28, 1983, imposes a 10% tax upon gains derived from the transfer of real property located within New York State. For purposes of the gains tax, a transfer includes partial or successive transfers pursuant to a cooperative or condominium plan (Tax Law § 1440[7][b][iii]; ***see also***, ***Matter of Mayblum v. Chu***, 67 NY2d 1008, 503 NYS2d 316). However, the transfer gains tax is imposed on the overall condominium or cooperative plan, rather than on the individual units offered for sale pursuant to such a plan (***Matter of Mayblum v. Chu***, ***supra***; ***Matter of 1230 Park Assocs. v. Commr. of Taxation & Fin. of State of N.Y.***, 170 AD2d 842, 566 NYS2d 957, ***lv denied*** 78 NY2d 859, 575 NYS2d 455).

In the instant matter, pursuant to the terms of the offering plan, all 296 residential units along with each unit's undivided percentage interest in the common elements at the property were offered for sale (***see***, Finding of Fact "2"). There is no evidence that petitioner filed either an amendment, limiting the number of units to be sold to 295, or a notice of abandonment with the Attorney General (***see***, 13 NYCRR 23.1[n][2]). Furthermore, petitioner, in the project update documents submitted to the Division on May 1, 1990, computed the total anticipated gross consideration using the actual selling prices for 295 units and the "safe harbor" estimate for the unsold unit (***see***, Finding of Fact "10").

As for petitioner's alternative arguments concerning the transfer of unit #14A to the condominium board of managers, they are also without merit. The terms of the litigation settlement agreement specifically state that the agreement constitutes the contract of sale for unit #14A. The agreement also states that, in full settlement of all claims, petitioner agrees to transfer

unit #14A by deed and also pay $18,000.00 to the condominium association board of managers. (***See***, Finding of Fact "11.") There is also no evidence that the condominium by-laws in any way restrict ownership and occupancy of units (***see***, Real Property Law § 339-v[2][a], [c]).

The record clearly establishes that the last transfer pursuant to the offering plan was made on April 30, 1992. Therefore, pursuant to Tax Law former § 1444(3)(a)(1), the statute of limitations expired on April 30, 1995. The Division timely issued the Notice of Determination in this matter on March 25, 1995, prior to the expiration of the statute of limitations.

C. Tax Law former § 1440(1)(a) defines, in pertinent part, "consideration" as "the price paid or required to be paid for real property or any interest therein, less any customary brokerage fees related to the transfer if paid by the transferor . . . ." Tax Law former § 1440(3) defines "gain" as "the difference between the consideration for the transfer of real property and the original purchase price of the property." Tax Law § 1440 (former [5][a]) defined "original purchase price" for purposes of the gains tax as follows:

> "Original purchase price" means the consideration paid or required to be paid by the transferor; (i) to acquire the interest in real property, and (ii) for any capital improvements made or required to be made to such real property, including solely those costs which are customary, reasonable, and necessary, . . . incurred for the construction of such improvements. Original purchase price shall also include the amounts paid by the transferor for any customary, reasonable and necessary legal, engineering and architectural fees incurred to sell the property and those customary, reasonable and necessary expenses incurred to create ownership interests in property in cooperative or condominium form, as such fees and expenses are determined under rules and regulations prescribed by the tax commission.

The regulations set forth further descriptions, with illustrative examples, concerning what constitutes acquisition costs and capital improvements that would reduce the "gain" subject to tax (20 NYCRR 590.15, former 590.16, former 590.17 and former 590.39). Under 20 NYCRR 590.15, certain preacquisition and acquisition costs may be included in the computation of the

original purchase price such as legal and other professional fees, fees for marketing and feasibility studies and the cost of lease buy-outs. Under former 590.16, costs directly and indirectly related to capital improvements made to the real property may be included in the original purchase price. Costs directly related to capital improvements include consideration paid to contractors to make the capital improvement and the cost of built-in appliances. Indirect project costs must be "specifically identified with a project" (20 NYCRR former 590.16[d]) and include such costs as construction administration costs. The regulation provides that:

> [t]he full amount of indirect project costs that clearly relate to a specific project, such as costs associated with a field office at a project site and the administrative personnel that staff the office, may be added to the cost of the capital improvement (***id***.).

However, the regulation also provides that general and administrative costs such as corporate management salaries, corporate office expenses and "similar costs which are generally incurred by all enterprises in the conduct of business," may not be included as costs related to capital improvements.

D. Petitioner contends that the full amount of the brokerage fees, $1,609,368.00, which it paid to the RM Agency and Innovative as selling agents, should be allowed as customary brokerage fees to reduce "gross consideration" in the determination of "consideration" pursuant to Tax Law former § 1440(1)(a). It asserts that the evidence proves that it incurred and paid the full amount of the claimed brokerage fees. Relying on the RM Agency agreement, the Division allowed 5.5% of the sales prices of all units except the last unit, to wit: $1,041,202.00, as allowable brokerage fees (***see***, Finding of Fact "14"). The only brokerage agreement in the record is the RM Agency agreement which the Division used as the basis for its calculation of allowable brokerage fees (Findings of Fact "7" and "14"). It cannot be determined, from the

evidence presented, whether a brokerage agreement existed between petitioner and Innovative or whether Innovative provided services which qualified as brokerage expenses. Since petitioner has failed to sustain its burden of proof, no additional brokerage fees in excess of the amounts determined by the Division will be allowed (***see***, 20 NYCRR 3000.15[d][5]).

E. Petitioner contends that the Division improperly disallowed $132,970.00 of consideration it paid to contractors. The disallowed amount is comprised of $100,170.00 for "lost rents" paid to the prior owner of the property and $33,000.00 for furniture and fixtures for models 86 and 87. Petitioner did not submit any documentary substantiation for either of these expenses. The only explanation for these amounts is contained in petitioner's brief. In the brief, petitioner explained that the "lost rent" represented an additional cost of the improvements to the property and an economic cost to petitioner of the conversion of the property to condominium ownership. It asserted that the amount was paid so that improvements could be made and the conversion could proceed when the units became available. Petitioner contends that "the $33,000 amount represents amounts incurred to renovate the model units" (Petitioner's brief, p. 10). However, there is no further elaboration or explanation of exactly what types of renovations were made in the two units.

Petitioner has failed to submit adequate substantiation to support its claim that either of these expenses should be includible in the original purchase price. The Tax Appeals Tribunal has consistently held that taxpayers must have documents to substantiate costs claimed as adjustments to original purchase price (***see***, ***Matter of V & V Properties***, Tax Appeals Tribunal, July 16, 1992). The Division's disallowance of $132,970.00 of claimed consideration paid to contractors is sustained.

F. Petitioner's claim regarding appliances must be rejected. On this ground, petitioner has offered no specifics regarding the type of appliances or the nature or manner of their affixation to the premises (***see***, Paragraph "22"). While 20 NYCRR former 590.16 provided that *built-in* appliances may be allowable in original purchase price as a cost of capital improvements, there is no evidence in the record from which to conclude that the costs claimed by petitioner were incurred for built-in appliances or otherwise constituted capital improvements made to real property.

G. Petitioner contends that the Division's disallowance of $5,490.00 of legal expenses associated with refinancing is improper. While a general explanation of what these legal expenses represented is contained in petitioner's brief, there is no evidence to prove that the legal expenses were allowable expenses (***see***, ***Matter of V & V Properties***, ***supra***). Therefore, the Division's disallowance of $5,490.00 in legal expenses associated with refinancing is sustained.

H. The Division's disallowance of the claimed developer and supervisory fee of $795,000.00 must be sustained. Other than a canceled check, there is no evidence to show what Fishkill-Montclair Associates did for such a substantial fee and whether the claimed developer and supervisory fee was an allowable expense (***see***, Paragraph "24").

I. Petitioner contends that the $108,000.00 which it paid to settle litigation with the Montclair Townhouse condominium association is properly includible in original purchase price as a cost to create ownership interests in condominium form. It argues that the litigation concerned the conversion of the property and the representations made in the offering plan concerning the condition of the property and improvements thereon. The Division contends that these claimed expenses were properly disallowed since the expenses were not incurred to create ownership interests but rather were for the settlement of a lawsuit.

The character of a settlement payment is best determined by looking at the litigation documents (***Raytheon Products Corp. v. Commr.***, 144 F2d 110, 44-2 US Tax Cas ¶ 9425, ***cert denied*** 323 US 779; ***see also***, ***Matter of Harkness Company***, Tax Appeals Tribunal, May 16, 1991). Based on the record, I must find that the payment represented settlement of two lawsuits to avoid additional litigation costs. The only litigation document in the record is the settlement agreement executed by the parties to two actions (***see***, Finding of Fact "11"). That agreement specifically states that it was entered into by the parties "to avoid the expense and continuation of litigation and without acknowledging liability of any party" ***(see***, Finding of Fact "11"). Without copies of the additional litigation documents, such as the complaints, filed in the two actions, it is impossible to determine whether the expenses were incurred to create ownership in property. Therefore, the $108,000.00 payment to the Montclair Townhouse condominium association was properly excluded from original purchase price. Petitioner has claimed legal fees of $25,342.00 incurred in 1989, as well as legal fees of $9,500.00 with respect to this litigation. Legal fees related to the litigation are also not includible in original purchase price since they were specifically for litigation and not the sale of the property (***Matter of Benacquista, Polsinelli & Serafini Management Corporation v. Commissioner of Taxation and Finance of State of New York***, 191 AD2d 80, 598 NYS2d 829). It is noted that the invoice from the New Paltz law firm does indicate that the $9,500.00 legal fee included preparation of the deed for unit #14A and attendance of an attorney at that closing (***see***, Finding of Fact "19"). However, since there is no breakdown of the legal fee, it is impossible to determine what portion of the legal fees are attributable to the transfer of unit #14A. Therefore, all $9,500.00 of the legal fees must be determined to be litigation expenses.

In sum, the Division's disallowance of the claimed litigation settlement payment and the related legal fees must be sustained.

J. Petitioner contends that the Division improperly used October 15, 1989 as the beginning date for the computation of interest due on the additional gains tax asserted in the Notice of Determination. It argues that interest on the additional gains tax, if any, must be computed pursuant to the provisions of TSB-M-86(3)(R). TSB-M-86(3)(R) in the paragraph entitled "Effect of the Safe Harbor Estimate" states, in pertinent part:

> A transferor who uses the appropriate Safe Harbor Estimate to estimate the consideration to be received on the Unsold Units will be treated, during the period that such transferor is holding Unsold Units to sell pursuant to the cooperative or condominium plan ("Sell Out Period"), as if he had estimated this consideration at the exact amount that is actually received on these units when sold. Accordingly, penalty and interest will not accrue against such a transferor for the underpayment of Gains Tax during the Sell Out period, to the extent that such underpayment is the result of the excess of the actual consideration received on the sale of units over the Safe Harbor Estimate of consideration used for these units. *Penalty and interest may accrue during the Sell Out Period, however, for the underpayment of Gains Tax resulting from the understatement of any other component of the Plan Consideration or the overstatement of original purchase price.* (Emphasis supplied.)

Petitioner's argument is without merit. The auditor's computation of interest in this matter followed the guidelines set forth in TSB-M-86(3)(R) in the calculation of interest and penalty. In this case, the additional gains tax determined to be due resulted from petitioner's overstatement of original purchase price. The Division used the correct date, October 15, 1989, as the starting point for the computation of interest due on the additional gains tax determined to be due.

K. The final issue to be determined is whether petitioner is liable for the penalty for failure to pay the gains tax within the time required. Tax Law former § 1446(2)(a) provides , in pertinent part, as follows:

> Any person failing to file a tentative assessment and return or to pay any tax within the time required by this article shall be subject to a penalty of ten per centum of the amount of tax due . . . . Provided, however, that the minimum penalty for each transfer of real property or partial or successive transfer of real property shall be one hundred dollars. If the commissioner determines that such failure or delay was due to reasonable cause and not due to willful neglect, the commissioner shall remit, abate or waive all such penalty . . . .

Petitioner argues that it timely filed the tentative assessment and return for each unit's transfer. It also argues that all of the disputed items were properly reported and disclosed on the May 1990 Complete Project Update. Petitioner asserts that reasonable cause exists to abate the penalty because "any failure to pay the Gains Tax was based on well reasoned conclusions that the transfers of the 'taxable units' were properly reported" (Petitioner's reply brief, p. 8).

Petitioner's request for relief from the penalty imposed is based upon having adopted an interpretation of the law different from that taken by the Division. With respect to gains tax penalties, it has been held that: "the failure to pay a tax due to a different legal interpretation of a statute need not be considered 'reasonable cause'. In fact, if it were so considered, [the Commissioner] would rarely if ever be entitled to levy such penalties" (***Matter of Auerbach v. State Tax Commn***., Sup Ct, Albany County, March 27, 1987, Williams, J., ***affd*** 147 AD2d 390, 536 NYS2d 557). Accordingly the imposition of the penalty is sustained.

L. The petition of Montclair Sponsor Corporation is denied and the Notice of Determination, dated March 27, 1995, is sustained.

DATED: Troy, New York
January 28, 1999

/s/ Winifred M. Maloney
ADMINISTRATIVE LAW JUDGE