STATE OF NEW YORK

TAX APPEALS TRIBUNAL

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| In the Matter of the Petition | : | |
| of | : | |
| **SOGL ASSOCIATES** | : | DECISION<br>DTA No. 809356 |
| 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 SOGL Associates, c/o John A. Souto Co., Inc., 144 Bleecker Street, New York, New York 10012, filed an exception to the determination of the Administrative Law Judge issued on August 12, 1993. Petitioner appeared pro se. The Division of Taxation appeared by William F. Collins, Esq. (Kenneth J. Schultz, Esq., of counsel).

Petitioner submitted a brief in support of its exception. The Division of Taxation submitted a letter in opposition. Petitioner filed a reply letter brief, received on February 14, 1994, which began the six-month period to issue this decision. Petitioner's request for oral argument was denied.

Commissioner Koenig delivered the decision of the Tax Appeals Tribunal. Commissioner Dugan concurs.

## *ISSUES*

I. Whether the Division of Taxation properly modified petitioner's original acquisition costs, capital improvement costs and costs of cooperative conversion in its recomputation of petitioner's original purchase price.

II. Whether petitioner has established reasonable cause for its failure to pay the tax allegedly due.

## *FINDINGS OF FACT*

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

On March 16, 1989, the Division of Taxation ("Division") issued to petitioner, SOGL Associates, a Notice of Determination for real property gains tax for tax due of $105,314.00, penalty of $36,859.90 and interest of $61,167.02, for a total assessment of $203,390.92. Additionally, on the same notice, tax was assessed for the period ended July 1, 1986 in the sumof $16,058.00, penalty of $5,620.30 and interest of $4,071.60, for a total due of $25,749.90. The assessments for both years totalled $229,090.82.

The notice indicated that the assessments were reached as a result of a "recent field audit conducted by our New York District Office."

Although there was initially a question of petitioner's timely filing of a request for a conciliation conference with the Bureau of Conciliation and Mediation Services ("BCMS"), that issue has been resolved. However, no conference was ever held in this matter prior to formal hearing.

Petitioner was the sponsor of a plan to convert to cooperative ownership real property located at 240-242 West 23rd Street, New York, New York. The transfer of title to the premises from SOGL Associates to 240 West 23rd Owners Corp. (the "CHC") took place on February 10, 1984 and was adjourned and concluded on February 14, 1984. (Sixth Amendment to the Offering Plan.) However, no closing statement was ever produced on audit or at any time prior to or at hearing.

It was never established in the record whether or not petitioner filed returns for real property gains tax upon the transfer of shares in the cooperative conversion. The field audit report stated only that no tax was ever paid by petitioner. This fact was never challenged or controverted by petitioner.

Several months prior to the closing of title, a Certificate of Occupancy was issued by the City of New York for the premises at 240 West 23rd Street stating that said property "conforms substantially to the approved plans and specifications and to the requirements of all applicable laws, rules, and regulations for the uses and occupancies specified herein." The Certificate of Occupancy was dated October 19, 1983.

Upon audit, petitioner was asked to substantiate various elements of its original purchase price, including acquisition expenses, capital improvements, and cooping expenses. The auditor examined the documents provided by petitioner and made several adjustments. Petitioner had asserted an original acquisition cost of $597,270.00, capital improvements of $2,046,080.00 and cooping expenses of $1,339,070.00. However, on audit, the Division allowed only $488,650.00, $1,973,095.00 and $647,158.00 for those same items, respectively.

The Division allocated $2,962,500.00 for actual cash consideration which was taken directly from a schedule of unit sales. The anticipated consideration was gleaned from the Offering Plan, $255,142.00, yielding total consideration of $3,217,642.00. There were no grandfathered units, but $5,000.00 was allowed for reserve and working funds, leaving cash consideration of $3,212,642.00. The original mortgage indebtedness was $1,200,000.00 which, when added to the cash consideration, yielded total taxable consideration of $4,412,642.00. Another $121,013.00 was allowed for brokerage commissions,[1] leaving a balance of $4,291,629.00.

The original purchase price was erroneously increased by 5% due to a misallocation for commercial space which did not exist in the building. Therefore, the original purchase price as calculated, $3,108,903.00, had to be diminished by 5% or $155,445.00. This yielded an original purchase price of $2,953,458.00.

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[1]The anticipated broker's commission on the one unsold unit should have been $15,309.00 (6% x $255,142.00) not $12,900.00 as allowed. The Division conceded this at hearing and in its brief.

Therefore, an original purchase price of $2,953,458.00 was subtracted from the balance listed above leaving an anticipated gain of $1,338,171.00, an anticipated tax of $133,817.00 or $133.817 per share (1,000 total shares in Offering Plan). Since only 907 shares had been sold at the time of the audit, the tax on those totalled $121,372.00 (907 x $133.817).

With regard to the modifications made by the Division to original purchase price under original acquisition costs, $4,300.00 was disallowed in legal fees because they were for the preparation of partnership papers; also, $104,320.00 in relocation of tenants costs were reallocated to cooping costs and reduced to $95,000.00 for lack of substantiation.

In the area of pre-closing capital improvements, the Division disallowed $87,707.00 because of lack of substantiation. Those costs were as follows:

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| a) real estate taxes | $ 4,999.00 |
| b) professional fees | 23,930.00 |
| c) architects fees | 13,376.00 |
| d) repairs and maintenance | 7,334.00 |
| e) insurance | 34,164.00 |
| f) utilities | 7,264.00 |
| g) filing fees | 5,367.00 |
| Sub Total | $ 96,434.00 |
| less allowance for construction loan interest and closing costs | 8,727.00 |
| Total | $ 87,707.00 |

The Division also made adjustments to capital improvement costs which were incurred post-closing. The Division allowed $11,022.00 more than claimed by petitioner. When this figure was subtracted from the $87,707.00 disallowed for pre-closing capital improvements, the result was a total disallowance of $76,685.00 for capital improvements.

In the area of cooping expenses there were three categories: pre-closing, at closing and post-closing. The Division disallowed $602,379.00 in pre-closing cooping expenses for the reason that there was never any substantiation shown or the expenses were not allowable. The great majority of the claimed expenses were loan interest payments.

At closing, the Division reduced expenses by $117,422.00. One large expense disallowed was the interest on an alleged construction loan which was never substantiated to the Division. There were also satisfactions of mechanics' liens and a cash settlement on a heating system.

The Division disallowed $57,111.00 in post-closing cooping expenses comprised entirely of interest on construction loans which were incurred after the construction period had ended.

The Division considered the construction period to have ended when the building was substantially completed and ready to be occupied. The Division used the issuance of the Certificate of Occupancy as an indication of the state of readiness.

Although petitioner did not receive a BCMS conference, it did have an informal conference at its place of business with two auditors, at which time nothing was produced to substantiate the disallowed expenses. On subsequent occasions prior to hearing, petitioner was offered opportunities to produce records but failed to do so.

Petitioner claimed that most of its records were lost when it moved to new offices.

At hearing, petitioner produced 100 checks payable to one Boris Teichman issued between September 1983 and July 1985. But no invoices were produced to demonstrate what the checks were for. As a result, the Division allowed only $75,766.00 of these costs for which it had seen substantiating documentation. It could not be determined which of the checks submitted in evidence represented allowed expenses.

Petitioner also produced an inspection report completed in September 1984 by DDC Consultants, Inc. of Upper Montclair, New Jersey, which indicated many deficiencies in the building. Petitioner asserted that said report clearly indicated that much work remained to be done and that, in fact, the construction period should have been construed to run long after December 31, 1983.

Petitioner also submitted a "punch list of problems" brought to his attention by the CHC, dated October 4, 1985. Petitioner said this was evidence of the non-completion of the building and, therefore, the ongoing construction period.

Petitioner also submitted a settlement agreement between himself and the owners' corporation, dated April 14, 1987, which finally settled petitioner's dispute with the owners' corporation and obligated petitioner to make payment of $230,000.00 to the owners' corporation for, among other things, repairs and maintenance. Petitioner interpreted this settlement as further proof that the construction period went well beyond December 31, 1983.

Petitioner claimed nine mortgages on the property and included them and their interest cost in the original purchase price. However, the Division disallowed these mortgages due to petitioner's failure to produce records which indicated what the proceeds were used for. Petitioner testified that they could only have been used for construction, but offered nothing further to substantiate its claim.

***OPINION***

In the determination below, the Administrative Law Judge held that the distinct problem in this case was petitioner's inability to prove the truth and validity of its position due to the lack of any records, such as the Closing Statement from the February 1984 transfer to the cooperative housing corporation as well as documentation concerning the mortgages petitioner wished to include as construction loans.

The Administrative Law Judge further held that the Division properly disallowed interest expense on funds used to acquire the property as well as claimed interest expense after the construction period, again due to lack of proof.

The Administrative Law Judge also held that it was not arbitrary for the Division to rely on the Certificate of Occupancy issued on October 19, 1983 as defining the ending of the construction period, and it was unreasonable for petitioner to believe that expenses incurred for years after the closing, which appear to be common repairs and maintenance, would be allowed as expenses includable in its original purchase price.

The Administrative Law Judge also did not allow as expenses to be included in the original purchase price a substantial payment claimed by petitioner as a result of a suit with the

cooperative housing corporation. The Administrative Law Judge also disallowed other undocumented expenses.

Finally, the Administrative Law Judge held that: 1) the burden of proof was upon petitioner to establish its claims and its failure to produce specific evidence to support its claims was fatal; 2) there is no authority for the position that the Division must produce the auditor and petitioner could have subpoenaed the auditor, but this was not done; 3) penalties and additional interest assessed must be sustained since petitioner failed to show that its failure to pay the tax was due to reasonable cause and not willful neglect; and 4) the Division conceded to making a modification on its computation resulting from the anticipated broker's commission on the one unsold unit.

On exception, petitioner argues that the Division's use of the issuance date of the Certificate of Occupancy as the date when the property is ready to be placed in service or is ready for sale is arbitrary. Petitioner asserts that the regulation does not specifically state this rule in its definition, and this rule does not comply with the intent of the law. Further, petitioner contends that the issuance of a Certificate of Occupancy does not mean the building is in a move-in condition but that the "building . . . conforms substantially with approved plans and specifications." By incorrectly limiting the construction period, petitioner argues, that the auditor improperly disallowed almost $800,000.00 in additional costs.

With respect to the exclusion of the interest and costs on the eight mortgages, the Administrative Law Judge's determination states that petitioner failed to produce records which would indicate what the mortgage proceeds were used for, but petitioner asserts that these documents were produced during the audit. Petitioner argues that: 1) the auditor's work papers would indicate such; 2) petitioner was not given access to them and this denial of access to the auditor's work papers was an unjust denial to an insolvent partnership; 3) the mortgages in question are of public record, especially to the Division; and 4) if the Division allowed almost

$3,000,000.00 in costs, the inclusion of interest and costs on only a $1,000,000.00 first mortgage is unfair and incorrect.

The Division, in a letter, argues that since petitioner has not raised any arguments which were not properly dealt with by the Administrative Law Judge, the Division will rely on the reasoning set forth in the determination.

Petitioner, in a reply brief, again argues that the Division's use of the Certificate of Occupancy's issue date as the end of the construction period not only has no basis in law, but is also inaccurate. Further, petitioner asserts that the Administrative Law Judge is not an expert in building codes, is not a licensed architect and "cannot fathom under what circumstances the New York City authorities issue a Certificate of Occupancy let alone determining that its issuance means that a building is ready to be placed in service or is ready for sale" (Petitioner's reply brief).

Petitioner's reply brief has attached an affidavit of Sy Churgin who states that he is a New York State registered architect. Petitioner requests that the Tax Appeals Tribunal accept said affidavit since the basis of his exception is of a technical nature requiring expert opinion.

The Division, in reply, requests that the affidavit be disregarded and stricken from the record.

We find no basis in the record before us for modifying, in any respect, the determination of the Administrative Law Judge. Therefore, we affirm the determination of the Administrative Law Judge for the reasons stated in his determination.

However, we must address and reject petitioner's attempt at this late date to place before this Tribunal additional evidence in the form of an affidavit which is not part of the record below.

As we held in Matter of Schoonover, Tax Appeals Tribunal, August 15, 1991):

> "[i]n order to maintain a fair and efficient hearing system, it is essential that the hearing process be both defined and final. If the parties are able to submit additional evidence after the record is closed, there is neither definition nor finality to the hearing. Further, the submission of evidence after the closing of the record

> denies the adversary the right to question the evidence on the record. For these reasons we must follow our policy of not allowing the submission of evidence after the closing of the record (see, Matter of Oggi Rest., Tax Appeals Tribunal November 30, 1990; Matter of Morgan Guar. Trust Co. of N.Y., Tax Appeals Tribunal, May 10, 1990; Matter of International Ore & Fertilizer Corp., Tax Appeals Tribunal, March 1, 1990; Matter of Ronnie's Suburban Inn, Tax Appeals Tribunal, May 11, 1989; Matter of Modern Refractories, Tax Appeals Tribunal, December 15, 1988)."

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of SOGL Associates is denied;

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

3. The petition of SOGL Associates is granted to the extent set forth in conclusion of law "D" of the Administrative Law Judge's determination but in all other respects the petition is denied; and

4. The Division of Taxation is directed to modify the Notice of Determination dated March 6, 1989 in accordance with paragraph "3" above, but such Notice is otherwise sustained.

DATED: Troy, New York
August 4, 1994

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

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