STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
PETER H. McCALLION	:	DECISION DTA No. 809834
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 Peter H. McCallion, 2201 Maple Avenue, Peekskill, New York 10566 and the Division of Taxation each filed an exception to the determination of the Administrative Law Judge issued on March 7, 1996. Petitioner appeared by Stern, Keiser, Panken & Wohl, LLP (Andrew I. Panken, Esq., of counsel). The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (Michael J. Glannon, Esq., of counsel).

Petitioner filed a brief in support of his exception and a reply brief in opposition to the Division of Taxation's exception. The Division of Taxation filed a brief in support of its exception and in opposition to petitioner's exception and a reply brief. Oral argument, at the request of both parties, was heard on March 6, 1997.

After reviewing the entire record in this matter, the Tax Appeals Tribunal renders the following decision.

ISSUES

I. Whether there was an acquisition on November 3, 1987 of a controlling interest in Indian Hill Associates, Inc. which is subject to real property transfer gains tax.

II. Whether petitioner met his burden of proof to demonstrate that the transferee's unsecured promise to pay $350,000.00 approximately six monthsafter the transfer of the controlling interest occurred was worthless on the date of transfer.

FINDINGS OF FACT

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

Petitioner, Peter H. McCallion, and seven other individuals formed a corporation known as Indian Hills Associates, Inc. (the "corporation"). Although no stock certificates were issued to the eight individuals, their respective shareholder interests in the corporation were as follows: petitioner -- 13 shares; Terence Gargan -- 4.25 shares; Frank Loomis -- 2.25 shares; Gregory O'Neill -- 2.25 shares; William E. Fowler -- 2.00 shares; Richard DeLorenzo -- 2.00 shares; Kenneth McCallion -- 1.125 shares; and Bernard Persky -- 1.125 shares.

At the hearing, petitioner explained that the corporation was formed in the first half of 1987 as an S-corporation.

Petitioner was president and a director of the corporation; while the other two directors and officers of the corporation were Terence Gargan, treasurer and William E. Fowler, secretary.

Both petitioner and Terence Gargan acted as attorneys on behalf of the corporation and its shareholders.

On July 6, 1987, the corporation entered into a contract to purchase ("purchase contract") four parcels of real estate, totaling approximately 165 acres, located in Putnam and Westchester Counties, New York from Putnam Limited Partners ("Putnam") for $3,425,000.00 (see, Division of Taxation's [the "Division"] Exhibit "L"). The closing was to take place on November 7, 1987. A deposit of $300,000.00 was paid by the corporation when the contract was signed. According to paragraph 32 of the rider to the purchase contract, the $300,000.00 payment was to be held in escrow, in an interest-bearing account, by Putnam's attorney John D. Bamonte, Esq. Paragraph 35 of the rider gave the corporation, as purchaser, the right to assign the contract without consent of the seller, Putnam.

The sole asset of the corporation was the purchase contract with Putnam.

The shareholders of the corporation decided to sell their shares to Andrew Lane ("Lane"). Lane was a real estate developer from Framingham, Massachusetts. A written agreement to

acquire all of the corporation's interest in the purchase contract and to acquire all outstanding shares of the corporation was entered into on November 3, 1987 by the shareholders and Lane. The agreement was signed on behalf of the corporation by petitioner as both president and as attorney for the shareholders/sellers.

The Division's Exhibit "K" is the agreement ("agreement") between the shareholders of the corporation ("sellers") and Lane ("purchaser"). According to the terms of the agreement, the sellers

> "in consideration of the sum of One Million Six Hundred Seventy Five Thousand Dollars ($1,675,000.00) paid to the Sellers by the Purchaser as hereinafter provided, hereby convey, sell and assign to the Purchaser all their shares in the Corporation."

Paragraph 4 of the agreement sets forth the following terms of how the $1,675,000.00 consideration was to be paid:

> "a) Three Hundred Thousand Dollars ($300,000.00) to be paid upon the signing of this agreement by certified or bank check, and held in escrow until released for payment no later than December 10, 1987;[1]
>
> "b) Seventy Five Thousand Dollars, payable by certified or bank check, at or prior to the delivery of the deed to the
>
> above-described premises by Putnam Limited Partners to the Corporation at the office of John D. Bamonte, 24 Ellis Place, Ossining, New York 10562, or at the address of the Corporation's lending institution, at 10:00 a.m. o'clock on November 7, 1987, or on such other date or place as may mutually be agreed to by the Corporation and Putnam Limited Partners in writing; and
>
> "c) One Million Three Hundred Thousand Dollars payable by an irrevocable letter of credit issued in favor of Peter H. McCallion, as attorney for the Sellers, for the account of the Purchaser, by Bankers' Trust or other bank acceptable to the Sellers. The letter of credit shall be obtained at the expense of the Purchaser. The letter of credit shall provide for payment of the principal amounts and accrued interest on the dates as follows:
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> "Three Hundred Fifty Thousand Dollars plus interest on January 4, 1988, on the receipt of land funding by a Bank after Jan. 1, 1988;[2]

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[1] This term was modified and the handwritten changes were initialed by both petitioner and Lane.

[2] The handwritten portion concerning the land funding was initialed by both petitioner and Lane.

"Three Hundred Fifty Thousand Dollars plus interest on July 1, 1988;

"Three Hundred Fifty Thousand Dollars plus interest on December 30, 1988;

"Two Hundred Fifty Thousand Dollars plus interest on June 30, 1989.

"Said payment shall be made by Purchaser in favor of the Sellers from the funds obtained in the aforesaid manner.[3] Receipt by Sellers of said letter of credit duly executed by Bankers' Trust or other bank acceptable to the Sellers shall be a condition of the performance of the Sellers' duties under the Agreement. The letter of credit shall be in a form acceptable to the Sellers. A copy of a form of a letter of credit acceptable to Sellers is attached to this Agreement as Schedule C. The letter of credit shall not be revocable by the Purchaser. The Purchaser shall provide that the term of the letter of credit shall run from November 4, 1987 to July 21, 1989. Payment under said letter of credit shall be made to Peter H. McCallion, as attorney, directly by the bank issuing said letter of credit. In the event the Purchaser receives any notice that affects or may affect said letter of credit, Purchaser shall notify Sellers immediately of

such notice by mailing a certified letter to Peter H. McCallion, 2201 Maple Avenue, Peekskill, N.Y. 10566. Sellers will in such event be entitled to demand assurances of payment under said letter of credit satisfactory to them. In the event such assurances are not received within ten days of demand, Sellers have the right to draw payment in full of the balance of the purchase price plus interest."

According to paragraph 5 of the agreement, the interest rate on the irrevocable letter of credit payments was to be 10% per annum, compounded quarterly and was to be paid on the dates the principal amounts were due.

The last term of the agreement, which is handwritten and has both petitioner and Lane's initials after it, follows:

"Sellers agree to accept payment from an escrow fund to be released by the bank funding the land purchase in lieu of a letter of credit."

During the hearing, petitioner stated that at the time the agreement was signed, the conditions precedent to the shareholders' obligation to transfer the shares did not occur. He stated that Lane did not obtain a letter of credit from a bank nor was an escrow fund established. In addition, the shareholders did not receive the $300,000.00 down payment required by the

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[3] This sentence was modified and the handwritten changes were initialed by petitioner and Lane.

agreement. According to petitioner, Lane did not pay any consideration at the time the agreement was signed (tr., p. 20).

The Division's Exhibit "B" is the Real Property Transfer Gains Tax Questionnaire - Transferor, Form TP-580 ("transferor questionnaire") which petitioner executed as president of the corporation. According to the transferor questionnaire, the corporation was transferring a 100% controlling interest in the corporation which had a contract to purchase real property located in Indian Hill - Section 2.5, Town of Yorktown, Westchester County, New York and Indian Hill - Section 120, Block 3, Lots 18 and 19, Town of Putnam Valley, Putnam County, New York, on November 3, 1987 to transferee Andrew J. Lane. According to Schedule B of the transferor questionnaire, the gross consideration to be paid for the transfer by the transferee was $4,800,000.00; the purchase price paid to acquire real property was $3,425,000.00; allowable selling expenses were $100,412.00 and the gain subject to tax was $1,274,588.00, with an anticipated tax due of $127,458.00.

The Division's Exhibit "M" is the letter dated November 18, 1987 which was submitted along with the transferor questionnaire. In this letter, petitioner wrote in pertinent part:

> "The enclosed papers are submitted by me on behalf of all the former shareholders of Indian Hill Associates, Inc., who sold 100% of their interest in the corporation on 11/3/87 to Andrew J. Lane. The corporation's sole asset as of this date is a contract to purchase 165 acres from Putnam Limited Partners.
>
> "We have received to date no cash from Mr. Lane, but will be receiving $1,375,000.00 over the next twenty months, in addition to the return of our $300,000.00 deposit. Mr. Lane will be closing on the property on December 4, 1987, at which time he will pay Putnam Limited Partners $3,125,000.00, and the $300,000.00 deposit will be released to the Seller."

Petitioner also identified the following selling expenses, listed on the transferor questionnaire to the date of the closing and "owed by former shareholders, not Lane": Legal expenses - Peter McCallion - $78,000.00; Engineer - $1,260.00; Site Planner - $6,652.00; Appraiser - $4,500.00 and Mortgage Broker - $10,000.00.

The Division's Exhibit "C" is the Real Property Transfer Gains Tax Questionnaire - Transferee, Form TP-581 ("transferee questionnaire") which Mr. Lane executed. According to the transferee questionnaire, Mr. Lane was the transferee who was acquiring 100% controlling

interest on November 3, 1987 for $1,375,000.00 from transferors "Peter H. McCallion, Terence Gargan, Gregory O'Neill, Frank Loomis, Richard DeLorenzo, William Fowler, Kenneth McCallion and Bernard Persky (former shareholders of Indian Hill Associates, Inc.)". The location of the property to be transferred was Indian Hill - Section 2.5, Parcel 2, Town of Yorktown, Westchester County, New York and Indian Hill - Section 120, Block 3, Lots 18 and 19, Town of Putnam Valley, Putnam County, New York.

Petitioner's Exhibit "1" is a letter dated November 30, 1987, written by Andrew Lane to Terence Gargan, Esq.,[4] in which Mr. Lane wrote:

> "When I discussed the purchase of the stock of Indian Hills [sic] Associates, it was understood by the shareholders that I was doing so, solely that I might acquire the Indian Hill property from Putnam Limited Partners while peserving [sic] the rights of Indian Hill Associates vis-a-vis the Town of Putnam Valley. Repeated representations were made to me by the shareholder's [sic] that Banker's [sic] Trust of New York was prepared to finance the purchase of the property, and that the lender was prepared to go forward quickly. It was in reliance on these representations that I signed and delivered the November 3rd agreement with the shareholders. They were well aware that I had no intention to finance the purchase out of my own cash flow, and that, had I not been told of the ready financing, I would not have had an interest in the purchase of the stock of Indian Hills [sic] Associates.
>
> "Since entering into the agreement with the stockholders, I have, as you know, learned that the representations concerning the availability of the purported financing package were, at best, less than accurate and misleading. I had been led to believe that Banker's [sic] Trust was looking to the land only as security for the loan.
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> "As you know, my discussions with Banker's [sic] Trust continue, but they have made it clear that if they make a loan, it will be a recourse transaction and that, therefore, there will be a period of evaluation before they decide whether to proceed. You are also aware that I have already sent the shareholders $40,000 to be utilized in connection with their efforts, on my behalf, to acquire the additional Bayha parcel adjacent to the Weingarten property.
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> "I am, therefore, prepared to proceed alternatively:
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> 1) If the Purchase and Sale Agreement with Putnam Limited Partners can be renegotiated so that Indian Hill Associates' obligations thereunder are contingent on obtaining financing and the agreement
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> is likewise clarified to reflect this financing contingency, I am prepared to pay the $300,000 sum, together with the other sums due and payable, upon closing of the

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[4]This letter references: "Indian Hill Associates, Your File No. 6048-1, Your letter dated November 23, 1987."

transaction. I would continue to use my best efforts to obtain financing and to close both transactions as quickly as possible after financing is obtained; or;

2) If your clients would prefer to pursue other opportunities with the prospective purchasers you mention in your letter, I am prepared to permit them to do so. They need simply to return to me the $40,000 which I've sent them and I will execute whatever documents you reasonably deem advisable to evidence the release of my rights to acquire the stock of Indian Hill Associates.

"Please discuss this matter with your clients and advise as to their choice of options. Banker's [sic] Trust representatives will be in our office on Thursday, I am making every effort to obtain financing as quickly as possible."

On December 1, 1987, the Division issued a Real Property Transfer Gains Tax Tentative Assessment and Return, Form TP-582 ("tentative assessment") to petitioner which contained the following computation:

1. Gain subject to tax as computed by the Transferor on Form TP-580, line 9	1,274,588.00	
2. Net adjustments (see Form TP-582.1 attached)		14,500.00
3. Gain subject to tax (line 1 plus or minus line 2)		1,289,088.00
4. Tentative assessment of tax due (10% of line 3)		128,908.80
5. Penalty due	0.00	
6. Interest due	0.00	
7. Total (lines 4,5 and 6)	128,908.80	
8. Amount Previously Paid	0.00	
9. Total due (line 7 less line 8)	128,908.80	

Attached to the tentative assessment was a "Schedule of Adjustment" which explained the adjustment made by the Division. According to this schedule, selling expenses, totaling $14,500.00, claimed for the appraisal and the mortgage broker were disallowed.

Andrew Lane proposed to amend the agreement. Mr. Lane sent a letter agreement ("letter agreement") dated January 4, 1988 to "The Shareholders of Indian Hills Associates, Inc.", in care of petitioner, which referenced the stock purchase agreement dated November 3, 1987 and the payment provisions set forth therein (Division's Exhibit "N"). According to this letter agreement, Lane had reached an agreement with Putnam to further extend the closing date under the purchase contract from January 4, 1988 to February 12, 1988

"in consideration of release from escrow for Putnam's account of the $300,000 payment previously made by Indian Hills [sic] Associates, Inc. under the terms of the July 6, 1987 agreement, Lane's additional payment on account of the purchase price of $360,000 to be made this date."

However, he was not prepared to make the additional payments unless the shareholders agreed inter alia to the following terms:

> "(1) Shareholders agree to the release of the $300,000 deposit amount held in escrow pursuant to the terms of the July 6, 1987 agreement for the account of Putnam.
>
> "(2) Notwithstanding any contrary provisions in the November 3, 1987 Agreement, no payments on account of the $1,675,000 purchase price of the shares shall be due and payable until such time as Lane is actually able to close a land loan and actually receives the proceeds of such land loan. At the closing and funding of such land loan, Lane will pay the shareholders $375,000 on account of the $1,675,000 purchase price. Ninety (90) days after the date of such land loan closing, Lane will pay to shareholders an installment payment of $350,000 together with interest; a second installment payment of $350,000 together with interest shall be due and payable one hundred and eighty (180) days after the date of such closing. No additional payments shall be due and payable until Lane has obtained all necessary governmental approvals for a subdivision from the Town of Putnam Valley. Lane will pay the shareholders, within sixty (60) days after receipt of Town of Putnam Valley approvals (receipt of approvals shall mean receipt of a signed final zoning map from the planning board of the Town of Putnam Valley and the running of all applicable appeals periods so that the same are no longer subject to challenge by appeal) the balance of the purchase price, $600,000, together with interest thereon. The outstanding balance of the $1,675,000 purchase price will bear interest from the date of the land loan closing, until paid, at the rate of 10% per annum; no interest shall, however, be due and payable except upon loan funding as aforesaid. All references to an irrevocable letter of credit as set forth in the November 3, 1987 agreement are hereby deleted; all due dates for payment as set forth in the November 3, 1987 agreement are superseded hereby."

Petitioner accepted and signed this letter agreement as president of the corporation and as attorney in fact for the shareholders.

According to a letter dated February 2, 1988, written by Terence Gargan to David A. White, Esq.,[5] Mr. Lane had obtained a loan commitment from Merchants Bank of Boston, which was to close on February 5, 1988, the proceeds of which were to be more than sufficient to consummate the land purchase which was to take place on February 12, 1988. Mr. Gargan wrote, in pertinent part, that:

> "[p]ursuant to paragraph 2 of the Agreement between Andrew Lane and the shareholders of Indian Hill Associates, Inc., dated January 4, 1988, which supplements the parties' agreement of November 3, 1987, the shareholders are due an initial payment of $375,000 at the closing and funding of the loan to be used to

[5]Mr. White was retained to represent Andrew Lane and the corporation at the closing of title between Putnam and the corporation for the land purchase.

consummate the land purchase. Accordingly on February 5 this initial payment will be due and owing.

"Peter has conveyed to me your request that he, as President, and I, as Treasurer of Indian Hill Associates, Inc. submit our resignations to you as officers of the corporation. We will execute and deliver the requested resignations, in favor of Manuel Rabbitt, at the loan closing on February 5th simultaneously with the payment of $375,000 by or on behalf of Mr. Lane, by certified check payable to Terence Gargan, as attorney. Please advise Peter or me in writing of the time and place of such loan closing and confirm that appropriate arrangements for such initial payment have been made." (Petitioner's Exhibit "3"; emphasis in original.)

Petitioner's Exhibit "4" is a letter, dated February 3, 1988, written by Terence Gargan, as attorney for the shareholders of the corporation to David A. White, Esq,, in response to Mr. White's proposed modification of the agreement between the shareholders of the corporation and Lane dated November 3, 1987 and January 4, 1988.[6] Mr. Gargan proposed the following:

"[t]he shareholders of Indian Hill Associates, Inc. agree to accept payment on account of the $1,675,000 purchase price of the shares of Indian Hill Associates, Inc. in the following manner:

"(1) A bank or certified check in the amount of $375,000 made payable to Peter H. McCallion, as attorney, shall be paid at the closing of title between Indian Hill Associates, Inc. and Putnam Limited Partners as the down payment for the sale of the shares of Indian Hill Associates, Inc. to Andrew J. Lane. This closing shall occur on February 12, 1988 at 1:00 p.m. at the office of John Bamonte, Esq., 24 Ellis Place, Ossining, New York. Time is of the essence for such closing.

"(2) If Mr. Lane elects to refinance the indebtedness on the Indian Hill property which is the subject matter of the closing referred to above, then $350,000 shall be paid by bank or certified check to Peter H. McCallion, as attorney, ninety (90) days after such refinancing. If Mr. Lane does not so refinance the indebtedness, the payment of said $350,000 shall be made no later than July 1, 1988.

"(3) $350,000 shall be paid one hundred eighty (180) days after refinancing, or in the event there is no refinancing, no later than October 1, 1988, by bank or certified check to Peter H. McCallion, as attorney.

"(4) The final and fourth payment in the sum of $600,000 shall be paid by bank or certified check to Peter H. McCallion, as attorney, after final approval of a subdivision by the Town of Putnam Valley. Final approval includes the running of any appeals period subsequent to Planning Board approval of the subdivision plan.

"Interest shall be due at the rate of 10% per annum together with all payments of principal, as previously agreed from February 12, 1988.

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[6]Mr. White's proposed modifications are not part of the record.

> "All other provisions of the contract between Andrew J. Lane and the shareholders of Indian Hill Associates, Inc. shall remain in effect."

An attorney for Mr. Lane agreed and accepted this proposal on Mr. Lane's behalf.[7]

On February 10, 1988, all eight shareholders of the corporation executed a document entitled "CONSENT OF SHAREHOLDERS" ("consent") by which they consented to sell all of the shares of the corporation to Lane

> "in consideration of payment by Lane of $1,675,000, to be paid as follows: $375,000 on February 11, 1988; $350,000 plus interest on the balance of the purchase price at the rate of 10% per annum on or before July 1, 1988; $350,000 plus interest on the balance of the purchase price at the rate of 10% per annum on or before October 1, 1988; $600,000 plus interest on the balance of the purchase price at the rate of 10% per annum upon approval of a subdivision by the Planning Board of Putnam Valley, New York on a 135 acre property located on Indian Hill Road to be conveyed by Putnam Limited Partners to Indian Hill Associates, Inc. on February 11, 1988, approval meaning the running of all appeals periods applicable thereto." (Petitioner's Exhibit "6".)

The following acknowledgment appeared on the consent:

> "Peter H. McCallion, being duly sworn, deposes and says that he is the President of Indian Hill Associates, Inc., the corporation referred to in the foregoing consent; that he is the custodian of the stock book of such corporation; that the persons who have subscribed to the foregoing consent are the owners upon the books of such corporation of the number of shares of stock therein set opposite their respective signatures to the foregoing consent, being at least two-thirds in amount of the capital stock of such corporation."

A special meeting of the board of directors of the corporation was held on February 10, 1988. Petitioner's Exhibit "7" is a copy of the minutes from that special meeting. Review of these corporate minutes reveals that as of the date of the special meeting, the shareholders had not received the down payment for the shares "as specified in the contract dated November 3, 1987." The minutes also reveal that the directors and officers were to resign their offices "as of the time of delivery" of Lane's bank check in the amount of $375,000 to Peter H. McCallion. The minutes also state that:

> "upon delivery of said down payment and said resignations, the sole shareholder of Indian Hill Associates, Inc. shall be Andrew J. Lane, who shall be then entitled to elect whichever directors and officers he chooses."

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[7]It is impossible to determine the name of the attorney who signed this proposal since his signature is somewhat illegible.

On February 11, 1988 the corporation closed on the purchase contract with Putnam and acquired title to the real property.

According to petitioner, the first payment of $375,000.00 was received by the shareholders on February 11, 1988, at the closing, at which time the shares were transferred to Lane (tr., p. 22).

Petitioner's representative asked petitioner what transpired on February 11, 1988 which led him to believe that the transfer of shares closed on that date, his response was:

> "[p]rior to that date all of the shareholders of Indian Hill Associates -- and I believe there were seven of them -- signed a consent to sell such shares. That was delivered to Mr. Lane's attorney at the closing on February 11, together with a document whereby the officers and directors of Indian Hill Associates, who were myself, Mr. Gargan, Mr. Fowler, resigned as officers and directors of Indian Hills [sic] Associates. And we also delivered that document to Mr. Lane's attorney. At that time we received a $375,000 check" (tr., p. 24).

According to petitioner, he brought a filled out stock certificate "ready to be signed" to the closing on February 11, 1988 (tr., p. 28). However, Mr. Lane's attorney David White indicated that the delivery of the shareholders' consent which transferred to Mr. Lane their equitable right to receive the actual stock certificates from the corporation was sufficient.

On February 11, 1988, petitioner filed with the Division the tentative assessment which had been previously issued to him. He also filed a Real Property Transfer Gains Tax Supplemental Return -- As completed by Transferor, Form TP-583 ("supplemental return") to elect to pay the gains tax in installments. The date of transfer listed on the supplemental return was November 3, 1987. Section B of the supplemental return is used if the actual cash received is less than or equal to the tax due. According to Section B, the amount of cash received was zero and the amount of tax deferred was $128,908.80.

In response to correspondence from the Division, petitioner sent a letter to Sharon Drosky, Tax Technician (Division's Exhibit "O"). In this letter petitioner supplied the following information to Ms. Drosky:

> "The shareholders of Indian Hill Associates, Inc. did not receive a purchase money mortgage from Andrew J. Lane when they sold him all the shares of the corporation on November 3, 1987.

"We have only Mr. Lane's promise to pay us the consideration. When we sold the corporation to Mr. Lane, we did not receive any portion of the consideration on the date of the transfer. That is why we have applied for treatment on the installment basis, and for a deferred payment plan.

"Mr. Lane purchased the shares in November, and closed on the property on February 11, 1988. The closing statement enclosed is that of Putnam Limited Partners, who sold the property to Indian Hill Associates, Inc. The purchase price to Putnam Limited Partners was $3,425,000.

"Subsequent to the closing between the seller and purchaser of the real property, the former shareholders of Indian Hill Associates, Inc. received the return of their downpayment on the contract to purchase the property from Andrew J. Lane.

"The first installment of the profit due the former shareholders is to be paid by Lane no later than July 1, 1988. This installment is $350,000. The second installment is to be paid by October 1, 1988, and is also $350,000. The final installment of $600,000 is due when all approvals for a subdivision are received from the Town of Putnam Valley."

On April 1, 1988, petitioner sent Ms. Drosky a copy of the January 4, 1988 letter agreement (***see***, Division's Exhibit "P"). In the cover letter which accompanied the letter agreement, petitioner again reiterated that the former shareholders of the corporation sold Lane their shares in the corporation, not the real property itself and that there was no purchase money mortgage securing payment of the debt. He further stated that there was no closing statement of the former shareholders in connection with the transfer of the real property from Putnam to the corporation because the former shareholders were not a party to that transaction "having sold their interest in the contract to Andrew J. Lane on November 3, 1987."

By letter dated August 18, 1988, the Division notified petitioner that his election to pay the gains tax due in installments had been accepted as filed (Division's Exhibit "Q"). According to the letter, the installment term was for a period of not more than 3 years, and minimum annual payment due on or before each anniversary date was $42,970.67. The "Anniversary/Closing Date" listed on the letter was November 3, 1987.

In July 1988, Lane made an installment payment of $350,000 on account of his purchase of the shares of the corporation (tr., p. 22).

In November 1988, petitioner made a gains tax installment payment to the Division in the amount of $42,970.67.

Lane did not make the installment payment of $350,000 due on October 1, 1988 to the former shareholders of the corporation. Instead, he commenced litigation on or about October 18, 1988 against petitioner and the other former shareholders alleging a defense to payment.

No approval of a subdivision was ever granted.

Lane filed a petition in bankruptcy under Chapter 11 on March 24, 1989 in the U.S. Bankruptcy Court, District of Massachusetts. His bankruptcy estate included the real property located in Putnam and Westchester Counties.

Petitioner did not pay the second installment gains tax payment in November 1989. Rather, he filed a Claim For Refund of Real Property Transfer Gains Tax ("claim for refund") (Division's Exhibit "F") dated November 1, 1989, for tax paid in the amount of $9,061.87 and the cancellation of the remaining installment balance of $85,938.13. Included in the attachments to the claim for refund is a Form TP-583 supplemental return and a letter which states the basis for the claim for refund.

Petitioner computed the tax on the supplemental return as follows:

1. Gain subject to tax as computed by Department of Taxation and Finance on Form TP-582		$1,289,088.00
ADJUSTMENTS BY TRANSFEROR		
2. Additions		
3. Subtractions	($950,000.00)	
4. Net adjustments		($950,000.00)
5. Gains subject to tax		339,088.00
6. Tax due (10% of line 5)		$33,908.80
7. Tax deferred		$42,970.67(paid)
8. Balance due		$0
9. Penalty due		
10. Interest due		
11. TOTAL DUE (add lines 8,9 and 10)		$0

Review of the letter which accompanied the claim for refund reveals that the basis of petitioner's claim for refund was a reduction in consideration. In his letter, petitioner stated that he had amended the gains tax return to subtract both the $600,000.00 of the purchase price which was due upon approval of a subdivision plan, as well as the $350,000.00 installment payment which was due on October 1, 1988. He noted in his letter that Lane had failed to make

the third payment of $350,000 due on October 1, 1988 and had subsequently filed a petition in bankruptcy on March 24, 1989 in the U.S. Bankruptcy Court, District of Massachusetts. Petitioner also noted that even though the purchase contract required a final payment of $600,000.00 to be made upon approval of a subdivision plan by the Town of Putnam Valley for the property which the corporation owned, Lane had not applied for any such approvals and based upon representations made by Lane to the former shareholders and to the Bankruptcy Court, it was unlikely that Lane would ever apply for such approvals.

Petitioner's explanation of how he arrived at the claim for refund figure of $9,061.87 follows:

> "The installment payment that I made in November, 1988 was for $42,970.67. Based upon the amount received to date, $425,000, minus the deductions previously allowed of $85,912, which yields a taxable gain of $339,088, the tax due is $33,908.80."
>
> "I have therefore made a claim for a refund of $9,061.87, based upon the difference between the amount paid to date and the tax due."

It is noted that some of the exhibits referenced in the letter which accompanied the claim for refund are not part of the record (tr., pp. 46-51).

During the hearing, petitioner was asked by his representative to clarify how he computed the claim for refund. Petitioner explained that the total consideration they received was $725,000.00 and that $300,000.00 had been paid as a down payment. He stated that he believed the profit to be $425,000.00 from which he subtracted the selling expenses allowed by the Division to arrive at the gain subject to the gains tax (tr., pp. 35-36).

The Division, on March 8, 1990, denied petitioner's claim for refund in its entirety and notified petitioner of its determination in a refund denial letter written by James Johnston, a tax technician in the Real Property Transfer Tax Gains Tax section of the Audit Division. In this letter, Mr. Johnston stated the Division's position regarding petitioner's claim that he did not expect to receive $950,000.00 originally claimed as consideration in the transfer. Mr. Johnston wrote, in pertinent part:

> "In October 1988, the transferee, Mr. Andrew Lane, was required to pay claimant $350,000 under the terms of the purchase agreement. Mr. Lane failed to make this

> payment and filed suit against claimant on October 14, 1988. Because this matter is, as yet, unresolved and no determination has been made with respect to the $350,000 payment, this amount cannot, at this time, be treated as a reduction in consideration.
>
> "The Department must take the same position concerning the payment of $600,000 due upon subdivision approval. Although Mr. Lane filed a petition in bankruptcy, pursuant to which the subject property may be sold, his intent with respect to the property has not yet been clearly established. The $600,000 payment shall be deemed consideration until such time as it is no longer possible for Mr. Lane to subdivide the property."

Mr. Johnston also notified petitioner that because he had failed to make the installment payment due in November of 1989, the entire unpaid balance of $85,938.13 had been assessed in accordance with Tax Law § 1442.

The Division issued a Notice of Determination (Notice No. L-001537708-8), dated March 30, 1990, to petitioner asserting additional real property transfer gains tax due in the amount of $85,938.13, plus interest of $3,892.17 and penalties of $15,468.85.

On July 10, 1990, the Bankruptcy Court approved the private sale of the real property to the mortgagee, Bankers Trust Company.

A Bureau of Conciliation and Mediation Services ("BCMS") conference was held on February 7, 1991. A Conciliation Order (CMS No. 106360), dated May 17, 1991, was issued which denied the request and sustained the statutory notice (L-001537708).

Petitioner filed a timely petition, dated August 7, 1991, which challenged the assessment of the additional real property transfer gains tax, plus penalties and interest and requested a refund of $9,061.87 in tax. In addition, petitioner requested that a judgment of liability for counsel fees and expenses in an amount to be determined be granted pursuant to CPLR 8601. Petitioner alleged, ***inter alia***, that the Division: (1) erroneously found that additional real property gains tax was due; and (2) erroneously found that no refund of real property gains tax paid was due in this matter. Petitioner asserts that no additional tax is due because of Lane's bankruptcy, and because the final installment payment of $600,000.00 was contingent upon approval of a subdivision, a contingency which never occurred. He also contends that a refund of tax paid in the amount of $9,061.27 should be granted.

On May 3, 1995 petitioner filed an amended claim for refund with the Division which requested a refund of the entire $42,970.67 in tax paid. In this amended claim for refund, petitioner claims that the consideration received totalled $725,000.00 and any additional consideration was "either (1) contingent upon a contingent event which never occurred or (2) a value properly resulting in the $1,000,000 threshold not being exceeded". He further claims that the additional "consideration" consisted of unsecured promises to pay money and that those promises were made by an individual purchaser who declared bankruptcy. The original amended claim for refund was submitted into the hearing record as Petitioner's Exhibit "8".

The Division's representative asked petitioner what the total consideration for the transfer was, his response was that "[t]here was a total consideration, non-contingent, of $1,075,000, and a contingent consideration of $600,000" (tr., pp. 43-44).

According to petitioner the stated non-contingent consideration of $1,075,000.00 was based upon Lane's totally unsecured promise to pay. He also averred that the total consideration he actually received was only $725,000.00; Lane never paid the additional $350,000.00 (tr., p. 53).

At some point, Lane's reorganization plan was confirmed and he was discharged from all claims and all debts that arose before the confirmation date. The record is silent as to the confirmation date.

Petitioner stated that the time for any appeal of the Bankruptcy Court's ruling has expired and that he has no chance of receiving anything more than $725,000.00 from Lane (tr., p. 33).

THE DETERMINATION OF THE ADMINISTRATIVE LAW JUDGE

The Administrative Law Judge determined that Lane acquired a controlling interest in the corporation on February 11, 1988 and not on November 3, 1987, as contended by the Division. The Administrative Law Judge concluded that it was the acquisition of the controlling interest by the transferee which triggered the tax. The Administrative Law Judge concluded that because Lane did not perform his obligation under the November 3, 1987 agreement (i.e.,

payment of $300,000.00 on the signing of the agreement), the shareholders were not under any obligation on November 3, 1987 to transfer the shares to Lane and they did not do so.

The Administrative Law Judge found that on February 10, 1988, each of the eight owners of record of the corporation's stock, including petitioner, executed a Consent of Shareholders to sell Lane their shares in the corporation. However, there was no evidence in the record that at any time prior to February 10, 1988 the shareholders consented to the transfer of their shares or that Lane acquired a controlling interest in the corporation which had an interest in real property.

The Administrative Law Judge concluded that on February 11, 1988, petitioner received $1,075,000.00 in consideration. She granted a portion of petitioner's refund claim, determining that $600,000.00 of the amount reported by petitioner as consideration was actually contingent consideration and was not required to be added to consideration as of the date of the transfer. The Administrative Law Judge noted that the Division had conceded in its post-hearing brief that if the transfer of a controlling interest in the corporation was found to have occurred on February 11, 1988 and not on November 3, 1987 and was subject to the $600,00.00 subdivision approval contingency, then petitioner was entitled to a reduction in consideration in the amount of $600,000.00. The Administrative Law Judge denied that portion of petitioner's refund claim alleging entitlement to a reduction of consideration by $350,000.00 because the unsecured promise to pay represented by that amount was, in effect, worthless on the date of the transfer. Further, the Administrative Law Judge denied petitioner's claim that the transfer of the controlling interest in the corporation was exempt from the imposition of transfer gains tax because the consideration for the transfer was below $1,000,000.00.

ARGUMENTS ON EXCEPTION

Petitioner argues that the amount of consideration received for the transfer of a controlling interest in the corporation was only $725,000.00 (the actual amount received) rather than the $1,075,000.00 determined by the Administrative Law Judge since the actual value of the promise to pay $350,000.00 on October 1, 1988 by Lane was zero on the day it was made.

Petitioner argues that the Administrative Law Judge erred in finding ***Matter of Cheltoncort Co***. (Tax Appeals Tribunal, December 5, 1991, ***confirmed Matter of Cheltoncort Co. v. Tax Appeals Tribunal***, 185 AD2d 49, 592 NYS2d 121) controlling here because this is not a case of subsequent events altering the value that the consideration had at the time of the transfer. Rather, based on the Tribunal's decision in ***Matter of Old Farm Lake Co.*** (Tax Appeals Tribunal, April 2, 1992), petitioner argues that Lane's unsecured promise to pay was shown to have been worthless when given because of Lane's "string of broken promises" and the fact that eight months subsequent to the transfer of a controlling interest, Lane had not only failed to make the payment of $350,000.00 then due but filed for bankruptcy (***see***, Petitioner's brief in support, pp. 6-7). Therefore, that note should be included in consideration at its fair market value on the date of transfer of $0 rather than at its face value. Petitioner did not raise on exception the argument made to the Administrative Law Judge that there is no tax due on the transaction because the overall consideration is less than $1,000,000.00. In opposition to the Division's exception, petitioner argues that the Administrative Law Judge correctly determined that Lane did not acquire a controlling interest in the corporation until February 11, 1988.

The Division argues that Lane acquired a controlling interest in the corporation on November 3, 1987. There were no conditions precedent nor any contingent consideration in the November 3, 1987 agreement. As a result, the consideration for the purchase of the shares was $1,675,000.00 rather than $1,075,000.00 as found by the Administrative Law Judge. Further, the Division argues that the Tribunal's decision in ***Cheltoncourt*** rather than ***Old Farm Lake*** controls here as to the $350,000.00 payment due but unpaid by Lane. As ***Cheltoncourt*** establishes, in calculating the amount of gains tax due, the value of the consideration has to be determined at the time of the transfer and subsequent events (such as the failure of the transferee to make the scheduled payment) do not alter the value of the consideration at the time of the transfer. The Division, in opposition to petitioner's exception, argues that the actual value of Lane's unsecured promise to pay $350,000.00 on October 1, 1988 was its face value.

OPINION

Tax Law former § 1441 imposed a 10% tax upon gains derived from the transfer of real property located within New York State.[8] Tax Law former § 1440(7) included in the definition of a "transfer of real property" the "acquisition of a controlling interest in any entity with an interest in real property." A "controlling interest" was defined in Tax Law former § 1440(2) as, in the case of a corporation, "either fifty percent or more of the total combined voting power of all classes of stock of such corporation, or fifty percent or more of the capital, profits or beneficial interest in such voting stock of such corporation."

There is little question that petitioner, as a result of his execution of the November 3, 1987 agreement, his reporting of the transaction on the transferor questionnaire and his correspondence with the Division subsequent thereto, represented to the Division that all the shares of the corporation had been transferred to Lane on November 3, 1987 pursuant to the agreement of that date. However, petitioner's inaccurate representation is not sufficient to change the legal consequences of that agreement.

As the Administrative Law Judge noted in her determination, it is the acquisition of a controlling interest, not the transfer thereof, which is the taxable event. The Division's regulations (20 NYCRR former 590.44) provide that:

> "in the case of a corporation which has an interest in real property, the acquisition of a controlling interest in the corporation occurs when a person or group of persons, acting in concert, acquires a total of 50 percent or more of the voting stock in such corporation. . . . Because the statute looks to the acquisition of a controlling interest, it is the act of the transferee which triggers the tax."

In examining the terms of the agreement, the conduct of the shareholders who did not personally execute the November 3, 1987 agreement and of Lane, the transferee, at and subsequent to the execution of that agreement, we agree with the Administrative Law Judge that, despite petitioner's representation, there was no evidence in the record that at any time prior to February 10, 1988 the shareholders consented to the sale of their shares or that Lane

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[8]The real property transfer gains tax imposed by Tax Law Article 31-B was repealed on July 13, 1996. The repeal applies to transfers of real property that occur on or after June 15, 1996 (L 1996, ch 309, §§ 171-180).

acquired a controlling interest in the corporation which had an interest in real property. The Division relies on our decision in ***Matter of Goldlex Holding Co.*** (Tax Appeals Tribunal, June 29, 1995) to support its argument that Lane acquired the shares of the corporation on November 3, 1987. We do not find that decision controlling. In ***Goldlex***, the issue concerned whether or not transfers of interests in real property were made pursuant to an agreement entered into prior to the effective date of Tax Law Article 31-B. Here, the transfer of corporate ownership was made pursuant to the terms of the November 3, 1987 agreement, as modified on January 4, 1988 and February 3, 1988. However, the issue before us is the date on which that transfer occurred, not the date on which the parties entered into the agreement to transfer. The Division argues that Lane could only close on the real property owned by Putnam if he had acquired 100% of the shares of the corporation on November 3, 1987. Had he done so on November 3, 1987, however, the subsequent actions of Lane and the shareholders would have been meaningless.

In ***Matter of Old Farm Lake Co***. (***supra***), we concluded that because an unsecured promise to pay was not a mortgage, purchase money mortgage, lien or other encumbrance, it was included within the scope of "any other thing of value" as provided in Tax Law former § 1440(1)(a). Accordingly, we concluded that the actual value of such note, rather than its face value, was to be included in calculating consideration given for the transfer of an interest in real property. The petitioner in ***Old Farm Lake*** introduced evidence of its method of calculation of the present value of the unsecured promissory note given as part of the consideration. Using the methodology provided in Internal Revenue Code § 483 for imputed interest, the petitioner applied a discount rate equal to 120% of the Federal long-term rate then in effect. The parties in ***Old Farm Lake*** also stipulated that if the petitioner prevailed in its argument that such note was to be valued at its actual value, the matter would be remanded for verification of the payments made and computation performed. Unlike the petitioner in ***Old Farm Lake***, petitioner in the instant proceeding has failed to introduce probative evidence of the actual value on February 11, 1988 of Lane's unsecured promise to pay $350,000.00 in October 1988. The question of value

is one of fact and petitioner bears the burden of proof on this issue (20 NYCRR 3000.15[d][5]). Other than petitioner's unsupported speculation that this promise to pay was worthless when given, there is no basis on which to conclude that the actual value of this promise differed from its face value. To the contrary, what little evidence there is in the record of Lane's financial condition disproves petitioner's position.

In a February 2, 1988 letter from Terence Gargan, Esq., one of the shareholders of the corporation, to David White, Esq, attorney for Lane on the purchase of the property at issue, Mr. Gargan stated: "I was pleased to hear that Mr. Lane has obtained a satisfactory commitment for financing the above transaction from MerchantsBank of Boston. I understand . . . that the loan proceeds will be more than sufficient to consummate the land purchase" (Exhibit "3"). This statement does not support petitioner's position that on the date of the closing of the sale of shares and purchase of the land at issue, the financial condition of Lane was such that petitioner could reasonably deem his unsecured promise to pay in six months approximately one-fourth of the balance due on the purchase to be totally worthless. Further, petitioner did not adopt this position of the worthlessness of the unsecured promise to pay until subsequent to Lane's failure to make payment as due. Correspondence with the Division subsequent to February 11, 1988 and prior to October 1988 indicates an expectation that payment would be made on time and in full. In short, petitioner's situation is easily distinguished from that of the petitioner in ***Old Farm Lake*** and he has not met his burden of proof to demonstrate that the unsecured promise to pay given by Lane was worthless on the date of transfer.

As a result of the foregoing, we affirm the determination of the Administrative Law Judge.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Peter H. McCallion is denied;
2. The exception of the Division of Taxation is denied;
3. The determination of the Administrative Law Judge is sustained;

4. The petition of Peter H. McCallion and his claim for refund are granted to the extent of Conclusion of Law "O" of the Administrative Law Judge's determination, but are otherwise denied; and

5. The Notice of Determination (L-001537708), as modified, is sustained.

DATED: Troy, New York
September 4, 1997

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Donald C. DeWitt
President

_____
Carroll R. Jenkins
Commissioner

_____
Joseph W. Pinto, Jr.
Commissioner