STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
HENRY MENDLER	:	DECISION DTA No. 805824
for Revision of a Determination or for Refund of Real Property Transfer Gains Tax under Article 31-B of the Tax Law for the Year 1985.	:	

Both the Division of Taxation and petitioner Henry Mendler, 157 Seventh Avenue South, New York, New York 10014 filed exceptions to the determination of the Administrative Law Judge issued on August 13, 1992. Petitioner appeared by Fred Lichtblau, Esq. The Division of Taxation appeared by William F. Collins, Esq. (Andrew J. Zalewski, Esq., of counsel).

Petitioner filed a brief in support of his exception and in opposition to the Division of Taxation's exception. The Division of Taxation filed a brief in support of its exception. The Division of Taxation's request for oral argument was granted. The Division of Taxation withdrew its request for oral argument on April 8, 1993, which date began the six-month period for the issuance of this decision.

The Tax Appeals Tribunal renders the following decision per curiam.

ISSUES

I. Whether petitioner was entitled to an exemption from real property transfer gains tax pursuant to Tax Law § 1443(1) because the consideration received for three of the four units of the cooperative conversion plan totaled less than one million dollars.

II. Whether the anticipated consideration for cooperative shares allocated to an unsold unit in a cooperative building should take into account that the unit is encumbered by a life estate.

III. Whether the penalty imposed pursuant to Tax Law § 1446(2)(a) should be abated.

FINDINGS OF FACT

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

Petitioner, Henry Mendler, purchased a four-story, four-unit "brownstone" building, located at 11 West 11th Street in New York City, for which he paid $125,000.00 in 1967. Three of the four units in the building were rented and the fourth unit was occupied by petitioner and his family as a personal residence.

On March 14, 1973, petitioner and his wife, Judith Marion Mendler, entered into a separation agreement which was incorporated without merger into a Supreme Court Judgment of Divorce, entered on February 6, 1974.

One of the provisions of the separation agreement provided Judith Mendler with a life estate in the fourth unit as follows:

> "the Wife shall have the right to the exclusive occupancy of the present marital apartment at 11 West 11th Street, New York, New York, as her personal residence. The Wife is herewith conveying all of her right, title and interest in the real property known as 11 West 11th Street, New York, New York to the Husband subject to the Wife's right to occupy said apartment free of rent for the time, and under the conditions hereinafter set forth. In connection therewith, it is further understood that the Wife shall not be obliged to pay for the maintenance of the air conditioning system, the major appliances presently contained in said apartment, all utilities including electric, gas and telephone (at a cost consonant with present usage only). Any obligation deemed necessary by this paragraph in order to satisfy the Wife's enjoyment of her life estate may be made directly to her, or directly to the appropriate creditor.
>
> It is expressly agreed that the wife's rights under this paragraph shall terminate at the earliest of (a) the Wife's death, (b) her intentional vacature or abandonment of said apartment, or (c) if the Wife is not the sole and exclusive occupant of said apartment. As used herein, 'abandonment' is understood to mean the continuous absence of the Wife from the premises for a period of no less than four months. The provisions of this paragraph shall be binding upon the present and any further owner of premises 11 West 11th Street, New York, New York and the Husband expressly covenants that he will not convey said premises except subject to the provisions herein contained. Upon the termination of the wife's occupancy, the owner of said premises shall have the right to re-enter and peaceably take possession of the apartment."

Petitioner sponsored a cooperative offering plan, dated July 28, 1983, with respect to the building located at 11 West 11th Street. The offering plan contained the following schedule of anticipated purchase prices of shares allocated to the four units:

Unit	Share Allocations	Cash purchase price at $600 per share	Approximate amount of mortgage allocable to shares $375 per share
C	300	$180,000	$112,500
M	325	195,000	121,875
1	375	225,000	140,625
2	600	360,000	225,000
	1,600	$960,000	$600,000

The offering plan was amended three times. The first amendment, dated June 5, 1984, reduced the principal of the wraparound mortgage from $600,000.00 to $440,000.00 thereby also reducing the amounts allocable to the apartments to $275.00 per share. The second amendment, dated August 27, 1984, reduced the price of Unit M to $570.00 per share in lieu of $600.00 per share, or $185,252.00. The purchaser of Unit M became a tenant pursuant to an interim lease in August 1984. The second amendment also declared the offering plan effective on August 27, 1984. In the third amendment, dated March 29, 1985, it was noted that on January 14, 1985 the title closing took place whereby petitioner conveyed the entire 11th Street property to a cooperative corporation, 11 West 11th Street Owners Corp., pursuant to the offering plan. It was also noted in the third amendment that on the closing date the property was encumbered by a wraparound mortgage in the principal amount of $440,000.00 which wrapped around a superior mortgage in the principal amount of $49,000.00.

By May of 1985, three of the units were sold for the following purchase prices:

Unit	
1	$205,000.00
M	185,250.00
C	170,000.00
	$560,250.00

In addition, a brokerage fee of $11,115.00 was paid by the transferor corporation with respect to Unit M.

Petitioner's ex-wife, Judith Mendler, occupied Unit 2 in accordance with the provisions of the separation agreement. In an affidavit submitted by petitioner, he stated the following:

"Since our divorce in February, 1974, I have made numerous serious efforts to 'buy out' my ex-wife's life estate and relocate her. I engaged counsel for this purpose, who contacted my former wife's attorney. All my offers were rejected, and my former wife refused to move -- at any price. She refused to even make any counterproposals, and insisted that she remain in the apartment indefinitely. She insists on remaining in the apartment pursuant to the Separation Agreement and Judgment of Divorce, rent free and utility free (which I pay) for the remainder of her life."

In May of 1987, the Division of Taxation ("Division") commenced an audit of the cooperative purchase.

By letter dated October 29, 1987, petitioner's accountant objected to information contained in the Division's audit report and stated the following:

"In reviewing your audit report we have noted your anticipated value of the unsold apt. #2 at $342,000.00.[1]

The market for co-opapartments [sic] has been exceptionally soft and will apparently remain that way. We feel the anticipated selling price is considerably less and thus affects your computations.

We are enclosing two independent appraisals which reflect the value of the unsold apartment.

We sincerely hope you will adjust your computations to reflect the true world value [sic] and not the anticipated value.

We are enclosing a check in the amount of FIVE THOUSAND DOLLARS ($5,000.00) as a partial payment of any tax due."

Attached to this letter were two letters appraising Unit 2 for $240,000.00 and $230,000.00, respectively.

Using the anticipated purchase price of $240,000.00 for Unit 2, the auditor calculated real property transfer gains tax due as follows:

	Actual	Anticipated	Total
Cash consideration	$560,250	$240,000	$ 800,250
Less reserve fund			10,000
Estimated cash consideration			790,250

[1] Apparently, petitioner and 11 West 11th Street Owners Corp. filed a transferee and transferor questionnaire on December 24, 1984 stating the anticipated sale of Unit 2 on January 14, 1985 by the corporation to petitioner for $342,000.00. The transferor questionnaire stated anticipated gains tax due in the amount of $11,586.00 for the sale of Unit 2.

(Plus) mortgage indebtedness	440,000
Gross consideration	1,230,250
(Minus) brokerage commissions	(11,115)
(Minus) original purchase price	(510,365)
Anticipated gain	708,770
Anticipated tax at 10%	70,877
Anticipated tax per share (based on 1,600 shares)	44.298

The auditor multiplied the anticipated $44.298 tax per share by the 1,000 shares actually sold to determine total gains tax due of $44,298.00.

The Division issued a Notice of Determination, dated January 20, 1988, stating the following amounts due:

Tax	$44,298.00
Penalty	15,504.00
Interest	13,088.00
Total	72,890.00
Paid 11-02-87	5,000.00
Balance	67,890.00
Interest (11/3/87-2/21/88)	1,197.37
Total	$69,087.37

A conciliation conference was held on August 28, 1990. The conferee issued a Conciliation Order, dated February 8, 1991, sustaining the statutory notice.

By petition dated April 16, 1991, petitioner challenged the statutory notice arguing that the assessment was based on incomplete and erroneous facts. Petitioner contended that the evaluation of Unit 2 at $240,000.00 failed to take into account the deteriorating market conditions with respect to cooperative apartments and the fact that Unit 2 was encumbered by the life estate held by Judith Mendler. Petitioner asserted that because of the life estate, Unit 2 had only nominal value and that the value of Unit 2 "was impossible and incapable of accurate assessment in the tax year, 1985, and at the present time or at the time of audit." Petitioner concluded that there was no market for Unit 2 at the time of conversion to cooperative status and that therefore no tax was due, or, if any tax was due, such tax was a "far lesser amount than determined by the commissioner."

The Division filed an answer, dated June 25, 1991, stating, inter alia, that the notice assessed gains tax for the transfer of 1,000 shares allocated to three cooperative units.

In its submissions, petitioner filed two affidavits in support of its contention that Unit 2 was overvalued at $240,000.00 by the Division's auditor. One affidavit was by David B. Malkin, who was a Chartered Financial Consultant, a Chartered Life Underwriter and a principal in New Jersey Life & Casualty Associates, Inc., specializing in financial planning for individuals and corporations. He stated that he was fully familiar with actuarial methods and practices and that assuming Judith Mendler was 60 years of age in 1985,[2] in reasonably good health and with a leisurely lifestyle, his opinion was, based on the Standard Ordinary Mortality Table used in 1985, that Judith Mendler had a life expectancy of an additional 21.25 years, or to age 81.

A second affidavit by Brian R. Corcoran was submitted. Mr. Corcoran was a member of the Board of Directors, an Executive Vice President, and the National Director of the Appraisal Division of Cushman & Wakefield, Inc. In his affidavit, Mr. Corcoran set forth his analysis of the market value of Unit 2 in 1985 as follows:

> "Generally, apartments which are encumbered by leases to either rent controlled or rent stabilized tenants sell in the range of 20% - 25% of the market value of the same apartment if it were vacant and available for use by the purchaser. The reason for this deep discount is the negative carrying charges which exist in terms of maintenance and financing charges, which are usually in excess of the regulated rents which can be collected from rent controlled or rent stabilized tenants and the uncertainty regarding when possession of the apartments might occur.
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> The subject apartment is encumbered by a guaranteed life tenancy which has been granted to the former owner's wife under a separation and divorce agreement. This life tenancy carries with it no obligation for maintenance of the apartment and no obligation for any carrying charges, which rests solely with the owner. In this regard, the subject apartment is considered less attractive than the typical occupied cooperative because there is no rental income being paid to offset the cooperative maintenance charges. For these reasons, it is my opinion that the likely range in market value for the subject apartment would be between 10% and 20% of the value of the apartment as if it were vacant. Assuming, therefore, a market value of $240,000.00 if unencumbered and transferable in a vacant state, the market value for the subject apartment would have been between $24,000.00 and $48,000.00 during the subject tax year, 1985."

OPINION

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[2] According to petitioner's affidavit, Judith Mendler was born on December 3, 1925.

The Administrative Law Judge rejected petitioner's argument that only the actual consideration received for sold units should be used to determine whether the exemption provided by section 1443(1) of the Tax Law for transfers for less than $1 million applies. Relying on Tax Law § 1442 and Mayblum v. Chu (67 NY2d 1008, 503 NYS2d 316), the Administrative Law Judge concluded that the total consideration anticipated under a cooperative plan is to be considered when applying the $1 million exemption. Applying this rule, the Administrative Law Judge determined that "at the time of the audit, the Division correctly calculated the amount of gains tax due based on the information provided to it -- the actual and anticipated consideration for all four units" (Determination, conclusion of law "B"). However, the Administrative Law Judge also found that at the hearing petitioner had established that the life estate which encumbered Unit 2 affected the market value of the unit and that the anticipated consideration should take into account the life estate. The Administrative Law Judge also held that petitioner had established that the value of Unit 2 as encumbered was between $24,000.00 and $48,000.00. Utilizing even the lowest value of $24,000.00 still caused the anticipated consideration for all of the units to exceed $1 million; therefore, the Administrative Law Judge concluded that the three units sold were subject to the gains tax. The Administrative Law Judge recalculated the tax per share using the $48,000.00 value and stated that penalty and interest should also be reduced accordingly. Finally, the Administrative Law Judge determined that petitioner's "alleged belief" that he was not subject to gains tax was contradicted by a plain reading of the statute and the Option A and B payment methods established by the Division and, therefore, his failure to pay was not based on reasonable cause.

On exception, petitioner argues that for purposes of determining whether the $1 million exemption of section 1443 applies, only the consideration, as defined by section 1440 of the Tax Law, actually received for an actual transfer is relevant. Petitioner contends that as long as the consideration received, or to be received, for actual transfers is less than the statutory exemption, the provisions of section 1442 of the Tax Law, relating to payment, are not

triggered. In the alternative, petitioner argues that the statutes are ambiguous and petitioner is entitled to a liberal construction in his favor. Petitioner also argues that penalty should be abated because "petitioner was trapped into non-payment by the statutory ambiguities which existed" (Petitioner's brief, p. 20). Finally, petitioner contends that the Administrative Law Judge erred in determining the value of Unit 2 at the high end of its value range, and that the Administrative Law Judge should have chosen the mean value, i.e., $36,000.00.

In its exception, the Division contends that its estimate of the consideration to be received by petitioner on the transfer of Unit 2 was reasonable and that "the record does not support a determination that the petitioner reasonably anticipated to sell unit '2' for $48,000 or any amount below $240,000. The petitioner has, therefore, failed to establish that the Division of Taxation's determination was erroneous or improper" (Division's brief, p. 4). The Administrative Law Judge erred, asserts the Division, by determining that the anticipated consideration on unit sales is the equivalent of the present day appraised value of the units. The Division contends that "[t]he present day fair market value of unsold occupied units may be useful in determining the anticipated consideration only when unsold units are not being held for future sale at the time they become vacant" (Division's brief, p. 6). In the alternative, the Division argues that petitioner failed to prove that the market value of Unit 2 was $48,000.00.

In response to the Division's exception, petitioner argues that he established that the encumbrance reduced the value of Unit 2 to between 20% - 25%. Applying these percentages to the market value of Unit 2, which was ascribed to it by the Division as if it were an unencumbered apartment, led petitioner to the valuation of between $24,000.00-48,000.00

The Division did not respond to petitioner's exception.

We affirm the determination of the Administrative Law Judge.

Petitioner seeks to interpret the $1 million exemption contained in section 1443(1) of the Tax Law apart, and in isolation, from the other provisions of Article 31-B. As the Administrative Law Judge noted, section 1442(b) of the Tax Law provides in part that:

> "[f]or purposes 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" (emphasis added).

We agree with the Administrative Law Judge that this statutory provision indicates that the total consideration anticipated under a cooperative plan is to be considered in calculating the amount of tax due on each transfer and that a calculation of tax requires a calculation of whether the $1 million exemption applies.

We also believe that the sentence in section 1442(b) following that relied on by the Administrative Law Judge supports the conclusion to reject petitioner's argument. This sentence states: "[p]rovided, however, in the case of partial or successive transfers, other than transfers pursuant to a cooperative or condominium plan, no tax is due until the consideration paid or required to be paid for the real property transferred equals or exceeds one million dollars." If, as petitioner asserts, the general rule under the gains tax was that no tax was due on multiple transfers until the consideration received on the actual transfers had exceeded the $1 million threshold, this sentence would be unnecessary. The fact that the Legislature enacted the rule that petitioner urges, but excluded transfers pursuant to a cooperative plan from it, compels the conclusion that the Legislature intended to apply the $1 million exemption to cooperative conversions based on the consideration anticipated to be received.

We also agree with the Administrative Law Judge that our reading of:

> "[t]he statute is further supported by the Court of Appeals' decision Mayblum v. Chu (67 NY2d 1008, 503 NYS2d 316), wherein the court stated that gains tax is imposed on the overall cooperative conversion itself which is to be treated as a single transfer for computing the tax, whereas the actual payment of the tax is due upon the subsequent transfer of shares to individual purchasers pursuant to the cooperative plan (see also, Matter of 1230 Park Associates v. Commr. of Taxation and Finance, 170 AD2d 842, 566 NYS2d 957, lv denied 78 NY2d 859, 575 NYS2d 455; 20 NYCRR 590.22)" (Determination, conclusion of law "A").

After the issuance of the Administrative Law Judge's determination in this case, the Appellate Division, Third Department, issued its opinion in Matter of Albe Realty Co. v. Tax Appeals Tribunal (___AD2d___, 598 NYS2d 602). In Albe, the court rejected a taxpayer's claim for the section 1443(1) exemption where the taxpayer had transferred 12 of the 46 units offered for sale and the consideration for those units was less than $1 million. Citing 1230 Park Assocs., the Court denied the exemption because "it is undisputed that the consideration to be generated by petitioner's overall cooperative conversion plan exceeds $1 million" (Matter of Albe Realty Co. v. Tax Appeals Tribunal, supra). The Albe decision provides additional support for our conclusion in this case.

It follows from the above discussion that we do not believe that the statute was vague and that this vagueness trapped petitioner into noncompliance with the law. Accordingly, we affirm the Administrative Law Judge's determination to impose penalties for the reasons stated in the determination.

Turning to the Division's exception, we see no basis to disturb the Administrative Law Judge's determination that petitioner provided sufficient evidence to warrant reducing the anticipated consideration for Unit 2 from $240,000.00 to $48,000.00. Petitioner's principal evidence on this point consisted of the affidavit of Brian R. Corcoran, which stated Mr. Corcoran's credentials and the means by which Mr. Corcoran arrived at the $24,000.00 to $48,000.00 value. The affidavit states that apartments that are encumbered by leases to either rent controlled or rent stabilized tenants sell in the range of 20% - 30% of the market value of the same apartment if it were vacant. Because the life estate that encumbered Unit 2 generated no rent stream, Mr. Corcoran estimated that it was worth less than the typical occupied cooperative and opined that the value was between 10% and 20% of the value of the apartment if it were vacant. Mr. Corcoran finished his calculation by applying this range of percentages to the value of $240,000.00, which was assumed to be the market value of Unit 2 if vacant.

Although, as asserted by the Division, the affidavit of Mr. Corcoran may not constitute an appraisal, we conclude that it is sufficient for the purpose offered by petitioner, i.e., to provide

an estimate of anticipated consideration with respect to Unit 2. The Division has not directed us to any official statement by it, and we have found none on our own, where the Division has established rules that are required to be followed to estimate anticipated consideration. Thus, we know of no regulation, Technical Services Bureau Memorandum or instruction to a gains tax form that tells a transferor what method must be followed to estimate the anticipated consideration. The rules contained in TSB-M-86-(3)-R, the "Safe Harbor Estimate for Transfers Pursuant to Condominium and Cooperative Plans," assure taxpayers that if they follow the safe harbor estimating rules, the taxpayers will not be subject to penalty and interest on underpayment (see, Matter of Belvedere Garden Assocs., Tax Appeals Tribunal, June 18, 1992); however, there is nothing in this TSB that requires that the safe harbor rules for estimating consideration be followed. If the Division has not published any rule directing transferors to utilize a certain means to establish the anticipated consideration on unsold units, we do not see how the Division can now insist that this estimate must be based on an appraisal. Therefore, we agree with the Administrative Law Judge that the evidence establishes that the anticipated consideration for Unit 2 is in the range of $24,000.00 to $48,000.00.

For the same reason, we reject the Division's contention that, even if established, the market value of the encumbered apartment could not be used to estimate anticipated consideration. The Division asserts that petitioner could only anticipate the consideration for Unit 2 at an amount less than $240,000.00 if he proved that the apartment had been offered for sale, or the subject of a contract, as an encumbered unit, at a price below that set forth in the offering plan. Again, the Division has not directed us to any source for these rules for estimating anticipated consideration, but instead appears to be proposing them for the first time in these proceedings. We reject this attempt and conclude that the Administrative Law Judge properly accepted petitioner's estimate of anticipated consideration with respect to Unit 2.

In its brief in support of its exception, the Division cautions that our decision in this case could have far reaching consequences with respect to estimates of consideration in noneviction cooperative plans. We respond that if the Division believes that it is critical to have a rule that

requires sponsors in noneviction cooperatives to prove that they intend to sell occupied units as occupied before the sponsor is entitled to estimate the anticipated consideration using a unit's encumbered value, the Division should exercise its rule making authority to adopt such a rule.

Finally, we find no basis for petitioner's contention that the Administrative Law Judge should have used the mean of the range of value for Unit 2 rather than its highest point to calculate tax per share and interest and penalty.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exceptions of Henry Mendler and the Division of Taxation are denied;

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

3. The petition of Henry Mendler is granted to the extent indicated in conclusion of laws "C" and "E" of the determination of the Administrative Law Judge, but is otherwise denied; and

4. The Division of Taxation is directed to modify the Notice of Determination dated January 20, 1988 in accordance with paragraph "3" above, but such Notice is otherwise sustained.

DATED: Troy, New York
September 23, 1993

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

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