STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
F. W. WOOLWORTH CO.	:	DECISION DTA No. 809878
for Revision of a Determination or for Refund of Sales and Use Taxes under Articles 28 and 29 of the Tax Law for the Period June 1, 1986 through May 31, 1989.	:	

The Division of Taxation filed an exception to the determination of the Administrative Law Judge issued on December 2, 1993 with respect to the petition of F. W. Woolworth Co., 233 Broadway, New York, New York 10279. Petitioner appeared by Michael Bray, Esq. The Division of Taxation appeared by William F. Collins, Esq. (James P. Connolly, Esq., of counsel).

The Division of Taxation filed a brief in support of its exception. Petitioner filed a brief in opposition. The Division of Taxation filed a reply brief. Oral argument was heard on June 15, 1994, which date began the six-month period for the issuance of this decision.

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

ISSUES

I. Whether certain expenditures by petitioner for work performed on the Woolworth Building during the audit period qualified as capital improvements to real property and were therefore exempt from sales and use taxes under the Tax Law.

II. Whether penalties were properly imposed upon petitioner for failure to pay the sales and use tax as assessed.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge.[1] These facts are set forth below.

F. W. Woolworth Co. ("petitioner" or "Woolworth") is a New York corporation conducting a retail merchandising business throughout the United States. Woolworth's headquarters and home office are in the Woolworth Building (the "building") located at 233 Broadway in New York City. The building has been certified as a historic landmark structure.

The tax assessment in question arose subsequent to Woolworth's adoption of a major renovation plan to rehabilitate the building's ornate terra cotta facade, and roofing elements and windows. The restoration program was conducted in conformity with Federal and State guidelines for the restoration of historic landmark structures.

The amount spent by petitioner on the restoration program and charged to the capital account on Woolworth's books under the "Exterior Restoration Account" (Account No. 0175) for the period February 1977 through January 1990 totalled $25,785,110.65. Included in such amount were expenditures for the audit period totalling $2,068,254.00 During corresponding years, the assessed value of the Woolworth Building increased from $12,600,000.00 to $48,000,000.00 (between 1978 and 1990), and for the audit period (1986 through 1989) the increase in assessed value was from $26,500,000.00 to $40,000,000.00.

The expenditures made by petitioner related entirely to invoices from Brisk Waterproofing Co., Inc. ("Brisk"). Both petitioner and Brisk treated these expenditures as capital improvements exempt from New York State's sales and use tax. There were 66 Brisk invoices during the audit period, each consisting of a cover sheet with daily time sheets for the work done during the

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[1]Post-hearing petitioner submitted a series of proposed findings of fact. It was determined by the Administrative Law Judge that proposed facts nos. 1, 4, 6, 7, 10-13, 15, and 17-35 were fully supported by the record, and accordingly are reproduced and/or incorporated with others below. Proposed facts nos. 2, 3, 5, 8, 9, 14, and 16 were partially supported by the record, and as such, were accepted to that extent. Additional findings of fact are also set forth below by the Administrative Law Judge.

month preceding the date of the invoice. The time sheets listed the Brisk employees that worked on the job for a particular date and the number of hours that they worked, and contained a summary of the work performed by these employees. There were 20 Brisk invoices characterized as "inspection or L.L. 10 work" which were charged to Woolworth's Exterior Maintenance and Miscellaneous Repairs Account (Account No. 4690). Local Law 10 is a law enacted by New York City in 1981 requiring building owners to make perpetual inspections of the sides of the building to protect pedestrians. The remaining 46 invoices were characterized by Brisk as "restoration work" and charged by Woolworth to its Exterior Restoration Account (Account No. 0175). The determination of whether the daily work was restoration or inspection (or L.L.10) work was primarily done by Michael Radigan, a 38-year employee of Brisk Waterproofing, a nationwide masonry and waterproofing business, whose testimony was accepted as expert testimony in this matter. Mr. Radigan made his determination in this regard by examining the daily time sheets which summarized the work performed for a particular day as consisting of rigging, handling of transportation of heavy equipment up to a particular work location, removal of terra cotta, mold making, building of a curing room, inspection by an engineer, replacement of steel work, pouring pre-cast concrete stones, curing stones, transporting stones, resetting terra cotta, resetting pre-cast concrete, pointing, caulking, removal of rigging, and removal of debris. He determined that certain tasks constituted "restoration work" rather than "inspection or L.L. 10 work" due to the listing of the crews on the billings because certain people consistently did routine maintenance work, which was included as part of the inspection and L.L. 10 work and other workers, who had more expertise and experience, did reconstruction work. He was further able to discern restoration work from the field reports prepared by Facade Maintenance which were prepared on a weekly basis. These reports contained photographs of the areas to be restored and a description of recommended work that should be done by Brisk. In addition, he distinguished restoration work from the inspection or L.L.10 work due to the location on the building where the work was performed. He was aware that particular sections of the building,

due to exposure to wind and water, required major replacement and reconstruction work and also from the presence of large spalls in the glazing of the terra cotta that had penetrated the "biscuit" of the terra cotta discovered during inspection work, that a major failure was indicated. Daily time sheets for work in such locations referred to restoration work. "Spalls" are the spots or blotches on the terra cotta where there is no glazing and the yellowish, tanish biscuit is exposed.

The term "terra cotta maintenance repair" and "epoxy repair" were used in both the L.L.10 or inspection invoices and in the restoration work invoices, but had two different meanings. When doing L.L.10 work it was a matter of patching small spalls with epoxy. In reconstruction, however, after taking out the stones, repairing the steel, and rebuilding the masonry backup, the repair work involved repointing, finishing and coloring to match the building.

The work done by Brisk for Woolworth was pursuant to a contract between them executed in 1987 entitled "Agreement for Maintenance Services" ("the agreement"). This agreement was for "a five year continuous maintenance program for the building located at 233 Broadway, New York, New York . . . and more particularly the facade and exterior areas of the Building" (Petitioner's Exhibit #5). Under the contract, Brisk agreed to perform services for petitioner which included: 1) inspection of the facade and exterior areas of the building, including all terra cotta surfaces; 2) documentation of all deficiencies in or deterioration of the facade and exterior areas; 3) consultation with Woolworth's architect to establish restoration procedures for all conditions of deterioration; 4) to perform all work necessary to effectuate a comprehensive repair and maintenance program for the facade and exterior areas of the building, including, but not limited to cutting, repointing, caulking, terra cotta repair and replacement; 5) maintaining a complete photographic record of all deficiencies in or deterioration of the facade and exterior areas of the building; 6) bearing the responsibility for rigging and erecting all scaffolding for the program; 7) consulting with petitioner's architect frequently to review the status of the program; 8) assisting petitioner in the determination of whether any emergency stabilization work was

necessary; maintain daily work logs of the work performed by Brisk. The fee schedule set forth in the agreement provided the following:

> "All sums actually expended by Contractor for materials and expendable supplies shall be billed to Owner at Contractor's cost, including sales tax, plus twenty-five percent (25%) thereof."

Upon audit by the Division, the auditor concluded that all of the expenditures of $2,068,254.00 charged to Woolworth's Exterior Restoration Account were repairs and maintenance subject to New York State sales tax. At the hearing, the Division conceded that a part of these expenditures may have constituted capital improvements.

The auditor also identified $324,122.00 paid to Brisk and charged to Petitioner's "Exterior Maintenance and Miscellaneous Repairs Account" (Account No. 4690). These payments were also treated by Petitioner and Brisk as exempt capital improvements. The auditor classified these expenditures as taxable repairs and maintenance rather than capital improvements.

A Notice of Determination and Demand for Payment of Sales and Use Taxes Due dated March 20, 1990 was issued to petitioner for the period June 1, 1986 through May 31, 1989 asserting additional sales and use tax due with respect to the Exterior Restoration Account in the amount of $170,630.86 and the Exterior Maintenance and Miscellaneous Repairs Account in the amount of $26,740.06, for a total amount due of $197,370.92, plus penalty and interest. A second notice of determination dated March 20, 1990 was issued to petitioner for the same period asserting a 10% omnibus penalty in the amount $19,737.08.

At the hearing in this matter, the Division noted and agreed to a reduction of the tax asserted in the amount of $6,280.37 due to a duplication of taxation by the auditor.

Petitioner executed consent extending the period of limitations for the purpose of allowing the sales and use tax asserted as due for the period June 1, 1986 through November 30, 1986 to be determined at any time on or before March 20, 1990.

Petitioner presented the testimony of Richard Lefever, the General Manager of Facade Maintenance Design ("Facade"), whose educational background includes metallurgic engineering

and architecture. He provided testimony at the hearing that the parties agreed would be accepted as expert testimony. He holds a certificate of completion from the Restore Program, which was described by him to be an intensive masonry rehabilitation program in New York State. In his current position with Facade, he is responsible for administration and field coordination of exterior restoration services, preparation of condition reports regarding deterioration of the exterior of structures, preparation of drawings for competitive bidding of construction repairs and he is responsible for administration as the work progresses. Mr. Lefever described the nature of the work performed on the Woolworth Building as "an intensive exterior restoration project taking care of the deterioration to terra cotta facing material on an extremely large terra cotta building" (Tr., pp. 50-51).

Richard Lefever provided testimony in substantial detail regarding the composition of the building structure. He described the terra cotta substance as a fired clay material which bears similarities to brick, with the primary difference being the fact that terra cotta bears a glazed coating. It is a ceramic material that is fired during the formation of the block. The glaze is applied to the face of the block and is typically approximately one-sixteenth of an inch thick, acting as a very thin veneer that results in the waterproof portion of the terra cotta. The terra cotta material behind the glaze is called the biscuit. The biscuit is the structure of the terra cotta block. The glaze is intended to protect the terra cotta since the biscuit is an absorbent material. The face of the block (to which the glaze is applied) is about an inch and one-half thick. Each block is attached to the building's substructure of masonry or steel with iron hangers. There is a separate piece of iron for each one of the blocks.

Due to phenomena called "creep" and "compressive stress", it is necessary to probe behind the terra cotta panels and to stabilize the building's structural integrity by injecting epoxy into the back-up brick masonry. Creep is the shortening of the building frame over time due to gravity. Since the individual blocks of terra cotta are tied to the structure of the building, stress is built up in a wide variety of areas on the wall. The most effective way to alleviate this stress is to cut soft

joints into the mortar between the terra cotta units. Stress is also built up in the back-up brick due to expansion from moisture. Over the course of time, a substantial number of terra cotta blocks have so deteriorated from the loss of the glaze material that water begins seeping into the terra cotta block. When this moisture freezes, it expands in volume by about 8-12% and grinds away at the terra cotta biscuit.

When the mortar between the terra cotta panels gets wet, some of the salt in the mortar mix is put into solution and leached into the terra cotta biscuit where the glaze is missing. When the biscuit dries out due to evaporation from the sun, the salts recrystallize and come out of solution with an 8-10% volume increase. This salt recrystallization causes additional deterioration of the biscuit. There are certain areas of the building that are more susceptible to compressive stress build up and thermal movements, such as the corners of the building.

Mr. Radigan testified that approximately 80% of the work performed by Brisk is restoration work. Brisk has been involved in work on the Chrysler Building in New York City, the Trans-Am Building in San Francisco, and the White House, among many others. He indicated that the Woolworth Building is especially noted as the first building of its height and design to be totally clayed in terra cotta and that restoration work on a building of the type discussed in this case must follow certain rehabilitation guidelines which are addressed by the Department of Interior of Historic Places in Washington, D.C. Such guidelines require the owner to try and save the terra cotta cladding through reconstruction or duplicating the original features, even if this necessitates removing large sections and replacing them with new pre-cast concrete terra cotta.

The role played by Brisk in the work performed on the Woolworth Building included inspection, complex rigging, "sounding" the terra cotta, removal of defective portions and restructuring of such areas. In some cases there was removal of totally disintegrated pieces, replacement of such pieces with precast concrete and reconstruction of the under structure of the terra cotta. There are other situations where the structural steel showed signs of substantial rust caused by water entering through the terra cotta and held in suspension by the back-up brick, and

which consequently needed replacement. Certain other maintenance, referred to as pointing and dressing-up with epoxy, was done to the terra cotta sections that had not yet reached total deterioration. Mr. Radigan estimated that 90 to 95 percent of the dollars charged by Brisk went into replacement and reconstruction activity. During the audit period, $2,068,254.00 of the total amount billed ($2,392,376.00), or 86% was charged as a capital expenditure to the restoration work.

Mr. Radigan's testimony addressed the processes of reconstruction and replacement as they were employed in this case. He stated that reconstruction involved removing a substance, and then formulating a program for that area of the building. This analysis would then call for the reconstruction of the existing fabric or the replacement of the same with a totally new fabric, making sure that all the deficiencies uncovered behind the removal were addressed. Most of the restoration work done during the audit period consisted of reconstructing the biscuit of the terra cotta or replacing terra cotta panels in their entirety. The blocks or panels that required complete replacement were replaced with units fabricated from pre-cast concrete. The reconstruction of deteriorated biscuit was done with a bulky epoxy mixture. The epoxy that was used to replace the waterproof glaze was a thinner, more viscous material. Three to four thousand blocks were completely replaced with individually fabricated pre-cast concrete blocks. The biscuit of an additional two to three thousand blocks were reconstructed with bulky epoxy mixture.

The sections of the building that were addressed during the audit period were three of the four 43rd floor tourelles (or turrets), elevator bulkheads, gables between the 31st and 33rd floors on the north side, balustrades on the 28th floor and window spandrels on the 23rd floor. During his testimony, Mr. Radigan described a tourelle as a dome shaped collection of terra cotta units, in this instance covering vent structures located at the 43rd floor of the building. Balustrades are the vertical posts and horizontal rails which comprise a stairway-type railing along a parapet wall.

Terra cotta units that required replacement would first be measured to determine their shape and dimensions. Then, a mold would be created into which concrete would be poured. After this pre-cast unit was cured, it would be installed on the building with stainless steel anchors. If a terra cotta panel had lost more than a certain percentage of its glaze and the biscuit structure supporting the glaze was sufficiently deteriorated, it was no longer cost effective to reconstruct the panel and it would be subject to replacement.

Mr. Radigan of Brisk additionally provided testimony regarding the complex scaffolding and rigging system that was utilized by Brisk in order to access the work area. He stated that the architectural features of this particular building made it considerably difficult to hang the scaffolding, in part because the decking had to be cut specifically to fit the configuration of the wall where the work was being done. The scaffolding itself was a semi-permanent catwalk that had to be changed every five feet vertically. He indicated that in some cases, it would take the company weeks to get the scaffolding in place for a month's restoration work.

Mr. Lefever was questioned as to his opinion of whether the restoration work done on the Woolworth building extended its useful life. He responded that the restoration program, including both the epoxy repair work performed on deteriorated material, as well as the replacement work done with pre-cast concrete, served to extend the useful life of the building 20 years (Tr., pp. 62-63). Mr. Radigan's opinion was also elicited regarding the same aspect. He testified that the restoration work done during the audit period extended the useful life of the building between 20 and 30 years, and that the useful life of the building would have been dramatically shortened if such work had not been performed (Tr., p. 123).

Petitioner introduced into evidence 16 photographs exhibiting some of the more intricate details of the work performed on the building in issue. A synopsis below indicates the nature of the illustrations and testimony provided with each:

1) Photo #1 showed the general condition of balconies and an example of the stainless steel netting which was wrapped around a hanging pinnacle and secured with steel cables in order to protect a potential problem area until it could be fully addressed.

2) Photo #2 illustrates a tourelle on an elevator bulkhead before and after restoration.

3) Photo #3 is of the north bulkhead before and after restoration. In this photo there was a portion of the building that was being subjected to the process of sounding. A piece of terra cotta had been removed and the body of the building was being examined.

4) Photo #4 shows the condition of brick and terra cotta at the freight elevator bulkheads before construction. The rope in one of the segments of Photo #4 is securing certain terra cotta which is at risk of falling out of the building. The second illustrates a large spall of the glazing of the terra cotta which ultimately needs to be filled in with epoxy to avoid moisture penetration in that area.

5) Photos #5 and #6 illustrate the type of back-up brick that has been affected by freeze cycles and damaged by the same. Again, epoxy is used, and in this case, injected into the area. A chemical reaction stabilizes the back-up structure and the new terra cotta can then be anchored to that stabilized foundation.

6) The various photos in #7 and #8 give examples of the dismantling that takes place when certain portions of the building lose their structural integrity due to the freeze-thaw cycles and the reconstruction methodology that was implemented.

7) The next photo shows the restoration of three-story gables on the building between the 31st and 33rd floors.

8) The photos comprising #10 show the reconstruction of a tourelle, and contrast the before and after reconstruction.

9) The photos in #11-14 show the various types of conditions that are encountered in the reconstruction activity.

10) Photo #15 contrasts a section of a gable under repair and the completed gable.

11) The final photo is a closer view of a dissection of the terra cotta where the distressed brick is exposed and the structure is being supported by ropes.

OPINION

Tax Law § 1105 provides for the imposition of the sales tax on the receipts from the sale of tangible personal property and the rendering of certain services. Section 1105(c)(3) addresses those services of installing and servicing tangible personal property which are subject to the sales tax and, as pertinent here, provides an exception to the tax otherwise applicable when the property installed "will constitute an addition or capital improvement to real property . . . as such term capital improvement is defined" in Tax Law § 1101(b)(9).

Tax Law § 1101(b)(9) defines "capital improvement" as:

> "[a]n addition or alteration to real property which:
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> (i) Substantially adds to the value of the real property, or appreciably prolongs the useful life of the real property; and
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> (ii) Becomes part of the real property or is permanently affixed to the real property so that removal would cause material damage to the property or article itself; and
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> (iii) Is intended to become a permanent installation."

The regulations of the Division mirror the statutory definition (see, 20 NYCRR 527.7[a][3]) and also provide for an "end result test," i.e., "the imposition of tax on services performed on real property depends on the end result of such service. If the end result . . . is the repair or maintenance of real property, such services are taxable. If the end result of the same service is a capital improvement to the real property, such services are not taxable" (20 NYCRR 527.7[4]).

The Administrative Law Judge identified the "key determination" to be whether the "facets of the project in substance meet the criteria set forth by the Tax Law and regulations for an affirmative capital improvement determination."

In her analysis, the Administrative Law Judge opined that:

> "[w]hat sets apart repair activities which involve merely keeping real property in a condition of fitness, efficiency, safety or restoring it to such condition from activities which constitute a capital improvement, is the three-prong test of whether such improvement substantially adds to the value of the real property, becomes part of the real property such that removal would cause material damage, and whether the same is intended to become a permanent installation. The capital improvement criteria include by their very nature the repair and maintenance functions, i.e., a contractor is both repairing the real property and maintaining it while engaged in the process of doing something of a more permanent nature. Whether the individual facets of the work performed by Brisk in this case go beyond the maintenance point and rise to the level of a capital improvement depends upon the framework in which they are viewed, and the result of the application of the three-prong test. As additional guidance we are afforded the 'end result' test" (Determination, conclusion of law "G").

Applying this rationale to the work performed in the case, the Administrative Law Judge noted that certain of the work clearly meet the capital improvement criteria such as the reconstruction of the terra cotta, the replacement of terra cotta units, the reconstruction of the masonry substructure, as well as all the steps taken to accomplish the same, i.e., the inspection, rigging and erecting the scaffolding. She pointed out that other portions of the work such as the epoxy work that was done in order to patch the skin or the glazing of the terra cotta are less clearly defined. However, she determined that viewed on the whole, and applying the "end result test," the work was part of a capital improvement.[2]

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[2]In her discussion, the Administrative Law Judge noted that:

> "[f]or example, the epoxy work that was done in order to patch the skin or the glazing of the terra cotta, and was classified as epoxy repair on some invoices, falls into this gray area. A "spall" represents an area where there is no longer any glazing and the biscuit of the terra cotta is exposed. If total deterioration has not occurred, a more viscous epoxy substance is used to secure the area. From the testimony provided by the experts in this case, petitioner has proven that the epoxy used in that situation cures and becomes a part of the real property such that removal would cause material damage. It is intended to become a permanent installation, as is evidenced by the fact that it is not used as a temporary cure, and since it acts to protect the biscuit of the terra cotta as well as other major structural elements (such as those described and illustrated by the photos), petitioner has shown that such work appreciably prolongs the useful life of the real property. This type of epoxy work differs in a significant way from the mere repair of an interior wall such as spackling of drywall. When isolated spackling is done in a case where a portion of drywall is worn or damaged, e.g., punctured, the alteration to the real property may very well become part of the real property

(continued...)

The Administrative Law Judge concluded that:

> "[p]etitioner has well established by the documents, photos and testimony that the restoration work became part of the Woolworth building or was permanently affixed to the building so that removal would cause material damage to the building, and that such restoration work was intended as a permanent installation. In addition, such evidence, especially the uncontroverted testimony of the experts in this matter, Mr. Radigan and Mr. Lefever, established that the restoration work prolonged the useful life of the Woolworth building. As petitioner points out, isolated tasks might very well be deemed repairs and maintenance; however, where such activities are part of a major renovation project, a fact well established by the documents and testimony, the activities must be viewed in their entire context. To conclude otherwise would be losing sight of the permanence of the work done, the increased value to the building and ignoring the extension of the building's useful life (Determination, conclusion of law "E").

The core of the Division's exception is that the portion of the restoration project completed during the audit period, i.e., $2,068,254.00 of the $25,785,110.65 13-year program to restore the Woolworth building's ornate terra cotta facade and roofing and window elements in accord with Federal and State guidelines for the restoration of historic landmark structures, is not an "addition or alteration" to the building. Specifically, the Division asserts that the Administrative Law Judge's:

> "error is captured in her references to 'the three prong test' . . . for capital improvements. Contrary to her view, the definition of capital improvement does not simply provide for a three prong test. Rather, it has, quite indisputably, a threshold requirement that work done on real property constitute an 'addition or alteration.' Thus, under the definition, it is only where work on real property rises to the level of an 'addition or alteration' that one even reaches the issue of whether the work adds to the

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[2](...continued)
and be intended to become permanent. However, it is doubtful whether it substantially adds to the value of the real property or appreciably prolongs the useful life of the real property. Unlike the case at hand, where further serious deterioration can be avoided, the drywall is repaired for primarily cosmetic reasons and not for the purpose of prolonging the useful life of the wall or the building. It has been held by the Tax Appeals Tribunal that if a determination is made based on the facts presented in a case that the activities meet the statutory definition of capital improvement it is also a capital improvement under the 'end result test' (Matter of Nu-Look Specialists, Tax Appeals Tribunal, November 3, 1988). Independently viewing the 'end result' of the work performed in this case gives further support to the finding that the work undertaken by Brisk for petitioner was capital improvement in nature" (Determination, conclusion of law "H").

> value of the real property or extends its useful life, becomes part of the real property, and is intended to be permanent" (Division's brief, p. 19).

The Division acknowledges that "[t]he terms 'addition' or 'alteration' as used in section 1101(b)(9) are not defined further in the Tax Law or the Division's regulations. Nor has case law addressed their meaning" (Division's brief, p. 19). The Division asserts, therefore, that they should be given their dictionary meaning.[3]

The Division argues that the work covered by the "terra cotta maintenance invoices," i.e., reconstructing deteriorated blocks or replacing the blocks with prefabricated blocks, and the

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[3]The Division offers the following meanings:

"Black's Law Dictionary (5th Ed., 1979) defines 'addition' as follows:

> "**addition**. Implies physical contact, something added to another. Structure physically attached to or connected with building itself. Mack v. Eyssell, 332 Mo. 671, 59 S.W.2d 1049. Extension; increase; augmentation. Meyering v. Miller, 330 No. 885, 51 S.W.2d 65, 66. That which has become united with or a part of.

"Webster's Third New International Dictionary (1976) defines the same term as follows:

> "**addition**. n. 1a: the result of adding: anything added: INCREASE, AUGMENTATION b: something added that improves or increases value 2: the act or process of adding: the joining or uniting of one thing to another . . . 5a: a part added to or joined with a building to increase available space b: a suburban area marked out into streets and lots as a future residential section c additions pl: facilities, structures, equipment, or other property added to what is already in service . . .

"Thus, the clear meaning of 'addition' especially as relates to real property is something that enlarges or augments the real property.

> "As for the meaning of 'alteration,' Black's Law Dictionary defines it as follows:
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> "**alteration**. Variation; changing; making different. A change of a thing from one form or state to another; making a thing different from what it was without destroying its identity.

"Webster's Third New International Dictionary defines the same term as follows:

> "**alteration**. n. 1a: the act or action of altering . . . d: a change or modification made on a building that does not increase its exterior dimensions.

"Thus, 'alteration' in relation to real property refers to a change in the real property which modifies, but does not destroy, the building's character" (Division's brief, pp. 19-20).

associated work, does not constitute an "addition or alteration." Specifically, the Division asserts that:

> "that work, the purpose of which was to restore the Woolworth building's exterior as close as possible to its original condition, does not qualify as a capital improvement, even if, as the ALJ opined, the work adds to the value of real property or extends its useful life, becomes a part thereof, and is intended to be permanent.
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> "Reconstructing an existing terra cotta block cannot be considered an 'addition' because it does not involve an enlargement of real property. Nor can it constitute an 'alteration,' since its purpose is to restore the individual block to its original condition.
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> "Similarly, the replacement of a terra cotta block via a precast block does not enlarge a building or alter its essential character: again, it merely restores the exterior as closely as possible to its original condition" (Division's brief, p. 22).

The Division emphasizes that of 50,000 terra cotta blocks on the Woolworth building the Administrative Law Judge found that between three and four thousand were replaced and two to three thousand were reconstructed. The Division argues that:

> "if a mere replacement of part of a functional unit were held to constitute an addition or alteration within the meaning of the definition of capital improvement, then the distinction inherent in section 1105(c)(5) between repairs of real property and capital improvements would be obliterated" (Division's brief, p. 23).

In essence, the Division argues that:

> "any work on a building involving a repair . . . arguable [sic] always satisfies the last two prongs of the three-pronged, secondary requirement of the definition of a capital improvement, i.e., that the work become part of the real property, and is intended to be permanent" (Division's brief, pp. 23-34).

The Division asserts that the L.L. 10 invoice work also does not result in "an enlargement or substantial change of the character of a functional unit of a building . . ." (Division's brief, p. 27) and, thus, do not constitute a capital improvement. The Division also asserts that: the work represented by these invoices fails to meet the three-prong test of the definition; petitioner

did not prove that all the work was essential to the completion of the terra cotta reconstruction; and, thus, the end result test does not mandate that those invoices be deemed nontaxable.

Finally, the Division also asserts that Matter of Nu-Look Specialists (supra) is factually distinguishable and that petitioner has failed to meet its burden with respect to any of the nonconforming or missing invoices.

Petitioner responds to the Division's exception by asserting that a restoration project which meets the three criteria of the definition is a capital improvement. Petitioner asserts that the phrase "addition or alteration" is merely introductory to the three-part definition of capital improvement.

> "The notion that there is a separate 'addition or alteration' requirement that supersedes or is a condition precedent to the three-part definition of capital improvement is nowhere supported in the regulations or cases. . . . To the contrary, in Matter of Building Contractors Assoc. v. Tully, 87 AD2d 909, 449 NYS2d 547 (3d Dept. 1982), the Appellate Division, Third Department, held that the removal of construction and demolition debris qualified as a capital improvement, noting that 'it does not follow, as [Tax Commission] suggests, that the reference to "capital improvement"; in [§1105(c)(5) of the tax law] implies that services not directly resulting in additions to the real property are fully taxable'" (Petitioner's brief in opposition, p. 6).

Petitioner asserts that, in any event, if there is a separate "addition" or "alteration" requirement, petitioner meets the dictionary definition cited by the Division because that definition recognizes increases in value as an addition.

Petitioner also takes issue with the Division's introduction of the concept of "functional unit" such as a roof or a wall and the Division's assertion that replacing only a portion of a "functional unit," here the outer terra cotta facade of the Woolworth building, is "quintessentially a repair" (Petitioner's brief in opposition, p. 10). Petitioner asserts that whether the work done is partial or total is a superficial guideline.

> "The issue is not the totality of the work done during the audit period. The issue is the amount of added life and value resulting from the work. Petitioner has proven and the ALJ has determined that the

> work done by Brisk added substantially to the Building's life and value. The Division has not challenged this finding" (Petitioner's brief in opposition, p. 13).

Petitioner also rejects the Division's invoice by invoice approach and argues that in the case at bar the Division did not controvert the evidence of the invoices, the photos, field reports and the expert testimony of petitioner's witnesses, all of which well established that the restoration work was permanent and substantially prolonged the useful life of the Woolworth building. Petitioner embraces the determination of the Administrative Law Judge that:

> "isolated tasks might very well be deemed repairs and maintenance; however, where such activities are part of a major renovation project, a fact well established by the documents and testimony, the activities must be viewed in their entire context. To conclude otherwise would be losing sight of the permanence of the work done, the increased value to the building and ignoring the extension of the building's useful life" (Petitioner's brief in opposition, p. 14).

Finally, petitioner asserts that the imposition of penalties are "frivolous" at this juncture.

The Administrative Law Judge fully and correctly decided all of the issues in this case and we affirm her determination for the reasons stated therein.

In so concluding, we reject the Division's assertion that "addition" as used in section 1101(b)(9) is limited to an enlargement of the real property and that "alteration" excludes restoration of real property.[4] We find no basis for this limited definition of these terms in case law, the Division's regulations, nor even in the dictionary definitions to which the Division directs our attention. Further, it is inconsistent with the Division's own interpretation of the

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[4]The Division asserts that:

> "[r]econstructing an existing terra cotta block cannot be considered an 'addition' because it does not involve an enlargement of real property. Nor can it constitute an 'alteration,' since its purpose is to restore the individual block to its original condition.
>
> "Similarly, there placement of a terra cotta block via a precast block does not enlarge a building or alter its essential character: again, it merely restores the exterior as closely as possible to its original condition" (Division's brief, p. 22, emphasis added).

statutory language which embraces as capital improvements activities which, on their face, do not result in the enlargement of real property. We refer, for example, to the replacement of electric boilers; coal, electric and wood burning furnaces; garage doors; heating pump units; hot water heaters; attic fans; toilets; and central air conditioning systems, all of which the Division treats as capital improvements (see, "Publication 862: New York State and Local Sales and Use Tax Classifications of Capital Improvement and Repairs to Real Property").

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of the Division of Taxation is denied;

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

3. The petition of F. W. Woolworth Co. is granted; and

4. The notices of determination dated March 20, 1990 are cancelled.

DATED: Troy, New York
December 1, 1994

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

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