STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
V & V PROPERTIES	:	DETERMINATION
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, V & V Properties, 86-01 114th Street, Richmond Hill, New York 11418, filed a petition 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 (File No. 801487).

A hearing was commenced before Dennis M. Galliher, Administrative Law Judge, at the offices of the Division of Tax Appeals, Two World Trade Center, New York, New York, on January 6, 1988 at 9:15 A.M., was continued on July 26, 1988 at 1:45 P.M., and on October 18, 1988 at 1:30 P.M., and was continued to conclusion on July 26, 1989 at 1:15 P.M., with all briefs to be submitted by September 21, 1990. Petitioner appeared on the first hearing date by Duoba & Hill, Esqs. (Valdas C. Duoba, Esq., of counsel), and on each of the subsequent hearing dates by such counsel and by Bergman, Horowitz & Reynolds, Esqs. (James R. Brockway, Esq., and Joy Myasaki, Esq., of counsel).[1] The Division of Taxation appeared at all times by William F. Collins, Esq. (Paul A. Lefebvre, Esq., of counsel).

ISSUES

I. Whether the July 28, 1983 acquisition of a controlling interest in petitioner, a partnership, by one Lucio Petrocelli properly results in gains tax liability to petitioner computed

[1]By letter dated June 19, 1990, the firm of Bergman, Horowitz & Reynolds, Esqs. (James R. Brockway, Esq., of counsel), formally advised both parties and the administrative law judge of its withdrawal from representing petitioner in the subject matter.

upon the difference between consideration of $8,620,000.00 versus an original purchase price of $5,471,830.00.

II. Whether, assuming tax is determined to be due, petitioner has established any basis for the remission or abatement of penalty imposed for its failure to have filed returns and paid tax due in a timely manner.

III. Whether, again assuming tax is determined to be due, interest should accrue on the entire amount of tax due commencing as of the July 28, 1983 date of the subject transfer of the controlling interest.

FINDINGS OF FACT

On June 18, 1984, the Division of Taxation issued to petitioner, V & V Properties ("V & V"), a Notice of Determination of Real Property Transfer Gains Tax Due under Tax Law Article 31-B (more commonly known as the "gains tax"). This notice assessed gains tax liability in the amount of $750,000.00, plus penalty and interest, based upon the Division's position that a controlling interest in V & V had been transferred to one Lucio Petrocelli on July 28, 1983, and that such transfer was a taxable transaction. Since petitioner did not comply with the pre-transfer filing provisions (see, Tax Law § 1447), and since full documentation as to petitioner's original purchase price was not subsequently supplied to the Division as requested, per letters issued as early as January 1984 and thereafter, the Division made no allowance for original purchase price and simply calculated gain as being equal to the $7,500,000.00 amount of consideration allegedly received, with tax due computed as 10 percent thereof ($750,000.00).

Based upon additional information provided by petitioner during the course of these proceedings, the Division has twice revised and reduced its initial calculation of tax due.

(a) The Division first recalculated consideration received and original purchase price as follows:

Consideration:

$ 250,000.00	Cash Deposit
$5,245,000.00	Cash received before July 29, 1983
$2,000,000.00	Third mortgage to Litas
	"Kicker" consideration at 10% of

$1,739,000.00	condominium sales
$9,234,000.00	Total

Original Purchase Price:

$4,800,000.00	Mortgage
$ 135,000.00	Accrued interest
$ 94,000.00	Back taxes
$ 34,000.00	O'Hara buyout
$ 196,000.00	Dinolfo buyout
$ 17,830.00	Capital improvement receipts
$ 195,000.00	Sewage treatment facility
$5,471,830.00	Total

Comparing the above two totals ($9,234,000.00 less $5,471,830.00) results in a gain of $3,762,170.00 and a revised tax due of $376,217.00, plus penalty and interest.

(b) The Division's second revision to liability was based upon additional information provided. Specifically, the parties agreed that the maximum additional "kicker" consideration received on condominium unit sales was $1,125,000.00. This agreement reduces total consideration to $8,620,000.00 which, when compared to an original purchase price of $5,471,830.00, leaves a gain of $3,148,170.00, and a revised tax due of $314,817.00, plus penalty and interest.

V & V was an Illinois limited partnership formed in 1968. At the time of formation, one Vytautus Vebeliunas was the partnership's sole general partner. In 1975, Mr. Vebeliunas continued to be V & V's sole general partner, with V & V having approximately 70 limited partners, most of whom were small, individual investors. In 1975, Litas Investing Co., Inc. ("Litas"), a New York corporation having approximately 500 shareholders, was one of V & V's limited partners. Mr. Vebeliunas was, and continues to be, a principal of Litas. The date when Litas became a limited partner in V & V and its initial percentage of interest therein was not specified in the record.

The real property involved herein was an apartment complex known as Hidden Hollow Garden Apartments ("Hidden Hollow"). Hidden Hollow consisted of 18 two-story buildings, housing a total of 280 garden apartment units, located on approximately 37.1 acres of land in Wappingers Falls, Dutchess County, New York. In addition to the 18 two-story residence

buildings at Hidden Hollow, the complex also included a combination clubhouse and office building, a shed for storage of swimming pool equipment, and a barn used for maintenance equipment storage. Other improvements at the complex included a 30' by 100' swimming pool, two "doubles" tennis courts, a children's playground, parking areas and landscaping.

Prior to December of 1975, Hidden Hollow had been developed, constructed, owned and operated by a New York general partnership known as Kord Company ("Kord"). In 1973, Kord's six partners were the following individuals: Charles Dinolfo, Joseph Dinolfo, Laurence Kleinman, John Reventas, James O'Hara and Neil Saltzman. In 1973 and 1974, the six individual partners of Kord were also the principals of Dutchess 3 Realty Corp. ("Dutchess 3"), a New York corporation. During 1973 and 1974, Dutchess 3 obtained from Citibank four construction loans for the Hidden Hollow project totalling $4,800,000.00 (the "Citibank construction loans"). These loans were secured by mortgages on Hidden Hollow.

V & V's Acquisition of Hidden Hollow through Kord

In December 1975, the Hidden Hollow project was in severe financial difficulty. The Citibank construction loans were in default and Citibank was threatening to foreclose on the mortgages. Around December 1975, after obtaining Citibank's approval, V & V began negotiations for the acquisition of Hidden Hollow from Kord, including V & V's participation in the project. V & V's objective at and after that time was to complete construction of the Hidden Hollow project, under Citibank's supervision, to stabilize the rent roll, and eventually to sell the apartment units as condominiums.

Pursuant to an agreement dated December 26, 1975, V & V was to become a general partner in Kord, acquiring a 49% interest therein. Pursuant to the terms of the December 26, 1975 agreement, V & V was to convey to Kord's partners 38 investment units in V & V valued at $10,000.00 each. V & V and Kord's partners also agreed that V & V was to assume the following liabilities:

(a) the Citibank construction loans of $4,800,000.00, plus accrued interest;[2]
(b) a truck loan of $5,477.00 owed to Citibank;
(c) a loan of $55,000.00 owed to County Trust Co.;
(d) accounts payable of $40,700.00 owed to building contractors;
(e) tenants' rent security of $21,254.00;

(f) outstanding real estate taxes of $94,000.00; and
(g) a short-term loan of $30,000.00 owed to Citibank.

The December 26, 1975 agreement described above was subsequently modified by an agreement dated May 21, 1976. The modified agreement called for V & V to receive a 50% interest in Kord in exchange for infusing $225,000.00 in cash into the partnership and assuming liability for real estate taxes of $94,000.00 and accrued interest of $135,000.00 (accrued after April 1, 1976) owed to Citibank on the Citibank construction loans. The May 21, 1976 agreement also modified the December 26, 1975 agreement with respect to the other liabilities that V & V had agreed to assume under the earlier agreement. More specifically, pursuant to the May 21, 1976 agreement, V & V directly assumed only the liabilities owed by Kord to Citibank, and did not assume the other liabilities referred to in the December 26, 1975 agreement. Petitioner alleged, however, that the other liabilities remained as liens against Hidden Hollow which were paid by V & V out of the operating cash flow of the project. Finally, the May 21, 1976 agreement also called for V & V to satisfy certain loans in the aggregate amount of $40,000.00 made by Litas to two of Kord's partners, to wit, Charles Dinolfo and John Reventas.

V & V also purchased the interest in Kord held by James O'Hara, as such had devolved to Mr. O'Hara's wife upon his death. Documents in evidence list the contract purchase price for such interest to be $40,000.00, and petitioner alleges it paid such amount. The Division asserts, by contrast, that petitioner has documented only $34,560.00 as the amount actually paid.

Pursuant to an agreement dated March 10, 1977, the agreements of December 26, 1975 and May 21, 1976 were further modified. Pursuant to the March 10, 1977 agreement, V & V

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[2]As of April 1, 1976, Citibank determined that the accrued interest on the construction loans totalled $348,692.98.

noted an increase in its interest in Kord to 60%, and recognized that the sum of $25,000.00 had been "previously advanced to Charles Dinolfo and John Reventas". While this agreement specifies V & V's right to be repaid this $25,000.00 amount before any partnership payments to Messrs. Dinolfo and Reventas, the agreement does not specify the nature or purpose of the $25,000.00 advance. The agreement, however, specifies at paragraph 3 (see Exhibit 20[2]) that the increase in V & V's ownership interest in Kord from 50% to 60% results from the purchase of the O'Hara interest as described above (as opposed to resulting from the $25,000.00 amount advanced to Dinolfo and Reventas).

Pursuant to an agreement dated February 21, 1979, V & V allegedly paid, inter alia, an additional $50,000.00 to Dinolfo and Reventas, and also forgave indebtedness of $6,000.00 owed by Reventas, in exchange for Dinolfo's and Reventas' remaining interests in Kord. The Division maintains there is no evidence proving such payments were in fact made, and argues that a subsequent agreement dated November 1, 1979, calling for (inter alia) a payment of $112,000.00 to Dinolfo and Reventas plus relief from $6,000.00 of debt owed by Reventas as described, superceded the February 21, 1979 agreement as to the amount actually paid. Petitioner also maintains that the 38 investment units in V & V initially to be conveyed by V & V to the Kord partners pursuant to the December 26, 1975 agreement were eventually repurchased by V & V at $10,000.00 per unit. The Division challenges this allegation as unproven.

On or about February 22, 1979, an amended business certificate was filed in the Dutchess County Clerk's Office indicating the withdrawal of Dinolfo and Reventas from Kord, thus leaving V & V as the sole surviving participant doing business under the name of Kord Company. An indenture subsequently executed on August 14, 1979 transferred Hidden Hollow from Kord to V & V. This indenture was recorded in the Dutchess County Clerk's Office on August 20, 1979.

Petitioner summarizes the total consideration paid by V & V to acquire Hidden Hollow through Kord to be $6,071,123.98, consisting of the following amounts:

(a) $380,000.00; investment units in V & V, valued as $10,000.00 each, as repurchased;
(b) $4,800,000.00; Citibank construction loans;
(c) $5,477.00; truck loan from Citibank;
(d) $55,000.00; loan from County Trust Company;
(e) $40,700.00; accounts payable to building contractors;
(f) $21,254.00; tenants' rent security;
(g) $30,000.00; short-term loan from Citibank;
(h) $348,693.00; accrued interest as of April 1, 1976 on Citibank construction loans;
(i) $135,000.00; additional accrued interest (post 4/1/76) on Citibank construction loans;
(j) $94,000.00; real estate taxes;
(k) $40,000.00; satisfaction of loans owed by Charles Dinolfo and John Reventas to Litas;
(l) $40,000.00; payment to purchase James O'Hara's interest;
(m) $75,000.00; payments of $25,000.00 and $50,000.00 made to Charles Dinolfo and John Reventas; and
(n) $6,000.00; forgiven loan owed by John Reventas.

Capital Improvements
Direct Costs and Additional Construction Period Costs

Citibank closely monitored V & V's activities in connection with the Hidden Hollow project. Initially, V & V was required to obtain Citibank approval for all disbursements for expenditures, including both operating expenses and capital expenses. The nature of a given expense was allegedly agreed upon between the resident manager at Hidden Hollow and a Citibank representative. V & V was also required to submit financial statements on the project for Citibank's review. These financial statements were prepared for V & V by one Joseph Polito, a public accountant, pursuant to the Citibank requirement.

Petitioner alleged, via Mr. Vebeliunas' testimony, that when V & V began its acquisition of Hidden Hollow in December 1975, the complex was approximately 60% completed and had an occupancy level of approximately 40%. Petitioner also alleged that, from the period 1976 through 1978, a "construction crew" was maintained at Hidden Hollow which fluctuated in number from 10 to 20 employees. Certificates of occupancy for 14 of the residential buildings had been issued by 1974 with 2 additional certificates issued in 1977.[3] Mr. Vebeliunas testified that "upon our taking control of it all, the structures were under roof and inside panelings were

[3]The record does not specify when (or if) certificates of occupancy were issued for the remaining two buildings.

done but a lot of finish work, carpeting, stairways, and some windows had to be removed and replaced. We had to finish interiors, some exterior, make the project habitable." Paragraph 2 of the May 21, 1976 amended buy-in agreement provides that "[a]n inventory of the vacant apartments reflects a certain amount of missing equipment and substantial repair required (emphasis added). Cost estimates and a "summary of necessary improvements" dated June 14, 1976 and prepared by A.K. Guidelis, Architect (see Exhibit "6 [5]"), lists an estimated cost of $593,300.00 for items such as painting, caulking, installing gutters, installing flashing, insulating water pipes, exterior site regrading and landscaping, and replacing wooden siding with vinyl, as recommended.

In 1976, petitioner allegedly incurred capital improvement costs of $283,610.00 consisting of the following amounts:

(a) $109,379.00 in direct capital improvement costs to complete the project;
(b) $129,600.00 in interest on Citibank construction loans;
(c) $10,685.00 in property taxes;
(d) $14,154.00 in school taxes;
(e) $6,992.00 in property insurance; and
(f) $12,800.00 for guaranty fee on Citibank construction loans.

The dollar amounts of Items (b) through (f) represent 40% of the total annual amount of each of such enumerated costs, apparently based on petitioner's estimate that Hidden Hollow was 60% completed at the time of petitioner's acquisition thereof. The Division challenges the propriety of including these amounts in original purchase price, alleging a lack of proof that all of the amounts listed in item "a" actually constituted capital improvements. The Division also argues there is insufficient proof that a construction period was ongoing, and alternatively, alleges a lack of proof as to the actual percentage of the project which was in fact still under construction and which could be the subject to an allocation.

In 1977, V & V allegedly incurred capital improvement costs of $375,288.00, similar in nature to those for 1977, as follows:

(a) $159,661.00 in direct capital improvement costs to complete the project;
(b) $172,800.00 in interest on Citibank construction loans;
(c) $10,065.00 in property taxes;
(d) $14,154.00 in school taxes;
(e) $5,808.00 in property insurance; and

(f) $12,800.00 for guaranty fee on Citibank construction loans.

As above, items (b) through (f) herein represent 40% of the total annual costs of such enumerated items. So too, the Division challenges all of the items upon the grounds described above.

V & V also incurred an additional capital improvement cost in 1977, involving the construction of a waste treatment plant for the project. Petitioner claims capital costs of $195,000.00 plus $17,598.15 consisting of the following items:

(a) $195,000.00 paid to the construction company under the construction contract for the treatment facility;
(b) $50.00 for title and recording fees;
(c) $15,000.00 in architect's fees;
(d) $1,048.00 in attorneys' fees; and
(e) $1,500.00 in mortgage taxes.

The Division, by contrast, has allowed the amount specified at (a) above, but has denied the following three items as not allowable expenses and has denied the final item as unsubstantiated.

In 1978, V & V allegedly incurred capital improvements of $429,136.00 consisting of the following amounts:

(a) $213,167.00 in direct capital improvements to complete the project;
(b) $172,800.00 in interest on Citibank construction loans;
(c) $10,065.00 in property taxes;
(d) $14,154.00 in school taxes;
(e) $6,150.00 in property insurance; and
(f) $12,800.00 for guaranty fee on Citibank construction loans.

As above, items (b) through (f) represent 40% of the total cost of such enumerated items. So too, the Division challenges these items as described.

The Division, after review, allowed in total $17,830.00 as capital improvement costs out of the amounts described above as direct capital improvements (item "a" from Findings of Fact "16", "17" and "19"). However, no listing of the specific items allowed as capital improvements was provided. Petitioner's evidentiary submission on these costs consisted of three file folders full of invoices and bills organized in no particular order and with no specific summarization or explanation of such items save for the general assertion that all of such

amounts constituted direct capital improvement expenditures includable in the original purchase price ("OPP"). Included among the folders of invoices alleged to represent capital expenditures were payments for paint (and painting), carpet (and installation), and snow removal as well as some invoices with no description at all.

Costs of Refinancing and Protecting Title

Although the financial situation improved under V & V's management, Hidden Hollow continued to face serious financial difficulties. In January 1979, Citibank filed a mortgage foreclosure action with respect to the Citibank construction loans against Kord and V & V, among others, in the Supreme Court of New York, Dutchess County. To prevent a foreclosure, on January 17, 1979, Kord (i.e., V & V d/b/a Kord) filed a petition under Chapter 12 of the Bankruptcy Code. By order dated February 22, 1979, this Chapter 12 petition was dismissed.

By an agreement dated February 1, 1979, Citibank granted Kord an option to pay $3,750,000.00 in settlement of the mortgage debt if payment were made by July 5, 1979. However, if such option was not exercised, Citibank would obtain title to Hidden Hollow. In turn, V & V approached approximately 25 lending institutions, including Consolidated Capital Income Trust ("CCIT"), to obtain financing. On or about June 28, 1979, Mr. Vebeliunas submitted a loan application to CCIT on behalf of V & V seeking a $3,750,000.00 loan. On July 2, 1979, CCIT issued its loan commitment letter to V & V, and the transaction closed on July 5, 1979. The CCIT loan was originally due for payment on July 4, 1980. However, the payment date was extended to July 4, 1981 and, again, to July 4, 1982.

In June 1981, V & V instituted an action against CCIT in the United States District Court in the Southern District of New York seeking a declaration that the CCIT loan was usurious and an injunction against collection thereof. However, CCIT filed a counterclaim and the action resulted in a judgment of foreclosure in favor of CCIT. V & V appealed this judgment, which was ultimately affirmed by the Second Circuit Court of Appeals in or about June 1983. To prevent foreclosure, in or about June 1983, V & V filed a petition under Chapter 11 of the Bankruptcy Code.

From 1979 to 1981, V & V incurred costs of $447,245.00 in obtaining the CCIT financing and, in connection therewith, in protecting its title in the property, consisting of the following amounts:

(a) $112,500.00; fee to CCIT;
(b) $18,350.00; attorneys' fees to Weil, Gotshal, et al.;
(c) $7,500.00; attorneys' fees to Valdas Duoba;
(d) $7,423.00; title insurance and recording fees;
(e) $50.00; title closer's fee;
(f) $5,172.00; fees to Citibank;
(g) $20,000.00; mortgage broker commitment;
(h) $112,500.00; extension fee (3 points) to CCIT as noted;
(i) $161,250.00; second extension fee (4 points) to CCIT as described; and
(j) $2,500.00; appraisal fee in connection with refinancing.

The Division of Taxation does not deny that such costs were incurred; the Division however denies that such expenses are allowable costs in determining original purchase price.

From about 1981 to 1983, V & V incurred $150,346.00 in costs to protect its title to Hidden Hollow against foreclosure consisting of the following amounts:

(a) $30,831.00 in legal fees to Anderson, Russell, Kill & Olick for representation against CCIT;
(b) $114,515.00 in legal fees to Alan Rubin for representation against CCIT and to prevent additional brokerage fees; and
(c) $5,000.00 in legal fees to Angel and Frankel in connection with the Chapter 11 filing.

As above, the Division does not contest that these costs were incurred; rather, the Division denies that such costs are allowable in computing original purchase price.

Capital Improvements - Condominium Conversion Costs

In 1982 and 1983, V & V also incurred costs of $50,000.00 in converting Hidden Hollow into condominiums, which costs consisted of the following amounts: (a) $10,000.00, State of New York condominium filing fee; and (b) $40,000.00 in legal fees. The Division admits that the $10,000.00 cost was incurred but denies the $40,000.00 cost as unsubstantiated.

The sum of the foregoing amounts described in Findings of Fact "13" through "26" leaves V & V's claimed original purchase price for Hidden Hollow as $8,036,907.00.

V & V to Petrocelli Transaction

The transfer at issue herein, i.e., Lucio Petrocelli's acquisition of an interest in V & V, was undertaken to save the project from foreclosure by CCIT. In this transaction V & V, with the assistance of Carl Turner Associates, sought and found a new general partner to infuse additional capital into the project and also to assist in obtaining refinancing for the debt then held by and owed to CCIT.

On June 20, 1983, V & V and Lucio Petrocelli executed an agreement to purchase, and subsequently executed an amendment thereto, under which the stated "purchase price" to be paid by Petrocelli for his interest in V & V was $7,500,000.00 plus an additional 10% of sales amount, described as follows:

> (a) $250,000.00 deposit;
> (b) $5,000.00 broker's fee;
> (c) $5,245,000.00 to be paid upon execution of an amendment to V & V's limited partnership agreement (recognizing Petrocelli's admission to the partnership);
> (d) $2,000,000.00 "purchase money mortgage" in favor of Litas; and
> (e) additional consideration to Litas equal to 10% of the gross consideration received in connection with the sale or transfer of the premises or of the individual units as condominiums.

The June 20, 1983 agreement, as amended (see Exhibit "18") further stated that "[V & V] acknowledges that this amendment provides for the complete equity sale of the limited partnership assets...."

In a letter dated May 31, 1984 (Exhibit "6 [27]") summarizing some of the events surrounding the CCIT problems, Mr. Vebeliunas relates the following:

> "Finally, on the last hour, a deal was consummated with a certain Louis [sic] Petrocelli, who bought the project for $7 million in mortgages, plus 10% participation on net sales from the condo units."

Exhibit 64, by which the amount of "kicker" consideration was admitted and agreed, by stipulation, to be $1,125,000.00, provides at paragraph 3-a as follows:

> "Litas and V & V agree to exchange General Releases as to any and all claims arising from the sale by Litas of its interest in V & V to Lucio Petrocelli on July 28, 1983." (Emphasis added.)

Under the terms of the June 20, 1983 purchase agreement, as amended, Mr. Petrocelli was described as the sole general partner entitled to receive 75% of V & V's net profits, and

Litas was described as the sole limited partner entitled to receive the remaining 25% of V & V's net profits. A July 28, 1983 amendment to the limited partnership agreement provides that Mr. Petrocelli shall infuse $7,500,000.00, with the limited partner (Litas) to make no additional capital contribution.

V & V and Mr. Petrocelli intended that V & V's new first mortgage obtained to refinance the CCIT loan would be paid out of the sales of the first 140 condominium units at Hidden Hollow. Under the Petrocelli agreement, Litas (through V & V) would be paid out of unit sales to the extent of the $2,000,000.00 first mortgage and, in addition, would receive up to a maximum of 10% of the gross sales proceeds. As phrased, if the project was successful and over 140 units were sold, the agreement provided for payment in the form of $15,000.00 to Litas for each condominium sold over the first 140 units, up to a maximum of $2,000,000.00, with an additional $12,500.00 per unit for each condominium unit sold over the first 140 units up to a maximum of 10% of the gross sales proceeds. The parties have stipulated that, pursuant to the agreement, Litas received a total of $3,125,000.00 in additional payments. This amount was comprised of the $2,000,000.00 stream of payments (for the mortgage) with the $1,125,000.00 balance representing 10% of the gross sales proceeds on the condominium units. These payments were received upon condominium sales at Hidden Hollow as follows:

Date	$2,000,000 Payments	$1,125,000 Payments (10% "Kicker Portion")
3/23/84	$ 30,000	$ 32,142.86
3/31/84	60,000	64,285.72
4/3/84	30,000	32,142.86
4/9/84	210,000	225,000.00
4/14/84	150,000	160,714.30
4/19/84	210,000	225,000.02
4/27/84	45,000	48,214.29
4/28/84	75,000	80,357.15
5/5/84	60,000	64,285.72
5/19/84	120,000	128,571.44
5/19/84	30,000	32,142.86
5/20/84	30,000	32,142.86
5/29/84	15,000	--
6/27/84	300,000	--
7/25/84	255,000	--
After 7/25/84	380,000	--

Total	~~$2,000,000~~	~~$1,125,000.08~~

In 1982, V & V engaged Carl Turner Associates to act as a broker in obtaining refinancing for the CCIT loan. V & V paid a brokerage fee of $95,000.00 for Carl Turner Associates' services in locating Mr. Petrocelli in connection with the infusion of additional capital in V & V and refinancing of the CCIT loan as described hereinabove.

In July 1981, one George R. Basciani, M.A.I., of the Albert Appraisal Company, Inc., prepared an appraisal report of Hidden Hollow for V & V. According to this report, the 1979 fair market value of Hidden Hollow was $4,800,000.00; the 1981 fair market value was $5,150,000.00; and the 1983 fair market value was $7,000,000.00 to $8,000,000.00.

Petitioner submitted proposed Findings of Fact numbered "1" through "67". Proposed findings "1" through "13", "16" through "18", "24", "25", "27", "28", "30", "38" through "49", "51" through "55", "59", "60", and "62" through "64" have been incorporated herein; proposed findings "14", "15", "19", "20", "22", "23" and "65" through "67" have been modified to more accurately reflect the evidence; proposed findings "21", "29", "31" through "33", "56" and "61" are rejected as not accurate or fully supported by the evidence; proposed findings "34" through "37" are rejected insofar as they conclude all amounts stated therein constitute capital improvement/construction costs; and proposed findings "26", "50", "57" and "58" are rejected as being conclusory to the central issues presented for determination herein.

CONCLUSIONS OF LAW

A. In this case, it is undisputed that an acquisition of a controlling interest in V & V occurred and that such acquisition constitutes a taxable transfer (see Tax Law § 1440[2][ii]; [7]). However, petitioner argues that here the acquisition results in no gain, and hence no tax due, because petitioner's original purchase price ("OPP") for the premises exceeded the consideration received by petitioner upon transfer of the interest in question. Thus, resolution may be had by the process of determining the amounts of consideration and OPP involved.

B. There is some question in fact as to the percentage interest in Hidden Hollow actually acquired by Lucio Petrocelli. While the parties have phrased the matter as an acquisition of a

75% interest, certain of the documents would support the view that, in fact, a 100% interest was acquired, with the described 25% interest held by Litas serving merely as a means of securing its right to a payout. In fact, the V & V/Petrocelli agreement, as amended, speaks of "a complete equity sale", leaving Litas no entitlement to anything once paid (through V & V) pursuant to the terms of such agreement. In any event, such determination of the actual percentage interest acquired is unnecessary, for the parties' agreement specifically calls for Lucio Petrocelli to pay to V & V the agreed sum of $7,495,000.00 plus 10% of gross sales (the "kicker") for the interest acquired by Mr. Petrocelli. Since the agreement calls for such payment to V & V and since the parties have stipulated that the "kicker" consideration totalled $1,125,000.00, it seems beyond dispute that Lucio Petrocelli paid V & V $8,620,000.00 in order to acquire his interest in V & V. The exact amount of such interest acquired is largely irrelevant as are the reasons for the structuring of the payment therefor in the manner described. While Mr. Petrocelli bought out Litas' interest, he did so at the V & V partnership level, as phrased in the agreements, thus reflecting his true cost as well as the consideration received by V & V to be $8,620,000.00. The argument that consideration should be 75% of such amount, apparently premised upon the position that Mr. Petrocelli only acquired a 75% interest in V & V, ignores the reality of what in fact was paid by Mr. Petrocelli and the words of the agreements by which it was paid. In fact, the complete equity sale spoken of occurred, with Lucio Petrocelli paying, in total, $8,620,000.00 at the partnership level; hence, consideration received by V & V is determined to be $8,620,000.00.

C. Petitioner paid Carl Turner Associates $95,000.00 for services rendered as the broker in the transfer of the subject interest to Mr. Petrocelli (see Finding of Fact "33"). The Division disallowed such amount upon the allegation that such expense was not an allowable cost in determining OPP. However, Article 31-B defines "consideration" as "the price paid or required to be paid for real property or any interest therein, less any customary brokerage fees related to the transfer if paid by the transferor..." (Tax Law § 1440.1[a] [emphasis added]). Accordingly, petitioner is entitled to reduce consideration received by such $95,000.00 amount, leaving

consideration received on the subject transfer to be $8,525,000.00.

D. The more cumbersome question is the determination of V & V's OPP for the premises, with respect to which petitioner must not only substantiate the amounts claimed but also must show that such amounts arise from items properly includable in OPP (Tax Law § 1440.5). Petitioner categorized its claimed total OPP of $8,036,907.00 into four cost categories, to wit:

(1) acquisition costs through Kord ($6,071,123.98);
(2) capital improvements:
    (a) direct costs ($694,806.00); and
    (b) additional construction period costs ($618,386.00);
(3) costs of refinancing and protecting title ($602,591.00); and
(4) condominium conversions costs ($50,000.00).

E. Treating the last item (condominium conversion costs) first, it has been held that such costs were not properly includable in OPP prior to statutory changes to Article 31-B which were enacted in the latter part of 1984. More specifically, Tax Law § 1440.5, as in effect on the July 1984 date of the transfer in question, provided, in part, as follows:

> "'Original purchase price' means the consideration (i) paid by the transferor to acquire the interest in the real property or (ii) in the case of property acquired through gift or inheritance, the consideration paid by the last transferor who paid consideration to acquire the interest in the real property; plus in both cases the consideration by the transferor for any capital improvements made to such real property (including in the case of clause (ii) above, those by the last transferor who paid consideration) prior to the date of transfer."

F. Tax Law § 1440.5 as above was repealed by Laws of 1984 (ch 900, § 3), with new subdivision 5 added in its place and providing, in relevant part, as follows:

> "(a) 'Original purchase price' means the consideration paid or required to be paid by the transferor; (i) to acquire the interest in real property, and (ii) for any capital improvements made or required to be made to such real property, including solely those costs which are customary, reasonable, and necessary, as determined under rules and regulations prescribed by the tax commission, incurred for the construction of such improvements. Original purchase price shall also include the amounts paid by the transferor for any customary, reasonable and necessary legal, engineering and architectural fees incurred to sell the property and those customary, reasonable and necessary expenses incurred to create ownership interests in the property in cooperative or condominium form, as such fees and expenses are determined under rules and regulations prescribed by the tax commission." (Emphasis added.)

G. As the above-quoted sections reveal, it was the amendment to subdivision 5 of Tax

Law § 1440 by which the meaning of original purchase price was expanded to allow inclusion therein of customary, reasonable and necessary expenses relating to:

(a) the construction of capital improvements;
(b) legal, architectural and engineering fees incurred to sell the property; and
(c) expenses incurred to create ownership interests in cooperative or condominium form.

This new subdivision 5 was made effective as of September 4, 1984 and was not, unlike certain other portions of Laws of 1984 (ch 900), made retroactive to prior periods. It is presumed that the Legislature acts with a purpose, and here that purpose was to allow, inter alia, such costs to be included as part of the original purchase price. As the memorandum accompanying passage of chapter 900 indicates, the change to allow, inter alia, such costs was a non-retroactive substantive change (1984 McKinney's Session Laws of NY, at 3458, 3461; see, Matter of Sea Crest Motel, Inc., State Tax Commission, June 9, 1987). The expenses of converting to condominium ownership were incurred in 1982 and 1983, and the transfer in question occurred in July 1984, both being prior to the above-described amendment. Thus the conversion expenses were not properly includible as part of petitioner's original purchase price.

H. Turning next to costs of refinancing and protecting title, there is no statutory or other entitlement to include such items in OPP, and petitioner has not provided any authority to support its claim that such costs are includable. Simply put, refinancing costs, including associated legal fees, extension fees and fees to protect title or interest in the premises, have not been shown here to constitute costs incurred to acquire the interest or to sell the interest. Hence, such claimed costs are disallowed (Tax Law § 1440.5).

I. With respect to claimed capital improvements and associated costs (as specified in Findings of Fact "16" through "19"), the Division allowed some $17,830.00 in direct capital improvement costs per receipts submitted, plus $195,000.00 for the construction of the waste treatment facility. However, the Division disallowed the balance of such claimed direct costs as either not traceable, not substantiated, or not allowable as part of OPP. Further, the Division disallowed all claimed construction period costs. A review of the evidence, such as it is, leaves such disallowances as proper. First, the costs associated with construction of the treatment

facility were not allowable prior to the statutory amendment as described hereinabove. In addition, petitioner falls short of clearly establishing that a "construction period" was ongoing (see, Matter of 15 East 81st Associates, State Tax Commission, April 15, 1986). Specifically, both the testimony of Mr. Vebeliunas as well as the architect's report (see Finding of Fact "15") describe steps to be taken which appear largely to constitute repairs or remedial steps rather than construction. Although the aggregate dollar amount expended over the three years (1976-1978) was not small, this factor does not mandate a conclusion that all such expense was for capital improvements. There is no clear evidence of major structural work ongoing, and in fact, the architect's report indicates that at least 14 out of 18 of the buildings had received certificates of occupancy prior to petitioner's involvement in the project, thus militating against a conclusion that a construction period was ongoing. The tenor of such report also contradicts Mr. Vebeliunas' estimate that the project was only 60% constructed. Finally, Citibank's monitoring of expenditures does not make the same capital improvements or establish that a construction period was ongoing. In fact, payroll expenses, per financial statements, appear low in light of the claim that 10 to 20 construction workers were employed. In sum, the evidence simply does not clearly support petitioner's claim that a construction period was ongoing nor, while it is certainly possible that capital improvements costs in excess of those allowed by the Division were in fact incurred, does the state of the evidence enable a conclusion that additional costs should be allowed. Even if it were assumed that petitioner is entitled to a greater amount than was allowed by the Division, the lack of clear explanations to accompany the documents submitted en mass leaves petitioner's proof level short of the requisite. The evidence leans more to supporting a conclusion that most of the claimed capital improvements represent ongoing costs of repairs and maintenance as well as cosmetic improvements aimed at attracting tenants to occupy the units and fill the rent roll.

J. The last, and most difficult, of the cost components involves V & V's acquisition costs through Kord. The state of facts, including a description of the changes of ownership and evolving partnership relationships is, at best, left less than crystal clear by the evidence as

presented. As costs (OPP) of acquisition through Kord, petitioner claimed the following:

PETITIONER'S COMPUTATION OF ORIGINAL PURCHASE PRICE
PAID BY V & V TO ACQUIRE HIDDEN HOLLOW THROUGH KORD

(a) 38 investment units in V & V valued at $10,000 each	$ 380,000
(b) Citibank Construction Loans assumed by V & V	$4,800,000
(c) Citibank truck loan assumed by V & V	$ 5,477
(d) County Trust Co. loan repaid by V & V	$ 55,000
(e) Accounts payable to building contractors repaid by V & V	$ 40,700
(f) Tenants' rent security repaid by V & V	$ 21,254
(g) Citibank short-term loan assumed by V & V	$ 30,000
(h) Accrued interest, as of April 1, 1976, on the Citibank Construction Loans assumed by V & V	$ 348,693
(i) Additional accrued interest on the Citibank Construction Loans assumed by V & V	$ 135,000
(j) Real estate taxes repaid by V & V	$ 94,000
(k) Loans owed by Charles Dinolfo and John Reventas to Litas satisfied by V & V	$ 40,000
(l) Payment by V & V to purchase James O'Hara's interest	$ 40,000
(m) Payments by V & V to Charles Dinolfo and John Reventas	$ 75,000
(n) Loan owed by John Reventas forgiven by V & V	$ 6,000
TOTAL	$6,071,124

By this list, it may be noted that petitioner's claimed acquisition costs fall into two categories, to wit, Kord Company partnership debts claimed to have been assumed (items "b" through "j") and amounts paid to acquire the partnership interests held by Kord's partners (items "a" and "k through n"). In turn, the Division allowed items "b" ($4,800,000.00), "i" ($135,000.00), and "j" ($94,000.00) in total, and also a portion of item "l" ($34,560.00 allowed out of $40,000.00 claimed by petitioner). The remainder of the claimed items, "a", "c", "d", "e", "f", "g", "h", "k", "m" and "n", remain at issue, as does the disallowed portion of item "l".

K. Careful review of the exhibits submitted as compared to both the costs (OPP) claimed by petitioner and those allowed by the Division results in certain necessary adjustments as follows:

Item	Conclusion
"a"..... ($380,000.00)	The December 26, 1975 agreement, by which V & V was to acquire 49% of Kord in exchange for issuing 38 investment units in V & V valued at $10,000.00 each (see Exhibit "5"), was modified by the May 21, 1976 agreement. Under the modified agreement, V & V acquired 50% of Kord in exchange for $225,000.00 cash, satisfying $40,000.00 in loans owed to Litas by

	C. Dinolfo and J. Reventas and by assuming those liabilities owed directly to Citibank with any other outstanding liabilities to be paid out of operating cash flow (see Exhibit "22"). Hence, the claim to include the 38 investment units at $10,000.00 each (item "a") in OPP is denied because the agreement calling for their issuance was supplanted as described. In its place, however, petitioner appears entitled to include the $265,000.00 covered by the May 21, 1976 agreement as well as certain liabilities assumed, as detailed below.
"c"..... ($5,477.00)	Although this amount represents an obligation to Citibank to be assumed per the May 21, 1976 agreement, the specification of such item as a truck loan leaves such item distinctly other than an interest in real property; hence, such claimed amount is disallowed.
"d"..... ($55,000.00)	The purpose for the County Trust loan was not specified; moreover, it was not an amount owed to Citibank and specifically assumed; hence, such amount is disallowed.
"e"..... ($40,700.00) "f"..... ($21,254.00)	These amounts were to be paid out of ongoing operating cash flow and were not assumed upon buy-in; moreover, documentation substantiating payment is lacking; hence, such amounts are disallowed.
"g"..... ($30,000.00)	As a Citibank amount directly assumed under the May 21, 1976 agreement, such amount is allowed.
"h"..... ($348,693.00)	The evidence does not clearly establish such accrued interest to have been in fact paid. Rather, the evidence suggests such amount may have been compromised or forgiven in ultimate settlement with Citibank; hence, such amount is disallowed.
"k"..... ($40,000.00) "m"..... ($75,000.00)[4]	The Division initially allowed $196,000.00 as paid to Dinolfo and Reventas (and Kleinman and Saltzman) per an agreement dated February 21, 1979 (see Exhibit "16"). However, by letter

[4]The $75,000.00 amount claimed by petitioner in Findings of Fact "10" and "11", and elsewhere described ($25,000.00 per Exhibit "20[2]" and $50,000.00 per Exhibit "16") is disallowed as described. The $25,000.00 amount does not appear to have been an acquisition cost (see Finding of Fact "10") and the $50,000.00 amount was supplanted by later agreement as described (Exhibit "17").

"n"..... ($6,000.00)	dated June 14, 1988 (see Exhibit "22"), petitioner's counsel admitted such agreement was abrogated by an agreement dated November 1, 1979 (see Exhibits "10" and "17"), and the Division disclaims its initial allowance. In turn, petitioner has only substantiated payment of $118,000.00, per Exhibits "10", "17" and "22", as opposed to the $121,000.00 claimed. Hence, the amount allowed is limited to $118,000.00.
"l"..... ($40,000.00)	The Division's allowance of $34,560.00, as substantiated by Exhibit "5[2] and [3]", omits the $10,000.00 cash amount paid upon execution of the initial O'Hara buyout agreement (see Exhibit "5[2]"). Thus, although petitioner claims only $40,000.00, the proper amount allowable appears to be $44,560.00 and such amount is allowed.

L. Based on the foregoing, petitioner's OPP for the acquisition of the premises through Kord (to the extent traceable based on the evidence) is as follows:

Item	Description	Amount
"a"	Acquisition per 5/21/76 agreement	$ 265,000.00
"b"	Citibank construction loans assumed	4,800,000.00
"g"	Citibank short-term loan assumed	30,000.00
"i"	Post 4/1/76 accrued interest	135,000.00
"j"	Real estate taxes	94,000.00
"k", "m", "n"	Dinolfo and Reventas amounts	118,000.00
"l"	O'Hara buyout amount	44,560.00
Subtotal		$5,486,560.00
	Capital improvements costs per receipts	17,830.00
	Treatment facility	195,000.00
	Total	~~$5,699,390.00~~

M. Comparing consideration of $8,525,000.00 (Conclusions of Law "B" and "C") to OPP of $5,699,390.00 (Conclusion of Law "L") leaves a gain of $2,825,610.00 and a gains tax liability of $282,561.00. Accordingly, the Division's notice of determination dated June 18, 1984 is to be (further) reduced to such amount.

N. As to the "kicker" consideration of $1,125,000.00, the same represents contingent consideration unknown in amount to petitioner until received, and not received in fact until the dates specified in Finding of Fact "32". Hence, interest on tax due for such amounts properly runs only from such dates of receipt, and the Division is directed to recalculate interest

accordingly.

O. Petitioner has not advanced grounds sufficient to warrant abatement of the penalty herein properly imposed. In this regard, it is noteworthy that while the project was financially troubled and while the transaction was complex and somewhat protracted, petitioner did not comply with the pre-transfer reporting requirements in any fashion. In fact, no return was filed and no action was taken by petitioner until the Division made initial inquiry (of petitioner) some six months after the transfer in question occurred (see Finding of Fact "1").

P. The petition of V & V Properties is granted to the extent of the reduction determined herein (see Conclusion of Law "M"), and also to the extent that interest with respect to contingent consideration is to be recalculated (see Conclusion of Law "N"), but is otherwise denied and the Notice of Determination of Real Property Transfer Gains Tax Due dated June 18, 1984, as revised in accordance herewith, is sustained.

DATED: Troy, New York

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ADMINISTRATIVE LAW JUDGE