

STATE OF NEW YORK  
TAX APPEALS TRIBUNAL

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In the Matter of the Petition	:	
of	:	
<b>I. MILES POLLACK</b>	:	DECISION
for Revision of a Determination or for Refund	:	DTA No. 809622
of Tax on Gains Derived from Certain Real	:	
Property Transfers under Article 31-B of the	:	
Tax Law.	:	

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Petitioner I. Miles Pollack, 925 Westchester Avenue, White Plains, New York 10604, filed an exception to the determination of the Administrative Law Judge issued on July 8, 1993. Petitioner appeared pro se. The Division of Taxation appeared by William F. Collins, Esq. (Kenneth J. Schultz, Esq., of counsel).

Petitioner filed a brief on exception. The Division of Taxation filed a letter in opposition to petitioner's exception. Petitioner filed a letter in reply to the Division of Taxation's letter in opposition on December 6, 1993, which date began the six-month period for the issuance of this decision. Petitioner's request for oral argument was denied.

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

***ISSUE***

Whether the consideration received by petitioner in respect of his transfer of a controlling interest in an entity with an interest in real property properly included the apportioned mortgage debt on the underlying real property.

***FINDINGS OF FACT***

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

On or about September 15, 1984, 22 Leroy Owners Corp., a New York corporation, acquired title in fee to certain real property located at 22 Leroy Street, New York, New York. The subject property at 22 Leroy Street was improved by an apartment building. The corporation's purchase price for the property was \$600,000.00, paid as follows: i) \$50,000.00 in cash, and ii) \$550,000.00 in a purchase money wraparound mortgage and note.

Petitioner, along with Aaron Gelbwaks, Martin V. Herzog and Lizabeth Levkoff each owned an undivided 25 percent interest in the 212 shares of the corporation issued and outstanding. Petitioner and the other shareholders acquired their respective 25 percent interests at the time the corporation acquired title to the subject property in consideration of the acquisition costs.

Pursuant to an agreement dated July 29, 1987, petitioner agreed to sell his 25 percent interest in the corporation to Aaron Gelbwaks. The purchase price for petitioner's interest was \$150,000.00, payable as follows: \$25,000.00 in cash upon the signing of the July 29, 1987 agreement and \$125,000.00 by a promissory note. The agreement provided that the promissory note was to be delivered to petitioner "on January 5, 1988, the closing date . . . ." The agreement further provided that the promissory note was to be "secured by a pledge, in escrow with Bernard J. Jaffe, Esq., of the shares of stock sold herein."

As part of the evidence submitted herein, petitioner submitted a copy of the promissory note referred to in the July 29, 1987 contract between petitioner and Aaron Gelbwaks. Said note was dated January 5, 1988 and provided in part:

"This note shall be secured by a pledge of the shares of stock sold pursuant to Agreement between Gelbwaks and Pollack, dated July 29, 1987, with Bernard J. Jaffe, Esq., to be released under such conditions and at such times as set forth in said Agreement."

The pledge agreement referred to above was not entered into the record.

Pursuant to an agreement dated September 29, 1987 Martin Herzog and Lizabeth Levkoff agreed to sell their aggregate 50 percent interest in the shares of the corporation to Aaron Gelbwaks. The purchase price for this 50 percent interest was \$550,000.00.

Petitioner was a party to the September 29, 1987 agreement which provided in part:

"B. (1) The Sellers [Herzog and Levkoff], the Purchaser [Gelbwaks] and Pollack [petitioner] shall execute and deliver to Purchaser a Stock Power and Assignment of Proprietary Lease . . . so as to effect the transfer of record of the Shares and Proprietary Lease to the Purchaser.

"(2) The Sellers, the Purchaser and Pollack shall cause the Apartment Corporation to cancel the share certificate evidencing ownership of the Shares by the Sellers, the Purchaser and Pollack as tenants in common ('Old Share Certificate') and to issue a new share certificate in the name of the Purchaser . . . and to issue a Recognition Agreement and a Consent to the Assignment of the Shares to Purchaser . . . ."

Mr. Gelbwaks subsequently became the sole sponsor of a cooperative offering plan to convert the premises at 22 Leroy Street to cooperative ownership. A copy of the offering plan was entered into the record here. Page one of the offering plan states in part:

"22 LEROY OWNERS CORP., acquired the fee interest in the Property at 22 Leroy Street, New York, New York on September 1, 1984 and issued all its outstanding shares to Martin V. Herzog, Lizabeth Levkoff, I. Miles Pollack and Aaron Gelbwaks in consideration of the acquisition costs. These individual sponsors submitted an Offering Plan ('red-herring') to the Department of Law on June 16, 1989. On September 29, 1987, AARON GELBWAKS became the sole stockholder of the corporation and sole Sponsor (the 'Sponsor') pursuant to written agreements by which he purchased all the interest held by Martin Herzog, Lizabeth Levkoff and I. Miles Pollack."

Page 74 of the offering plan states in part:

"The property was acquired by 22 LEROY OWNERS CORP. on September 15, 1984. Aaron Gelbwaks, Martin V. Herzog, Lizabeth Levkoff and I. Miles Pollack, were the sole shareholders of 22 LEROY OWNERS CORP. The same individuals were the collective Sponsor who submitted a proposed Offering Plan to the Department of Law on June 18, 1986.

"On September 29, 1987 Mr. Gelbwaks became the sole shareholder of the Corporation and the sole principal Sponsor of this Offering Plan. The three former members of the Sponsor, Martin V. Herzog, Lizabeth Levkoff and I. Miles Pollack have no interest in the Offering Plan, wrap-around mortgage or the basement lease except in so far as evidenced by a security interest Note for a portion of the consideration paid to them. Such security interest shall be released as units are sold. No purchasers will be subject to any security interest or lien other than the wrap-around mortgage set forth in the Offering Plan."

No transferor or transferee questionnaires were filed with the Division of Taxation ("Division") in respect of the transfer from petitioner to Gelbwaks. Petitioner did not

communicate with the Division with respect to this transfer until the Division initiated contact nearly two years after the transfer.

With respect to the purchase of the 22 Leroy Street property by the corporation on or about September 15, 1984, while the contract of sale indicates a mortgage in principal amount of \$550,000.00, the closing statement indicates a principal mortgage amount of \$549,993.75, which is the sum of the amounts of a "First Mortgage" (\$96,093.75) and a "Purchase Money Mortgage" (\$453,900.00). The contract of sale states that the wraparound mortgage was to be paid by payments of interest only for five years with a \$50,000.00 principal payment required to be made three years from the date of the closing.

Upon its review of the transfer from petitioner to Gelbwaks, the Division determined that, for gains tax purposes, the mortgage debt in the subject real property should be added, pro rata, to the consideration received by petitioner in respect of the transfer. The Division determined that the transfer in question occurred on July 29, 1987. Pursuant to the terms of the Contract of Sale with respect to the corporation's September 15, 1984 acquisition of the property, the principal mortgage debt as of July 29, 1987 was \$549,993.75. The Division allocated 25 percent of this indebtedness, or \$137,498.44, to the consideration received by petitioner in respect of the subject transfer. The Division thus determined that the consideration received by petitioner in respect of the tax transfer totaled \$287,498.44 (\$150,000.00 per the July 29, 1987 contract of sale plus \$137,498.44 of mortgage indebtedness). The Division allocated an original purchase price to petitioner's 25 percent interest in the corporation of \$150,000.00, i.e., 25 percent of the \$600,000.00 purchase price paid by the corporation to acquire the property. The Division thus determined a gain attributable to the subject transfer of \$137,498.44. The Division further determined that such gain was subject to tax under Article 31-B of the Tax Law and on August 1, 1989 issued to petitioner a Notice of Determination which assessed \$13,749.84 in gains tax due, in respect of the subject transfer plus penalty and interest.

It should be noted that the Division determined a total consideration for the 75 percent interest in the corporation acquired by Gelbwaks as follows:

Purchase Price for Pollack's 25% interest	\$ 150,000.00
Mortgage Indebtedness Allocable to Pollack's 25% interest	137,498.44
Purchase Price for Herzog/Lavkoff's 50% interest	550,000.00
Mortgage Indebtedness Allocable to Herzog/Lavkoff's 50% interest	<u>224,996.88</u>
Total Consideration	\$1,062,495.32

**OPINION**

The Administrative Law Judge determined that: a) the gain derived from petitioner's transfer of his 25 percent interest in the shares of the corporation and the transfer of the Herzog/Levkoff 50 percent interest constituted an acquisition of a controlling interest by Gelbwaks; b) the gain derived by petitioner was subject to tax under Tax Law § 1441; c) the Division properly determined petitioner's original purchase price in his 25 percent interest to be \$150,000.00, i.e., 25 percent of the corporation's original purchase price for the property at issue of \$600,000.00; d) the consideration received by petitioner in respect of his transfer of his 25 percent interest is properly determined by the fair market value of the subject property apportioned to the interest transferred; and e) that such fair market value properly took into account the mortgage debt encumbering the property.

On exception, petitioner makes the following relevant assertions:

"1. §1441 of the Tax Law imposes a tax on 'gains derived from the transfer of real property within the state.' In the instant case, the purchaser, Aaron Gelbwaks never paid the purchase price to the Petitioner. There has been a failure of consideration. Accordingly, no gain has been derived from the transfer of real property within the state pursuant to that section of the law which imposes the tax.

"2. The tax must be determined using the Fair Market Value of the interest transferred.

"No evidence has been submitted by the Tax Department that the Fair Market Value has been used in determining the tax allegedly due.

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"4. Tax Law §1440(1)(a) deals with mortgage indebtedness which is 'assumed or taken subject to...' or '...includes the cancellation or discharge of an indebtedness or obligation.' In the instant case, no indebtedness was assumed or taken subject to nor was an indebtedness canceled. In fact, the Petitioner sold his interest unencumbered by any

mortgage and such never was the subject of any mortgage. Accordingly, to allocate a percentage of the underlying mortgage on the building owned by the corporation whose stock was being transferred is improper in the instant case, as the general scheme of the Tax Law is to tax gains derived and to measure those gains by the benefit achieved by the seller. No gain can be shown in the instant case as it relates to mortgage indebtedness, as no mortgage indebtedness ever existed encumbering the stock transferred.

"5. The Administrative Law Judge was in error in conclusion J when he stated 'It was clearly reasonable for the Division to determine that the consideration received by Petitioner for his interest, i.e. the fair market value of petitioner's interest, consisted of the contract price of the shares plus the pro rata share of the mortgage debt encumbering the property,' since there is no statement in the contract between the Petitioner and purchaser as to how any mortgage is to be dealt with. Thus, his conclusion that 'the contract price plus the apportioned mortgage amount would appear to be the best evidence of Fair Market Value available to the Division' is erroneous. Furthermore, he doesn't deal with the contention that the consideration was not received.

"Based on all of the foregoing and the material previously submitted in this proceeding, it is respectfully prayed that the decision of the Administrative Law Judge be reversed and the Petitioner's petition granted in all respects" (Petitioner's brief, pp. 1-3).

On exception, the Division requests that "the ALJ's Determination be affirmed for the reasons stated therein, with the exception of the ALJ's reliance on fair market value in determining the consideration for Petitioner's transfer" (Division's brief, p. 1). On this latter point, the Division, relying on the first sentence of Tax Law § 1440(1),<sup>1</sup> asserts that:

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<sup>1</sup>As relevant here, consideration is defined as:

"any price paid or required to be paid, whether expressed in a deed and whether paid or required to be paid by money, property, or any other thing of value and including the amount of any mortgage, purchase money mortgage, lien or other encumbrance, whether the underlying indebtedness is assumed or taken subject to. Consideration includes the cancellation or discharge of an indebtedness or obligation.

\* \* \*

"(c) In the case of a transfer which includes other assets which are in addition to real property or an interest therein and for which there is no reasonable apportionment of the consideration for such real property or interest, consideration means that portion of the total consideration which represents the fair market value of such real property or interest. In the case of a transfer of a controlling interest in an entity with an interest in real property, there shall be an apportionment of the fair market value of the interest in real property to the controlling interest for the purpose of ascertaining the consideration for the transfer of such controlling interest"  
(Tax Law § 1440[1][a] & [c]).

"[s]ince there is nothing in the record indicating that any assets other than real property were owned by the corporation it is the Division's position that the consideration for the Petitioner's transfer of shares should be determined by reference to the price paid or required to be paid to him, not the fair market value of the property as determined by the ALJ" (Division's brief, p. 3).

The Administrative Law Judge fully and correctly dealt with the issues raised before him at hearing and we affirm the determination of the Administrative Law Judge on those issues for the reasons stated therein.

Since the Division has not filed a timely exception, we will not address its assertion that the Administrative Law Judge improperly relied on "fair market value" in determining the consideration for the interest in the real property transferred by petitioner.

With regard to petitioner's assertion, raised for the first time on this exception, that no gain has been derived because Mr. Gelbwaks never paid the purchase price to petitioner, we agree with the Division that the issue is resolved by Matter of Cheltoncort Co. v. Tax Appeals Tribunal (185 AD2d 49, 592 NYS2d 121). Tax Law § 1440(1) defines consideration as the price paid or required to be paid for real property. In Cheltoncort, the Court held that:

"[a]s the Tribunal noted, 'the value of the consideration has to be determined at the time of the transfer in order to finally fix the tax owed. Subsequent events do not alter the value that the consideration had at the time of the transfer'" (Matter of Cheltoncort Co. v. Tax Appeals Tribunal, supra, 592 NYS2d 121, 123).

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of I. Miles Pollack is denied;
  2. The determination of the Administrative Law Judge is affirmed;
  3. The petition of I. Miles Pollack is denied; and
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4. The Notice of Determination dated August 1, 1989 is sustained.

DATED: Troy, New York  
May 12, 1994

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

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