STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
EAST 61ST STREET COMPANY	:	DECISION DTA No. 811470
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 East 61st Street Company, c/o Donald J. Trump, 725 Fifth Avenue, New York, New York 10022, filed an exception to the determination of the Administrative Law Judge issued on July 13, 1994. Petitioner appeared by Spahr, Lacher & Sperber (Jack Mitnick, C.P.A.). The Division of Taxation appeared by William F. Collins, Esq. (Donald C. DeWitt, Esq., of counsel).

Petitioner filed a brief in support of its exception and the Division of Taxation filed a brief in opposition. Any reply brief by petitioner was due on November 29, 1994, which date began the six-month period for the issuance of this decision. Oral argument was not requested.

The Tax Appeals Tribunal renders the following decision per curiam.

ISSUES

I. Whether petitioner has established entitlement to more than the 50% allowed by the auditor on amounts claimed by petitioner for (i) accounting fees, (ii) development manager fees, (iii) costs incurred to "buy down" interest rates on purchasers' mortgages, and (iv) project over head costs so that its "original purchase price" should be correspondingly increased.

II. Whether petitioner has substantiated that the construction period extended beyond the transfer of the property to the cooperative housing corporation so that its "original purchase price" should be increased by interest payments made beyond the transfer.

III. Whether costs incurred to purchase tax abatements should be included in the calculation of petitioner's "original purchase price."

IV. Whether maintenance fees paid by petitioner to the cooperative housing corporation with respect to unsold units should be included in the calculation of petitioner's "original purchase price."

V. Whether the Division of Taxation properly disallowed petitioner's costs allocated to the renovation of certain townhouses and the construction of commercial space from inclusion in petitioner's "original purchase price."

VI. Whether the Division of Taxation properly disallowed the special additional recording tax of ¼% from inclusion in petitioner's "original purchase price" because such amount could be used as a credit against income tax liability.

VII. Whether petitioner has established that penalties should be abated.

FINDINGS OF FACT

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

The Division of Taxation ("Division") issued a Notice of Determination dated May 21, 1990 against petitioner, East 61st Street Company, asserting additional real property transfer gains tax due of $690,138.00, plus penalty and interest, as follows:

Tax Period Ended	Tax Asserted Due	Interest	Penalty	Number of Taxable Shares Sold
3/1/84	$ 90,570.00	$ 77,349.86	$ 31,699.50	9,714
4/1/84	255,702.00	213,969.90	89,495.70	27,425
6/1/84	100,807.00	80,982.48	35,282.00	10,812
5/1/85	113,525.00	71,347.60	39,733.75	12,176
6/1/86	86,729.00	38,267.71	30,355.00	9,302
3/1/87	42,805.00	14,659.96	14,981.00	4,591
Totals	$690,138.00	$496,577.51	$241,546.95	74,020

Petitioner is a partnership made up of three partners: Donald Trump, a 90% partner; Robert Trump, a 5% partner; and Louise Sunshine, a 5% partner. Petitioner was responsible for

the development of the luxury cooperative apartment project known as Trump Plaza on the east side of Manhattan at 167 East 61st Street, where units sold ranged in price from $243,000.00 for a unit on a lower floor to $950,000.00 for a penthouse unit.

The cooperative offering plan[1] for Trump Plaza, which noted that "[t]he approximate date of first offering of this Plan is December 10, 1982", referred to petitioner as the "sponsor-seller" under the plan. The Trump Corporation, located at 730 Fifth Avenue in Manhattan, was petitioner's so-called "selling-agent" under the plan.

The project consisted of a "tower building" which is described in petitioner's Exhibit "1" as consisting of:

> "[A] sub-cellar, a cellar, a lobby level and 38 floors. The sub-cellar and cellar will contain, in part, a garage with a capacity for approximately 128 automobiles. The lobby level will contain the building lobby and commercial space. Of the floors above the lobby level, the first will contain mechanical equipment and one residential apartment that will be occupied by the superintendent of the Property, the next 35 will contain a total of 175 residential apartments and the two highest will contain mechanical equipment. Each Townhouse consists of a cellar, a ground floor and three floors above the ground floor. There will be a total of four residential apartments in each Townhouse, one on each floor (other than the cellar). Thus, there will be a total of 184[2] residential apartments at the Property" (emphasis added).

The offering plan noted that "[c]onstruction of the Tower Building, and the renovation of the Townhouses, are scheduled to be substantially completed on or about January 1, 1984 . . . ."

The nature of the project was somewhat unusual. Petitioner acquired a 99-year leasehold on the west side of Third Avenue between 61st and 62nd Street in Manhattan from a Donald S. Ruth. Petitioner conveyed its rights under the leasehold to Trump Plaza Owners, Inc., the

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[1] Petitioner introduced into evidence a small portion of the offering plan as its Exhibit "1," consisting of photocopies of only nine pages. In fact, this was the only exhibit introduced into the record by petitioner.

[2] As noted below, there were 175 units covered by the offering plan. The nine-unit difference between the 175 units and the 184 units noted above appears to consist of eight units in the brownstones and the superintendent's unit. Petitioner's Exhibit "1" includes a section entitled "ground lease" which provides that, on the closing date, the cooperative housing corporation "will enter into a master lease of the commercial and retail portions of the Tower Building, together with the Townhouses, to the Trump Corporation." Therefore, it would appear that the eight units in the townhouses were leased away. Provisions of the offering plan concerning payments under this lease (if any) by The Trump Corporation to the cooperative housing corporation were not included in the record.

cooperative housing corporation, in exchange for cash and unsold shares on March 1, 1984 after construction was completed (or sufficiently completed so that units could be sold). At the end of the 99-year lease, the property will revert back to Mr. Ruth so that the cooperative housing corporation will have to negotiate a new lease or purchase the property.

The auditor's worksheet labeled "WEC & Audit Schedule" shows her computation of "estimated consideration" (emphasis added to show meaning of "WEC", i.e., "worksheet of estimated consideration") to be received by petitioner of $94,188,048.00 and of "anticipated gain on taxable sales" of $45,904,019.00. Gains tax due of $662,703.00[3] was calculated as follows:

Actual cash consideration	$76,034,328.00
Add: mortgage indebtedness	
Actual: $20,000,000.00 x 90.7686%	18,153,720.00
Total estimated consideration	$94,188,048.00
Less: (i) Fund reserved for housing corporation	(181,537.00)
(ii) Brokerage commissions	(5,249,295.00)
Balance	$88,757,216.00
Less: original purchase price	(42,853,197.00)
Anticipated gain on taxable sale	$45,904,019.00
Tax 10%	$ 4,590,402.00
Less: previous payments	(3,927,699.00)
Balance due	$ 662,703.00

The percentage of 90.7686%, used to allocate the underlying mortgage indebtedness of $20,000,000.00 assumed by the cooperative housing corporation, represents the percentage of "units sold per audit", which was calculated as follows:

	No. of Shares	Percentage	Units
Total per offering plan	81,548	100%	175
Less: grandfathered	5,245	6.4318%	13
Total taxable units	76,303	93.5682%	162
Units sold per audit	74,020	90.7686%	159
Units available for future			

[3]A Conciliation Order dated September 11, 1992 shows tax due decreased from $690,138.00, plus penalty and interest, as noted above, to $662,703.00, plus penalty and interest. The worksheet described above bears a date of October 17, 1991 (subsequent to the date of the Notice of Determination) as well as an unexplained additional date of July 15, 1992 next to the word "revised." It is noted that the Division did not present any witness to explain the audit. Furthermore, petitioner's representative objected to the Division including a "Report of Tax Conference" in its Exhibit "E," which the Division, in response, withdrew from its exhibit so that the record does not disclose the specific basis for the decrease in tax asserted as due by the conferee.

taxable sale	2,283	2.7996%	3

Mr. Mitnick, petitioner's representative who is an attorney as well as a certified public accountant, testified on behalf of petitioner and noted that "to date there are five unsold apartments" (Tr., p. 27). The variance between Mr. Mitnick's testimony and the auditor's calculation, which shows three unsold units, was not addressed by either party. A close review of the nine pages included in the Division's Exhibit "E" labeled "Schedule of Closed Apartments as of December 31, 1986" shows the typed names of purchasers for 164 units. In addition, the names of purchasers, with the number of shares and purchase prices, are pencilled in, presumably by the Division's auditor, next to seven units: 18C, 19A, 19C, 22C, 23C, 24C and 27C, respectively. The schedule shows four units unsold: 21C (681 shares); 32C (791 shares); 36B (415 shares) and 36C (831 shares). Consequently, a review of the relevant documents in the record shows four unsold units, in contrast to Mr. Mitnick's five unsold units and the three unsold units used in the auditor's calculation. The total unsold shares for the four unsold units noted on the schedule is 2,718. If the number of unsold shares calculated by the auditor of 2,283 is subtracted from 2,718, the difference is 435. It is noted that unit 36B appears to have allocated to it 415 shares. Perhaps this unit was sold after the auditor analyzed the schedule in Exhibit "E". If that was the case, then the difference of 20 shares might be explained by an undisclosed arithmetic error. In any event, the minimal presentation[4] by each party does not provide a way to do anything more than speculate in this regard.

As noted above, the Division's auditor subtracted $42,853,197.00 as petitioner's "original purchase price" from her calculation of "consideration" to compute the gain subject to tax. The Division did not introduce into the record an auditor's worksheet known as the "CACIC worksheet" (an abbreviation for computation of acquisition, capital improvements and conversion costs) to show how original purchase price was computed. However, Exhibit "E"

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[4] The minimal presentation may be the result of the parties believing that the matter was going to be settled on the day of hearing. The start of the hearing was delayed for approximately one hour at the request of the parties to permit them to negotiate a settlement, which proved unsuccessful.

includes a handwritten Schedule "A" dated October 28, in an undisclosed year, showing so-called "Total Adjusted Hard and Soft Costs" of $48,581,100.00 calculated as follows:

Hard costs claimed as of 12/31/86 - construction		$44,921,702.00
Less: Interest	$ 4,328,149.00	
Taxes	4,117,308.00	
	(8,445,457.00)	
Plus: Water & Sewage	104,684.00	
		(8,340,773.00)
Adjusted Hard Costs or Construction Costs		$36,580,929.00

Soft costs claimed as of 12/31/86 - project		$19,685,394.00
Less: Interest	$ 2,459,017.00	
Taxes	467,207.00	
Tax Abatement	195,468.00	
Sales Promotion	4,043,801.00	
Leasing Commission	3,600,790.00	
Rent & Occupancy	16,933.00	
Leasehold Costs	2,106,721.00	
Accounting Fees	76,270.00	
Development Manager	257,752.00	
Miscellaneous	68,995.00	
Buy downs	196,859.00	
	(13,489,813.00)	
Plus: Interest	5,403,714.00	
Taxes	400,876.00	
		(7,685,223.00)
Adjusted Soft Costs or Project Costs		$12,000,171.00
Total Adjusted Hard and Soft Costs		$48,581,100.00

On a handwritten Schedule "B" also dated October 28, in an undisclosed year, the auditor computed total original purchase price of $42,853,197.00 for shares sold (which corresponds to the amount used above) as follows:

Townhouse:

Hard cost - Brownstone renovation $ 672,224.00 = 1.8376%
Total hard costs $36,580,929.00

Soft costs $12,000,171.00 x 1.8376% = $220,515.00

Total townhouse costs:

hard	$ 672,224.00
soft	220,515.00
	$ 892,739.00

Total hard and soft	$48,581,100.00
Less: townhouse	(892,739.00)
	$47,688,361.00

Commercial space allocation $47,688,361.00 x 1%[5] = $476,884.00

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[5] It is unknown why 1% was used to allocate costs to the commercial space. Petitioner, however, did not raise this as an issue.

Total hard & soft costs $48,581,100.00
Less: Townhouse allocation (892,739.00)
Commercial allocation (476,884.00)
Total Soft & Hard Costs
Allocated to Shares $47,221,477.00 x 90.7686% sold

Total OPP/shares sold = $42,853,197.00

A notation on the Schedule "A", described above, indicates that the amounts subtracted from "soft costs claimed" for (i) "accounting fees" of $76,270.00, (ii) "development manager" of $257,752.00, (iii) "miscellaneous" of $68,995.00 and (iv) "buy downs" of $196,859.00 were the result of the auditor allowing only "50% of cost from 3/31/84[6] to 12/31/86." Another notation on the Schedule "A" indicates that the amounts subtracted from "soft costs claimed" for (i) "rent & occupancy" of $16,933.00 and (ii) "leasehold costs" of $2,106,721.00 resulted from the auditor allowing such costs "only til 3/31/84".

As noted in footnote "3", a Conciliation Order dated September 11, 1992 reduced tax asserted as due to $662,703.00, and the calculation of such reduced amount of tax due was detailed above which shows that an original purchase price of $42,853,197.00 was used in the calculation. Included in Exhibit "E" is a schedule labeled "Adjustment of Allocation of Mortgage Recording Tax" which shows "total original purchase price allowed" of $42,328,637.00, which is less than the original purchase price of $42,853,197.00 used to calculate tax due of $662,703.00 as asserted in the Conciliation Order. This schedule shows the following calculation:

Mortgage recording tax New York City = 2.25

N.Y. City	$1.25	
Basic	.50	
Additional	.25	
Special additional	.25	- full credit on NY State
	$2.25	income tax

Therefore the special additional must be removed from total costs - as follows.

$\frac{\$ .25}{\$2.25}$ = 11.1111% as applied to total mortgage tax paid

[6]It is unknown why the auditor used the March 31, 1984 date when Mr. Mitnick testified that the closing was on March 1, 1984.

Mortgage tax paid	$ 1,180,000.00
	.11
To be removed from costs	129,800.00

Total costs allowed for apartments	47,039,029.00
Less mortgage tax credit	129,800.00
Total cost allowed	46,909,229.00
Taxable per audit	90.2352
Total original purchase price allowed	42,328,637.00

The schedule then includes the following "revision" dated September 20, 1989 which used an increased allocation percentage of 90.7686 which corresponds to the percentage used above:

$47,039,029.00
129,800.00
$46,909,229.00
x 90.7686
$42,578,850.00

It is observed that even the "revised" original purchase price of $42,578,850.00 is less than the amount used by the conferee and, therefore, it does not appear that, in fact, petitioner's original purchase price was reduced in an amount equal to the special additional recording tax.

Included in the Division's Exhibit "E" is a Form DTF-940, "Advocate's Comments on Conciliation Conference" which notes that the "advocate", who was also an auditor in this matter, agreed with the findings of the conferee. She included the following "comments":

> "Due to the lack of substantiation by the taxpayer, only 50% of the accounting fees, develop. manager fees, miscellaneous and buy down costs from 4/1/84 - 12/31/86 were allowed. Also, at audit, the construction period interest was only substantiated till 3/31/84 and was allowed."

Petitioner's presentation consisted of the testimony of its representative, Jack Mitnick, who testified that he was "involved as the accountant for this project from its inception, prior to the formation of the partnership itself, through today" (Tr., p. 24).

Mr. Mitnick testified that on March 1, 1984 when the building was conveyed to the cooperative housing corporation, Trump Plaza Owners, Inc., it was not physically completed:

> "The units that were closed . . . were completed units . . . . The unsold units are not completed until purchasers have made various finishing selections . . . . As a consequence, a significant amount of construction costs remain to be expended and were, in fact, expended after the initial closing" (Tr., pp. 31-32).

Mr. Mitnick challenged the disallowance of interest of $1,383,452.00[7] because "the construction financing continues in place until such time as sufficient sales proceeds are generated to pay off the construction loan."

Mr. Mitnick provided no details or documentary evidence concerning the construction loans on which interest of $1,383,452.00 was allegedly paid subsequent to the closing on March 1, 1984. Most importantly, he did not provide any details concerning the amount of the construction loan outstanding, although it is possible to determine the dollar cost of work performed after the closing. A close review of the Division's Exhibit "E" discloses that a summary of construction costs (listing costs to September 30, 1986) shows a total amount of $44,860,673.00 and a summary of construction costs to March 31, 1984 shows a total amount of $37,663,994.00. The difference of $7,196,679.00 presumably represents construction costs expended in the period April 1, 1984 to September 30, 1986.

With regard to the other items which the auditor disallowed in her calculation of petitioner's original purchase price, as detailed above, and which petitioner contested, Mr. Mitnick testified as follows:

(i) Tax abatements of $195,468.00 represent amounts paid to certain unspecified "outerborough developers" for "tax abatements under 421-A or the J51 program," which petitioner "transferred" to its development site on the east side of Manhattan as well as filing costs paid to New York City for "certain abatements" (Tr., p. 33). Mr. Mitnick emphasized that the benefits from the tax abatements "runs entirely to the condo [sic] corporation" and lowers "the monthly carrying costs . . . and therefore [lowers] the monthly maintenance charges paid by the apartment purchasers" (Tr., pp. 33-34);

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[7]As noted above, the auditor allowed interest of $5,403,714.00 in calculating petitioner's "total adjusted hard and soft costs" or original purchase price. However, petitioner had included an interest amount of $4,328,149.00 in its hard costs and of $2,459,017.00 in its soft costs which total $6,787,166.00. The difference between this total and the amount allowed of $5,403,714.00 is $1,383,452.00, the amount of interest disallowed by the auditor which petitioner argues represents interest paid on construction loan(s) after the initial closing date. However, petitioner provided no details concerning such interest payments.

(ii) Leasehold costs[8] of $2,106,721.00 "represents condo [sic] carrying charges paid by the [petitioner] to the condo [sic] corporation with respect to unsold units" (Tr., p. 34);

(iii) Accounting fees of $76,270.00 were paid by petitioner to "the project accountant that was put in place by the lender, Manufacturers Hanover Trust Company . . . to verify that only costs of the project . . . were paid out of the loan proceeds (Tr., p. 35);

(iv) Development manager fees of $257,752.00 were paid by petitioner to "[a]n independent construction manager [HRH Construction] . . . to have his [sic] personnel on the premises until the completion of construction work" (Tr., p. 35);

(v) Miscellaneous costs of $68,995.00 represent project overhead "from the initial closing until the end of 1986 when construction was completed" including items such as "[c]ost of blueprints, supplies, other items that were incurred by the project manager on site, and which had to be paid over and above their fees" (Tr., pp. 36-37);

(vi) Buy downs of $196,859.00 represent "fees . . . paid [by petitioner] to mortgage lenders providing end loans to the purchasers of cooperative apartments . . . to reduce the interest rate" (Tr., p. 36);

(vii) Hard and soft costs of $892,739.00 allocated to renovation of the townhouses and of $476,884.00 allocated to construction of the commercial space should have been included in original purchase price as part of the overall project costs; and

(viii) Special additional recording tax of $129,800.00 was "a cost of the project" (Tr., p. 40).

On cross-examination, Mr. Mitnick noted that the special additional recording tax of $129,800.00 was reflected as a credit on petitioner's partnership return and "was passed through to the partners and would have been claimed on the individual returns of the partners." Mr. Mitnick has prepared Donald Trump's income tax returns for the last 20 years and testified

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[8]As noted above, the auditor subtracted "leasehold costs" of $2,106,721.00 because she allowed such costs "only til 3/31/84." Consequently, it appears that Mr. Mitnick might have misunderstood the nature of this item. Perhaps these costs relate to the unusual lease arrangement with Donald S. Ruth, who owns the land upon which the project was constructed. It seems possible that "leasehold costs" relate to payments made to Mr. Ruth pursuant to the 99-year ground lease covering the property which he holds. However, given the minimal nature of petitioner's presentation, this remains mere speculation.

that Mr. Trump had no income tax due against which the credit "could have been applied" (Tr., p. 41). As for the other two partners, he could not "state . . . whether the credit was availed of" (Tr., p. 40).

Mr. Mitnick testified that the amount of the tax abatement cost of $195,000.00 was not in dispute. He also testified that petitioner "substantiated" during the audit the leasehold costs of $2,106,721.00. According to Mr. Mitnick, accounting fees of $76,270.00, development manager fees of $257,752.00, project overhead (miscellaneous) costs of $68,995.00, and buy downs of $196,859.00 were all "costs incurred and verified[9] by the auditor, but only allowed to the extent [of] the fifty percent of the actual cost" (Tr., p. 34).

Petitioner did not introduce any specific evidence concerning the steps it took to ensure that it properly reported and paid gains tax on the transaction at issue.

OPINION

Tax Law § 1441 imposes a ten percent tax upon gains derived from the transfer of real property located within New York State. Gain for Article 31-B purposes is the difference between the "original purchase price" for the property and the "consideration" received for it (Tax Law § 1440[3]). Tax Law former § 1440[5] defined original purchase price as the consideration paid by the transferor to acquire the interest in the real property plus the consideration paid by the transferor for any capital improvements made to such real property prior to the date of transfer.

The Administrative Law Judge determined that Tax Law former § 1440 governs because the closing for the project occurred on March 1, 1984, three months prior to the statute being substantively amended to provide for additional costs that may be considered when determining original purchase price. Relying on Matter of V & V Properties (Tax Appeals Tribunal, July 16, 1992) for the proposition that this change was substantive, the Administrative Law Judge determined that legal, engineering and architectural fees incurred to sell the real property or to create ownership interests in cooperative form were not includible in "original purchase

[9]However, as shown above, the auditor's position was quite different. She noted her disallowance of these amounts because they were not "substantiated" by the taxpayer.

price." The Administrative Law Judge further determined that, under the old statute, costs incurred to "buy down" interest rates on purchasers' mortgages, costs for purchasing tax abatements and carrying charges paid by petitioner to the cooperative housing corporation with respect to unsold units were not includible in "original purchase price." Even if some of these costs were expended after the date of the amendment, the Administrative Law Judge found that petitioner did not prove which costs were expended after this date. The Administrative Law Judge also relied on Matter of 1230 Park Assocs. v. Commissioner of Taxation & Fin. (170 AD2d 842, 566 NYS2d 957, lv denied 78 NY2d 859, 575 NYS2d 455) for the proposition that maintenance and management charges on unsold shares are not costs incurred to create ownership in cooperative form. The Administrative Law Judge also noted that even under the subsequent, more liberal definition of "original purchase price," made effective by section 3 of Chapter 900 of the Laws of 1984, costs to "buy down" interest rates or to purchase tax abatements would not be included.

On exception, petitioner argues that the legal, engineering and architectural fees were not incurred to sell the real property but, rather, to acquire the property as well as construct improvements thereon and should be included in the original purchase price. Petitioner further asserts in its exception that Tax Law former § 1440 did cover costs to buy down interest rates, carrying charges and costs incurred to purchase tax abatements.

The Division argues that accounting fees, development manager fees, miscellaneous fees and buydowns were properly allowed to only 50% because petitioner could not establish the specific nature of these expenses or when they were incurred. The Division also points out that the leasehold costs represented carrying charges paid by the sponsor to the cooperative corporation with respect to unsold units. As found by the Administrative Law Judge, such costs have specifically been held by the courts and the Tribunal not to be includible in original purchase price.

We find the Administrative Law Judge correctly determined that the costs to "buy down"

interest rates, to purchase tax abatements and to pay carrying charges are not includible pursuant to Tax Law former § 1440(5), and we affirm the determination of the Administrative Law Judge for the reasons stated in the determination.

Next, the Administrative Law Judge found that 20 NYCRR 590.16, which became effective September 24, 1985, was applicable to determine consideration paid for capital improvements. As a result, the Administrative Law Judge concluded that accounting fees, development manager fees, interest on a construction loan, project overhead costs, interest paid on loans where the proceeds of such loans were used to make capital improvements to the real property, and mortgage recording tax may be included in "original purchase price" if incurred during the construction period. The Administrative Law Judge concluded that petitioner did not establish that it was entitled to any additional costs because it did not prove that any additional costs were incurred during the construction period.

The Administrative Law Judge, citing former 20 NYCRR 590.16(e), rejected petitioner's contention that the timing of payments should not be determinative. The regulation provides that:

> "[t]he construction period ends when the real property is substantially complete and ready to be placed in service. Some construction projects are completed in sections, leaving part of the real property capable of being used independently while construction continues on other sections. For such projects, allowable construction period expenses shall cease on each part when it is substantially complete and ready for use" (former 20 NYCRR 590.16[e]).

The Administrative Law Judge determined that petitioner did not establish that the Division acted improperly by treating the closing date of March 1, 1984 as the date on which the construction period ended. The Administrative Law Judge also found that petitioner failed to provide specific evidence that would match the additional costs claimed with the uncompleted sections. In concluding his discussion on this point, the Administrative Law Judge noted that it was reasonable for the auditor to allow 50% of such costs.

Petitioner further argues that former 20 NYCRR 590.16 does not limit costs to those incurred during the construction period, but requires only that they "clearly relate to a specific

project." Petitioner points out that in finding of fact "12," the Administrative Law Judge found that $7,196,679.00 of construction costs were expended between April 1, 1984 to September 30, 1986. The disallowance of 50% of these costs, argues petitioner, is clearly arbitrary.

The Division argues that, with respect to construction period interest, after the transfer to the cooperative corporation, the property was in use and interest on the construction loan could not be allowed beyond that time.

We find that the Administrative Law Judge correctly determined that petitioner could not include in its original purchase price, certain construction costs extending beyond the end of the construction period. As a result, we affirm the Administrative Law Judge on this issue for the reasons stated in the determination.

We must note, however, that petitioner is incorrect in asserting that the auditor disallowed 50% of $7,196,679.00 of the construction costs expended between April 1, 1984 and September 30, 1986. As found by the Administrative Law Judge, the auditor disallowed construction period interest after March 31, 1984 because he concluded that the construction period ended on this date. The auditor also disallowed 50% of accounting fees, development manager fees, miscellaneous and buydown costs incurred from March 31, 1984 to December 31, 1986 because of lack of substantiation. The Administrative Law Judge speculated that allowance of 50% of these costs after March 31st was the auditor's attempt to allow for costs incurred on uncompleted units after March 31, 1984. Given petitioner's failure to provide specific evidence that matched these additional costs to unfinished sections, we find nothing arbitrary about the auditor's conclusion on this score.

With regard to the costs to renovate the townhouses and construct the commercial space, the Administrative Law Judge determined that petitioner could not have its original purchase price increased by such amounts. The Administrative Law Judge based his conclusion on the fact that both the commercial portions of the Plaza Building and the townhouses were leased back to petitioner. The Administrative Law Judge stated that there was no evidence in the

record to show that the lease had any economic value in excess of the costs to construct and renovate said portions of the property. The Administrative Law Judge consequently found that the lease back could be viewed as "consideration" that "washes" the costs allocated to the renovation of the townhouses and the construction of the commercial space.

Petitioner contends that it was completely arbitrary for the Administrative Law Judge to uphold the disallowance of costs that were indisputably incurred for improvements of the townhouses and the construction of the commercial property.

The Division argues that none of the shares of the cooperative project were allocated to either the townhouses or commercial space. Consequently, the Division asserts that in arriving at the tax due, the total allowable costs of acquisition had to be allocated to the real property represented by these shares. The Division does not dispute that petitioner incurred these costs.

We reverse the determination of the Administrative Law Judge on this issue.

We find the Division improperly excepted from petitioner's original purchase price the costs to construct the commercial space and renovate the townhouses. We also find the Division erred in not including the value of the leaseback in the consideration given by the cooperative housing corporation. It is well settled that gains tax is imposed on the overall cooperative conversion plan (Mayblum v. Chu, 67 NY2d 1008, 503 NYS2d 316; Matter of 1230 Park Assocs. v. Commissioner of Taxation & Fin., supra; Matter of 61 East 86th St. Equities Group, Tax Appeals Tribunal, January 21, 1993). The record clearly reflects that the transfer to the cooperative housing corporation included the townhouses and the commercial space in the Plaza Building. We have in the past recognized that the Division may properly include in consideration paid on the transfer to a cooperative corporation the value of a leaseback given by the cooperative housing corporation (Matter of Cheltoncort Co., Tax Appeals Tribunal, December 5, 1991, affd Matter of Cheltoncort Co. v. Tax Appeals Tribunal, 185 AD2d 49, 592 NYS2d 121).[10] Likewise, the costs incurred on property to be leased back must be included in original purchase price. Without these components of the transaction, an

[10]To disallow, as the Division argues, these construction costs because shares were not allocated to the commercial space or townhouses would be inconsistent with Cheltoncort.

accurate reflection of the gain on the overall cooperative conversion cannot be achieved. Whether the gain is de minimis or not is irrelevant, the principle remains that the Division may not arbitrarily omit parts of a transaction that the Tax Law provides are includible. Accordingly, we conclude that petitioner is entitled to have the costs it incurred in the construction of the commercial space and in renovating the townhouses included in its original purchase price. We will not penalize a taxpayer for the Division's election to ignore part of a transaction.

Next, the Administrative Law Judge concluded that the Division properly disallowed the special additional recording tax of ¼% from inclusion in petitioner's "original purchase price" because such amount may be used as a credit against income tax liability by petitioner's partners.

Petitioner argues that there is no basis for disallowing the special additional mortgage recording tax.

The Division contends that to include the special additional mortgage recording tax in "original purchase price" would result in a windfall because the tax may be treated as a credit on the personal income tax of the respective partners.

We reverse the determination of the Administrative Law Judge on this issue.

As correctly found by the Administrative Law Judge, former 20 NYCRR 590.16 of the regulations which became effective September 24, 1985 is applicable to the matter before us. The regulation provides in part that:

> "(d) Question: What additional costs are allowed if incurred during a construction period?
>
> * * *
>
> "The items listed below, if paid for by a transferor for the construction of capital improvements made to real property, during a construction period, illustrate the types of costs that may be included in determining original purchase price:
>
> * * *
>
> "-- mortgage recording tax (building and loan mortgage only)."

As found in the auditor's notes at schedule six, petitioner was required to pay four mortgage recording taxes: New York City, Basic, Additional and Special Additional. The auditor allowed the first three but excepted the special additional recording tax for the reason stated above. This was improper. There is no provision in the regulation for excluding the special additional mortgage recording tax from original purchase price. The language of the Division's own regulation clearly allows for "mortgage recording tax" to be included in original purchase price with no qualifications. Absent a limitation in the regulation, we see no basis for disallowing a mortgage recording tax merely because a double benefit may be derived.[11]

As a final matter, the Administrative Law Judge determined that petitioner did not establish that its failure to pay tax was due to reasonable cause and not willful neglect.

Petitioner asserts that it prepared its tax returns based on competent professional advice and based on all of the facts and information. Further, petitioner argues there has been no showing of willful neglect.

The Division concludes by asserting petitioner has failed to establish willful neglect warranting abatement of penalty in this matter.

We find the Administrative Law Judge correctly determined that petitioner did not prove that penalty should be abated and we affirm for the reasons stated in the determination.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of East 61st Street Company is granted to the extent that the Division of Taxation is directed to include in the calculation of original purchase price the amounts disallowed on audit for renovating the townhouses and constructing the commercial space and for the special additional mortgage recording tax, but is otherwise denied;

2. The determination of the Administrative Law Judge is modified to the extent indicated

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[11]We note that 20 NYCRR 590.17 (effective November 9, 1994) specifically provides that among allowable costs associated with capital improvements is the special additional mortgage recording tax, but only for transfers on or after April 15, 1993. We find that this limitation is not controlling. As noted above, the regulations in effect during the period at issue clearly provide, without limitation, that mortgage recording tax is includible in original purchase price. We find nothing in the change made by section 60 of Chapter 57 of the Laws of 1993 that would lead us to conclude that the special additional mortgage recording tax had not always been contemplated as a mortgage recording tax. Consequently, the subsequent amendment to the Commissioner's regulations confirms our conclusion that the phrase "mortgage recording tax" includes the special additional mortgage recording tax.

in paragraph "1" above, but is otherwise affirmed;

3. The petition of East 61st Street Company is granted to the extent indicated in paragraph "1" above, but is otherwise denied; and

4. The Division of Taxation is directed to modify the Notice of Determination dated May 21, 1990 to the extent indicated in paragraph "1," but such Notice, as modified by the Conciliation Order dated September 11, 1992, is otherwise sustained.

DATED: Troy, New York
May 25, 1995

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

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