

STATE OF NEW YORK
TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
B & P REALTY ASSOCIATES	:	DECISION
for Revision of a Determination or for Refund	:	DTA No. 809560
of Tax on Gains Derived from Certain Real	:	
Property Transfers under Article 31-B of the	:	
Tax Law.	:	

Petitioner B & P Realty Associates, c/o Joseph Hershkowitz, Esq., 319 Fifth Avenue, New York, New York 10016, and the Division of Taxation each filed an exception to the determination of the Administrative Law Judge issued on February 3, 1994. Petitioner appeared by Whitman, Breed, Abbott & Morgan (Brian E. Gledhill, Esq., of counsel). The Division of Taxation appeared by William F. Collins, Esq. (Kenneth J. Schultz, Esq., of counsel).

Petitioner filed a letter in support of its exception. The Division of Taxation filed a letter in support of its exception and in opposition to petitioner's exception. Petitioner submitted a letter stating it would not be filing a brief in opposition which was received on May 23, 1994 and began the six-month period for the issuance of this decision.

The Tax Appeals Tribunal renders the following decision per curiam.

ISSUES

I. Whether the Division of Taxation properly determined that a purchase money mortgage received as consideration in exchange for the assignment of a contract for real property should be valued at its face amount although the mortgagor defaulted on the note before making any payments of the principal.

II. Whether petitioner has shown that any failure to comply with the provisions of Article 31-B of the Tax Law was due to reasonable cause and not willful neglect so as to warrant the cancellation of penalty.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge except for finding of fact "8" which has been modified. The Administrative Law Judge's findings of fact and the modified finding of fact are set forth below.

Petitioner, B & P Realty Associates, and the Division of Taxation ("Division") executed two stipulations of fact which were made a part of the record of this proceeding. The facts stipulated to have been incorporated into these Findings of Fact.

The real property which is the subject of the transfer at issue here is located at 14 Lafayette Square in Buffalo, New York and is commonly known as the Rand Building. On August 21, 1986, Lafayette Square Associates contracted to sell its fee interest in the Rand Building to the Hatoum Corporation which was acting as nominee for a charitable organization, Yeshiva Darkei Emunah.

On or about December 11, 1986, the Hatoum Corporation assigned its rights to purchase the Rand Building to petitioner, and petitioner then transferred its rights to Rand Associates in exchange for \$100,000.00 in cash and a purchase money note and mortgage in the amount of \$1,500,000.00. The mortgage which secured the note was subordinate to a first mortgage held by Lloyds Bank, Plc., in the amount of \$5,250,000.00.

By the terms of the mortgage note, petitioner was to receive "monthly installments of interest only, computed at the rate of 9% per annum, with the first payment due and payable on the 11th day of January, 1987, and monthly thereafter, until the 11th day of December, 1989." The full amount of the principal then became due with one proviso. If the first mortgage was extended for up to two years, the terms of the purchase money mortgage would likewise be extended for two years, contingent upon the payment of \$750,000.00 in reduction of the principal on the third anniversary of the mortgage agreement. Thus, the maximum term of the purchase money mortgage was five years with no payment on the principal amount due or owing until the end of the third year.

No payment of principal was made to petitioner under the terms of the mortgage. In November 1989, Rand Associates defaulted on the first mortgage and foreclosure by the first mortgagee followed. Rand Associates also defaulted on the subordinated mortgage at that time. In accordance with the terms of the mortgage note, petitioner received monthly payments of interest from Rand Associates until the default occurred.

Petitioner filed a supplemental real property transfer gains tax return in connection with the subject transactions on or about December 11, 1986. It reported gain subject to tax of \$1,575,000.00 with a tax due of \$157,500.00. Petitioner made a payment of \$7,500.00 with the filing of the return and deferred payment of the remaining \$150,000.00 due. A payment in the amount of \$15,000.00 was made on December 11, 1987, and a second payment in the same amount was made on December 11, 1988. No payments were made to the State after that time. In accordance with the gains tax return filed by petitioner, the amount of tax remaining due is \$120,000.00.

The Division issued to petitioner a Notice of Determination dated April 16, 1990, assessing tax in the amount of \$120,000.00, plus penalty and interest. An explanation attached to the notice provides the following information:

"TAX PERIOD ENDED DATE: 12/11/86
FILE DUE DATE: 12/11/86 DATE RECEIVED: 12/11/86

Tax Per Taxpayer:	7,500.00
Tax Per Dept of Tax & Finance:	78,750.00
Timely Payments/Credits:	7,500.00
Late Payments:	0.00
Amount Previously Assessed/Refunded:	0.00
BALANCE:	71,250.00"

"TAX PERIOD ENDED DATE: 12/11/87
FILE DUE DATE: 12/11/87 DATE RECEIVED: 12/11/87

Tax Per Taxpayer:	15,000.00
Tax Per Dept of Tax & Finance:	15,750.00
Timely Payments/Credits:	15,000.00
Late Payments:	0.00
Amount Previously Assessed/Refunded:	0.00
BALANCE:	750.00"

"TAX PERIOD ENDED DATE: 12/11/88

FILE DUE DATE: 12/11/88 DATE RECEIVED: 12/11/88

Tax Per Taxpayer:	15,000.00
Tax Per Dept of Tax & Finance:	15,750.00
Timely Payments/Credits:	15,000.00
Late Payments:	0.00
Amount Previously Assessed/Refunded:	0.00
BALANCE:	750.00"

"TAX PERIOD ENDED DATE: 12/11/89

FILE DUE DATE: 12/11/89 DATE RECEIVED: 12/11/89

Tax Per Taxpayer:	0.00
Tax Per Dept of Tax & Finance:	47,250.00
Timely Payments/Credits:	0.00
Late Payments:	0.00
Amount Previously Assessed/Refunded:	0.00
BALANCE:	47,250.00"

In an affidavit, Arthur H. Judelsohn, a general partner of 14 Lafayette Square Associates, stated his view that the Rand Building was worth \$5,700,000.00 when it was sold in December 1986.

We modify the Administrative Law Judge's finding of fact "8" to read as follows:

At the hearing in this matter, the Division sought to place in evidence a letter from petitioner's attorney to two individuals representing petitioner. In essence, the letter advised timely payment of the tax installments due to the State. Petitioner objected on grounds of attorney/client privilege. Petitioner requested permission to amend its petition in order to request cancellation of penalties. The Division objected to the amendment. Both objections were withdrawn by stipulation of the parties.

The body of the letter entered into evidence as Exhibit "G" stated as follows:

"November 9, 1987

Mr. Isack Bernstein
1418 52nd Street
Brooklyn, New York 11219

Mr. Isaac Perlstein
1270 48th Street
Brooklyn, New York 11219

Re: The Rand Building
Buffalo, New York

Dear Isaacs:

The closing of title for the above property was held on December 11, 1986. The first payment of gains tax is due on December 10, 1987.

The amount of gains tax due was \$157,500.00. \$7,500.00 was paid at closing. An installment of \$15,000.00 is now due. Payments should be sent the New York State Tax Commission, Department of Taxation and Finance, Property Gains Tax Division, Building No. 9, State Campus, Albany, New York 12227, and should refer to Assessment No. A-6054-3.

The State is currently assessing penalties of 35% plus interest on sellers of property who do not timely pay their installment of Gains tax. Additionally, they declare the entire tax due and payable.

Please make sure that this tax is paid immediately.

Sincerely,

Joseph M. Hershkowitz"¹

OPINION

The Administrative Law Judge stated that petitioner's assignment of its contractual right to purchase the Rand property was a transfer subject to the gains tax, pursuant to sections 1440(7) and 1441 of the Tax Law. The Administrative Law Judge, relying on Matter of Cheltoncort Co. (Tax Appeals Tribunal, December 5, 1991, affd Matter of Cheltoncort Co. v. Tax Appeals Tribunal, 185 AD2d 49, 592 NYS2d 121 [where the Tribunal stated that the value of the consideration has to be determined at the time of the transfer in order to finally fix the tax owed and that subsequent events do not alter the value that the consideration had at the time of the transfer]), found no merit to petitioner's argument that the gain must be redetermined in light of the default on the mortgage. The Administrative Law Judge further found that the Federal court decision cited by petitioner in its brief, 995 Fifth Ave. Assocs., L.P. v. New York State Dept. of Taxation & Fin. (963 F2d 503, cert denied ___ US ___, 121 L Ed 2d 302), "does not address the issue raised in this proceeding and lends no support to petitioner's position" (Determination, conclusion of law "A"). The Administrative Law Judge also found that Trump v. Chu (65 NY2d 20, 489 NYS2d 455, appeal dismissed 474 US 915) does not stand for the proposition that tax

¹We modified this fact at the request of the Division to add the second paragraph and the text of Exhibit "G."

will only be due if a profit is realized and that nothing in the Trump decision contradicts the conclusion reached here (Determination, conclusion of law "A").

With respect to petitioner's argument that the purchaser's promissory note should be accorded "open transaction" treatment, the Administrative Law Judge found that petitioner did not fully explain what "open transaction" treatment is. The Administrative Law Judge further found that TSB-M-86(4)R, which petitioner cited to, does not mention an "open transaction" approach to determine consideration. While the memorandum does discuss contingent future payments, the Administrative Law Judge stated that here there is no contract containing "an unvalued benefit" or "contingent payment"; the consideration was exact and certain (Determination, conclusion of law "B").

Finally, the Administrative Law Judge found that petitioner offered no reason for failing to pay the minimum amount due at the time of the transfer and for not paying the full amount of the installments due in 1987 and 1988 and, therefore, sustained the imposition of penalty. The Administrative Law Judge observed that \$71,250.00 of the tax assessed against petitioner (\$120,000.00) was due at the time of the transfer. The Administrative Law Judge further found that petitioner's belief that it did not have to pay gains tax because it had not realized a gain does not constitute reasonable cause. In this regard, the Administrative Law Judge found that petitioner made no attempt to ascertain its tax liability (Matter of Northern States Contr. Co., Tax Appeals Tribunal, February 6, 1992).

On exception, petitioner continues to argue that it was improper to include the face amount of the subordinated, non-recourse purchase money mortgage and note as consideration. Petitioner asserts that it was paid the mortgage and note "as a contingent amount for purchasing and immediately reselling, or 'flipping' the property involved" (Petitioner's Exception, Attachment, p. 2). Petitioner, relying on Trump v. Chu (supra) and 995 Fifth Ave. Assocs., L.P. v. New York State Dept. of Taxation & Fin. (supra), also continues to argue that gains tax is only to be imposed where there is a net profit. In addition, petitioner argues that it did have reasonable cause to believe that no gains tax was due because it realized no economic gain.

In its exception, the Division requests that finding of fact "8" of the Administrative Law Judge's determination be modified to include the text of Exhibit "G."

In its letter brief on exception, petitioner argues that the Administrative Law Judge did not attribute any significance to "the 'compensatory character' of the \$1.5 million subordinated, non-recourse mortgage, which was received by Petitioner as contingent compensation for 'flipping' the property," and to the fact that it was not paid for the interest in the real property itself (Petitioner's letter brief, p. 1). Petitioner also argues that the Administrative Law Judge did not recognize the "'hardship' aspect of this case in considering abatement of the penalty asserted" (Petitioner's letter brief, p. 1). Petitioner further argues that Exhibit "G" has no bearing on the reasonable cause issue since the letter was written more than two years before the default on the mortgage occurred.

In its letter in opposition to petitioner's exception, the Division argues that "the mortgage given to the petitioner in return for the assignment of its interest in the real property is clearly consideration within the meaning of Tax Law §1440.1 regardless of whether it was subordinated or nonrecourse" (Division's letter in opposition, p. 1). The Division also requests that its proposed finding of fact be adopted. The Division argues that the advice given to petitioners in Exhibit "G" is relevant to the penalty issue.

On exception, petitioner has raised the same arguments made before the Administrative Law Judge. Because the Administrative Law Judge adequately addressed these arguments, we affirm the determination of the Administrative Law Judge for the reasons stated in said determination.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of B & P Realty Associates is denied;
2. The exception of the Division of Taxation is granted;
3. The determination of the Administrative Law Judge is affirmed;
4. The petition of B & P Realty Associates is denied; and

5. The Notice of Determination issued on April 16, 1990 is sustained.

DATED: Troy, New York
November 3, 1994

/s/John P. Dugan

John P. Dugan
President

/s/Francis R. Koenig

Francis R. Koenig
Commissioner