STATE OF NEW YORK

DIVISION OF TAX APPEALS

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| In the Matter of the Petition | : | |
| of | : | |
| TROUTMAN STREET ASSOCIATES | : | DETERMINATION<br>DTA NO. 811104 |
| 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, Troutman Street Associates, c/o The Regency Group, 1035 Stewart Avenue, Garden City, New York 11530, 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.

A hearing was held before Catherine M. Bennett, Administrative Law Judge, at the offices of the Division of Tax Appeals, Riverfront Professional Tower, 500 Federal Street, Troy, New York, on June 9, 1993 at 1:15 P.M., with all briefs to be submitted by November 19, 1993. Petitioner, represented by Howard M. Koff, Esq., submitted a brief on July 26, 1993. The Division of Taxation, appearing by William F. Collins, Esq. (David C. Gannon, Esq., of counsel), filed its brief on August 5, 1993. Thereafter, no reply was filed by petitioner.

ISSUE

Whether the Division of Taxation properly aggregated the consideration from two sales of adjacent, vacant land with a third improved parcel such that the $1,000,000.00 threshold for gains tax liability was met under the theory that such were "partial or successive transfers" pursuant to a plan or agreement which otherwise would have been subject to gains tax.

FINDINGS OF FACT

Petitioner, Troutman Street Associates ("Troutman"), is a real estate investment project owned by The Regency Group ("Regency"). Regency, a privately held investment/development company specializing in the acquisition and development of income-producing properties, maintained the controlling interest (more than a 50% interest) in

Troutman, a partnership. A Regency promotional brochure introduced into evidence indicated that the property which comprised Troutman was a 115,000-square foot industrial complex in Maspeth, New York. Petitioner acquired the subject property, 1948-68 Troutman Street, on June 3, 1988 for $3,275,000.00. The conveyances which are the subject of the Division of Taxation's ("Division") proposed aggregation in this matter involve three contracts:

(a) The first contract, which Troutman entered into on October 18, 1988, involved the sale of a 5,000-square foot section of vacant land to Philip Sacco for $150,000.00. The Sacco deal closed in February 1989. This is referred to as "Unit F" on the Division's Exhibit G.

(b) The second contract entered into was between Troutman and Gilrose Trading, Inc. on April 18, 1989 for the purchase of approximately 22,500 square feet of space within the building structure at 1948-68 Troutman Street. The original contract price for such premises exceeded $1,400,000.00. According to a contract modification executed January 9, 1990, the purchase price was changed to $1,372,393.75. This sale closed in February 1990. Applicable real property gains tax was paid on this transfer. This section of the building is "Unit D" on Exhibit G.

(c) The third contract involved a sale of approximately 28,000 square feet of vacant land which was physically located between the portion of the building sold to Gilrose Trading and the small vacant parcel sold to Sacco. The contract for such land was between Troutman and Cloverdale Ridge Realty, Ltd. (later assigned to NHE Realty Co.) entered into on June 16, 1989 for a net purchase price of $832,124.00. This sale also closed in February 1990. This vacant land was designated as "Unit E" on Division's Exhibit G.

The Division's Exhibit G, referred to above consists of two documents depicting the property from which the transfers in issue were made. The first is a Proposed Tenant Subdivision map prepared by an engineering firm on December 29, 1988. Absent any detail as to measurement, the document sets forth the positioning of the units under discussion and hand-

written designations of Units A-F appear thereon (referred to in Finding of Fact "1" above).

The second document, a title survey and subdivision, is a larger version of the property map with specific measurements and notations. It was prepared by surveyors on May 19, 1989 and bears parcel designations which differ from those in the other Exhibit G document.

As previously stated, applicable real property gains tax was calculated and paid on the transfer of Unit D. The Division takes the position in this matter that the two transfers of vacant land described above should be aggregated with the sale of Unit D, resulting in additional gains tax. If the sales of Units E and F alone are aggregated, the $1,000,000.00 threshold is not met.

Petitioner provided the testimony of Susan McGuire, the director of financial management for Regency from September 1986 to May 1993. Her responsibilities included involvement in the purchase of properties, management of properties and post-acquisition follow-up. She described Regency as a long-term real estate investor/developer. Its primary goal was to create added value to property by choosing land and buildings which required renovations, or by converting property to establish a situation where it could result in long-term appreciation. She testified that the company's goal was always to look at each project as a long-term investment. During the eight years Ms. McGuire was employed by Regency, the only project that was owned by Regency in which there was a sale of a portion of property was the Troutman project. The remainder of the real estate portfolio was retained as a long-term investment. Ms. McGuire stated that the goals in place for Troutman were consistent with the traditional goals sought to be achieved by Regency as a whole. Ms. McGuire testified that she did not have any ownership interest in Regency.

A statement describing the history of Troutman was prepared by Ms. McGuire in April 1992, prior to petitioner's conciliation conference. Consistent with the hearing testimony, the background information provided that when petitioner purchased 1948-68 Troutman Street its original intent with regard to the property, which had under-market leases, was to upgrade the building and "develop a higher and better use for the property." Initially, a conversion of the front 21,000 square feet of space in the building to an outlet center was planned. In addition,

Troutman had also planned to construct an industrial building extension on the vacant land (which was eventually sold to Cloverdale). At the time of the preparation of the statement, Ms. McGuire indicated that Troutman "own[ed] an industrial building consisting of 63,165 square feet which [was] currently leased to two tenants . . . ."

Petitioner submitted the sworn affidavit of Ken Roth, the managing partner of Troutman, dated November 1, 1990, submitted to the Division in support of its claim for refund, and attached to its request for a conciliation conference. It provided the following:

> "I, Ken Roth, am the managing partner of Troutman Street Associates. The unimproved land at Troutman Street was originally purchased by Troutman Street Associates for development and expansion of the contiguous improved property.
>
> "We sold 5,000 square feet of the property to our neighbor, Philip Sacco, since it was an appendage that did not conform to a regular shaped parcel and was not required for development.
>
> "Subsequent to the sale of the 5,000 square feet, we were approached by a developer who induced us to sell him the remainder of the unimproved property rather than develop it ourselves. Accordingly, these two sales were separate and apart and not part of an overall plan of sale. Nor were such transfers pursuant to a plan or agreement to effectuate by partial or successive transfers a transfer which would otherwise be covered by Article 31B of the Tax Law."

Susan McGuire described the parcel of property that was the subject of the first transfer in issue (Unit F) as "a small piece that stuck off of the rest of the vacant land . . ." (tr., p. 20). She additionally provided the following testimony regarding this contract:

> Susan McGuire: "We were approached by Sacco because they were interested in using it and we sold off the piece of land because it would have been no use to us when we did the expansion on the building" (tr., p. 21).

With regard to the second contract (Gilrose contract for Unit D), Ms. McGuire explained that the building had been fully rented until one of the tenants vacated after the expiration of its lease. Petitioner claims to have attempted to actively market the space in order to secure another lease. However, what little interest was shown was not financially feasible. Gilrose Trading initiated discussions with petitioner regarding the space but was interested only in making a purchase of the building space, not leasing the same. Due to financial constraints petitioner was under at that time as well as the market conditions, petitioner agreed to sell off such portion of the building.

Turning to the contract representing the transfer of the large parcel of vacant land (Unit E), petitioner explained that its original intention was to expand the existing building from its original approximate 85,000 square feet to 115,000 square feet onto the vacant land. Having explored the market conditions, it was apparent to petitioner that it would not be able to lease at a rental sufficient to support the cost of construction, and petitioner had already spent a considerable amount of time attempting to pre-lease such proposed construction without success. Petitioner was approached by Cloverdale Ridge Realty and agreed to sell the 28,000 square feet. Although the contract between Troutman and Cloverdale Ridge Realty reflects a contract price of $925,000.00, revision of the same was made based on the actual square footage of the premises after it was surveyed. The gross contract price was reduced to $896,874.00, less brokerage commissions of $64,750.00, resulting in a purchase price of $832,124.00 which is the amount reflected as "consideration" on the transferor questionnaire submitted into evidence.

Petitioner seeks a refund in this matter ($20,426.00) of tax paid which is attributed to the aggregation of the two parcels of vacant land with the portion of the building sold to Gilrose Trading.

Petitioner received correspondence from the Division dated February 20, 1991 acknowledging its claim for refund in the amount of $63,901.31. The Division indicated that a refund to petitioner had been recommended in the amount of $30,224.14. However, such refund adjustment did not include any adjustment with respect to the aggregation. The Division continues to maintain the position that the two vacant parcels (Units E & F) should be aggregated with the improved parcel (Unit D).

SUMMARY OF THE PARTIES' POSITIONS

Petitioner asserts that the Division inappropriately aggregated the consideration received on the sales of the two portions of vacant land with the improved parcel. Petitioner maintains that the transfers of two separate but contiguous properties to unrelated transferees in unrelated transactions occurring at different times were not formulated to avoid or evade the gains tax,

nor were they pursuant to a plan or agreement to effectuate by partial or successive transfers a transfer which would otherwise be subject to the gains tax. Petitioner believes it has supported the same by testimony and documentary evidence.

The Division takes the position that a plan to sell the parcels existed and petitioner has failed to demonstrate that its sales of the subject parcels should not be aggregated. The basis for the Division's position is the proximity in time between the acquisition of 1948-68 Troutman Street and the time by which all three contracts were entered into. The Division further believes that its position is supported by the fact that the Regency promotional literature indicates that one method of short-term financing of its acquisitions is by the sale of certain parcels. In summary, the Division asserts that petitioner's evidence fails to carry its burden of proof.

CONCLUSIONS OF LAW

A. Tax Law § 1441 imposes a 10% tax upon gains derived from the transfer of real property located within New York State. Tax Law § 1443(1) provides for an exemption from gains tax when the consideration for the transfer is less than $1,000,000.00.

Tax Law § 1440(7) defines the "transfer of real property" as:

> "the transfer or transfers of any interest in real property by any method, including but not limited to sale, exchange, assignment, surrender, mortgage foreclosure, transfer in lieu of foreclosure, option, trust indenture, taking by eminent domain, conveyance upon liquidation or by a receiver or transfer or acquisition of a controlling interest in any entity with an interest in real property." (Emphasis added.)

Since a property owner could avoid the gains tax by subdividing and selling off portions of the property for less than $1,000,000.00 each, Article 31-B includes a provision for the aggregation of the consideration received on such multiple transfers, commonly referred to as the "aggregation clause" (see, Matter of Executive Land Corp. v. Chu, 150 AD2d 7, 545 NYS2d 354, 356, appeal dismissed 75 NY2d 946, 555 NYS2d 692). Tax Law § 1440(7), states, as pertinent here:

> "Transfer of real property shall also include partial or successive transfers, unless the transferor or transferors furnish a sworn statement that such transfers are not pursuant to an agreement or plan to effectuate by partial or successive transfers a transfer which would otherwise be included in the coverage of this article . . . ."

In interpreting section 1440(7), the regulations distinguish between transfers of contiguous parcels by one transferor to one transferee (20 NYCRR 590.42) and transfers of contiguous parcels to more than one transferee (20 NYCRR 590.43), the situation under discussion in this matter. Where the transfer is from one transferor to more than one transferee, 20 NYCRR 590.42 directs attention to 20 NYCRR 590.43, stating:

> "When the transfer is to more than one transferee, whether the amount paid for each deed transfer is added together depends on whether the transferor is subject to the aggregation clause for partial or successive transfers. (See section 590.43 of this Part.)"

20 NYCRR 590.43 provides, in part, as follows:

> "Question: How is the aggregation clause of section 1440(7) of the Tax Law . . . applied in the case of:
>
> "(a) One transferor, more than one transferee, contiguous or adjacent parcels of land?
>
> "Answer: When the sales are pursuant to a plan or agreement, the consideration for each parcel is to be aggregated in determining whether the consideration is $1 million or more.
>
> "A transferor may furnish, along with his questionnaire, a sworn statement that the sales are not pursuant to an agreement or plan to effectuate by partial or successive transfers a transfer which would otherwise be included in the coverage of article 31-B.
>
> "Whether the sales are pursuant to a plan or agreement depends on the intent of the transferor at the time of each transfer. The department will examine the transferor's intention, as manifested by his actions and the facts and circumstances surrounding the transfers, to ensure the transfers should not be aggregated."

B. Petitioner's burden in this matter is to establish that its intent at the time of its contract commitment was absent any plan or agreement to effectuate by partial transfers a transfer of the real property located at 1948-68 Troutman Street. Petitioner's witness, Susan McGuire, was intimately involved with the acquisition and management of Regency's properties during the Troutman acquisition and sales of the parcels in issue. She provided credible and unequivocal testimony that the motive behind Regency's business as a whole, and the Troutman project specifically, primarily centered around long-range investment. The company's promotional brochure describes its specialization in "acquisition and development" of commercial and industrial income-producing properties. It sets forth its goals of maximizing net operating

income and long-term appreciation, and lists several ways that it accomplishes such goals. Several of the properties in the brochure explicitly make reference to long-term development plans. In this brochure, the Troutman project appears under "Current Developments" implying it was either (or both) a new acquisition or a project that was currently under renovation, rehabilitation or construction. The description, accompanied by a picture, depicted the Troutman property as a "115,000 square foot industrial complex." If Regency had a plan for the property which included selling off the vacant land and a portion of the improved property, or if it had already done so, it is unlikely that it would promote it in a printed brochure as a complex of such proportion, and run the risk of misrepresenting a property in what could be deemed a material misrepresentation to its investors.

The Division challenges petitioner's stated "long-term" investment goals by pointing out that one of the projects in the promotional brochure (Astoria Blvd. Associates) indicates that its "cash investment was refunded within 9 months by selling off 32% of the facilities." Although petitioner's witness characterized the Astoria project as unique, the Division believes that this is indicative of a general practice of Regency to sell off portions of a project in pursuit of profitability. However, even though Astoria was approached in this manner, absent evidence of such, a like plan cannot be attributed to another project. Although Astoria represented one of the projects described in the Regency brochure, the total number of projects undertaken between 1988 and 1990 was approximately 17. Even if the eight projects described in the brochure were truly representative of the total number, which is a fair assumption, the investment tools employed by Astoria were used only 12½% (1/8) of the time. One could hardly deem such practices to be the "general rule". Thus, Ms. McGuire's characterization that the sell-off methods were unique is plausible.

The Division restates testimony by Ms. McGuire regarding Regency's philosophy that it will tolerate short-term losses to achieve its long-term investment target. However, the Division wants to hold Regency and Troutman to such overall approach without exception, and considers a change in approach a contradiction rather than a reevaluation of a given investment

project. The Division intimates that Regency's "plan" was to take "whatever steps were necessary to make a project profitable, including going into a deal with the intent to sell off portions of the property to either turn a short-term profit or fund the intended development, or both." I do not agree with this assessment of petitioner's motives. It is clear that petitioner's investment manner included absorption of short-term losses in some cases. However, it is unreasonable to assume that continued losses that may seriously affect the viability of the long-term investment would not be evaluated with a resulting decision to take some action. Initial short-term losses prolonged by stressful market conditions create a situation whereby a slightly altered investment approach is not only reasonable, but likely.

C. This is not a case like those in which aggregation was required because the transfers were part of a subdivision plan (see, e.g., Matter of Cove Hollow Farm v. State Tax Commn., 146 AD2d 49, 539 NYS2d 127; Matter of Benacquista, Polsinelli & Serafini Mgt. Corp., Tax Appeals Tribunal, February 22, 1991, confirmed 191 AD2d 80, 598 NYS2d 829) or where evidence of petitioner's activities establish the existence of a common development purpose (Executive Land Corp. v. Chu, supra). Rather, petitioner has established that its intention with regard to each of the three transfers was different. When petitioner signed the contract of sale with Mr. Sacco on October 18, 1988, it agreed to alter what it purported to be its plan for this property, i.e., to construct an industrial building extension utilizing the vacant 33,000 square feet adjacent to the existing structure. After being approached by Sacco to sell the approximate 5,000 square feet that comprised Unit F, petitioner considered whether it would be a necessary parcel to its projected building extension, decided it would not, and entered into the sale.

Prior to the execution of the contract with Gilrose Trading, Regency engaged the services of an engineering firm who prepared the Proposed Tenant Subdivision for 1948-68 Troutman Street on or about December 29, 1988. Each of the 4 segments of the building, roughly 20,000 to 23,000 square feet, are designated by letter, and preceding each letter is the word "tenant". This document is consistent with petitioner's stated goals of upgrading the property (which at its acquisition had under-market leases) and leasing the property to other industrial tenants. There

is no mention or document designation that even implies that a parcel may be sold.

When one of Troutman's leases expired and the tenant vacated, according to information provided by Susan McGuire, petitioner engaged brokers who were actively trying to rent the space. Market conditions worked against petitioner and what little leasing interest was shown was financially insufficient. Gilrose Trading was presented to petitioner, but was only interested in purchasing the space, not leasing it. Petitioner reconsidered its original intention to maintain leased industrial space and sold Unit D to Gilrose subject to its obtaining a subdivision for such purpose, a process which took about two years.

Although petitioner claims its intention for the Troutman Street property was to construct an industrial building extension to the current building on the vacant land while it upgraded the existing building, market conditions were a significant influence on petitioner's decision to abandon its original plan to extend the existing structure. Thereafter the contract with Cloverdale was entered into.

D. The Division argues that since the whole parcel was acquired in June 1988 and that by June 1989 three adjacent subdivided parcels (or parcels subject to a proposed subdivision) were under contract to be sold, a "plan" existed. This results in consideration from the two vacant parcels being aggregated with the improved parcel only because they happen to be adjacent to each other and were all sold within a relatively short period of time. This interpretation would irrefutably presume the existence of a plan whenever contiguous or adjacent properties are sold. If this is what the Legislature intended, the exception to aggregation for transfers not pursuant to an agreement or plan need not have been included in the statute (Matter of General Builders Corp., Tax Appeals Tribunal, December 24, 1992). In General Builders, the Tribunal clearly held that the determination of whether petitioner had a plan to dispose of parcels must be made at the time of the signing of the contract. Petitioner herein established by the credible testimony and written statement of a key financial figure that it had a plan, but not one that initially included the disposal of the parcels in question, but rather one which envisioned expansion and development, goals sought on a long-term basis. Petitioner had no intention of selling either

Units D or E until it had performed a review of the market conditions and of the possibilities of leasing in the case of Unit D and construction in the case of Unit E. The Division is critical that petitioner did not produce projections and other such documentation to support the analysis it claims to have performed. Certainly, given the facts, such information may have been helpful to establish petitioner's position. However, I do not find the absence of such evidence sufficiently compelling to warrant a finding that petitioner's intentions were other than it claims.

The only facts supporting aggregation are those which point to the proximity in time of the execution of the sales contracts to each other and to the acquisition of the entire property, and the very fact of the transfers. In consideration of all of the facts and circumstances presented, the evidence supports a finding that this was not a case where a taxpayer was attempting to perpetuate a tax avoidance scheme by arranging the disposal of a large parcel via several partial or successive transfers of subdivided portions (see, Matter of Cove Hollow Farm v. State Tax Commn., supra). Petitioner established that the transfers of the two vacant parcels (Units E and F) were not made pursuant to a plan or agreement and petitioner has met its burden of establishing that these transfers were in fact independent transfers from that of Unit D, and therefore, not subject to aggregation.

E. The petition of Troutman Street Associates is hereby granted.

DATED: Troy, New York
May 19, 1994

/s/ Catherine M. Bennett
ADMINISTRATIVE LAW JUDGE