STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
ZECKENDORF COLUMBUS CO.	:	DETERMINATION DTA NO. 812021
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, Zeckendorf Columbus Co., 55 East 59th Street, New York, New York 10022, 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 Jean Corigliano, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York, on June 28, 1994 at 9:15 A.M. Briefs were filed by both parties. Petitioner's reply brief was filed on November 21, 1994, which began the six-month statutory period for issuance of a determination. Petitioner appeared by Carolyn Joy Lee, Esq. and Joseph Lipari, Esq. The Division of Taxation appeared by William F. Collins, Esq. (Donna M. Gardiner, Esq., of counsel).

ISSUES

I. Whether certain interest expenses incurred by petitioner are includible in its original purchase price as consideration paid for capital improvements.

II. Whether the special additional mortgage recording tax paid by petitioner is includible in its original purchase price.

III. Whether payments of real estate transfer taxes made by individual condominium unit transferees should have been added to the consideration petitioner received for the sales of the condominium units.

IV. Whether penalties imposed may be abated or cancelled on the ground that any failure to pay the full amount of transfer gains tax was due to reasonable cause and not due to willful

neglect.

FINDINGS OF FACT

Petitioner, Zeckendorf Columbus Co., and the Division of Taxation ("Division") stipulated to certain facts which have been incorporated into these Findings of Fact.

For the most part, the facts are not in dispute and were established through stipulation, field audit reports and the testimony of Jerome Socher, who has worked for petitioner as an accountant for approximately 17 years. Mr. Socher has over 20 years of experience as an accountant working primarily in real estate development. He was involved in every financial aspect of the condominium development project which is the subject of this proceeding, and he represented petitioner at each stage of the audit of its gains tax filings.

Petitioner was a Manhattan real estate developer which was involved in a number of condominium projects. Early in 1983, petitioner began negotiations to acquire real property on the corner of 79th Street and Columbus Avenue in Manhattan with the sole intention of demolishing the existing structures and constructing a building containing commercial space and residential condominium units. The development project was known as the Park Belvedere. Petitioner wanted to move quickly on this project because it had determined that market conditions on the West Side of Manhattan were very strong at this time.

As Mr. Socher described it, the development of the Park Belvedere required an assemblage of components before petitioner could obtain financing for the project. Early in 1983, petitioner acquired a contract to purchase the land on which a new building was to be erected. With the land, petitioner acquired the right to build approximately 120,000 square feet of allowable floor area at the maximum floor-area ratio ("FAR"). From the owners of neighboring buildings, petitioner procured development rights, also known as air rights, which permitted it to build another 80,000 FAR. Petitioner's sole reason for acquiring the development rights was to gain the ability to construct a larger building than it could have constructed without such rights.

To obtain a demolition permit from New York City, petitioner had to provide proof that

the existing building was empty. Petitioner acquired the remaining leasehold terms of the commercial tenants in the building in order to obtain the demolition permit and accelerate the commencement of construction. The value petitioner acquired by buying out the tenants was the ability to commence construction without delay.

Petitioner paid $6,131,374.00 to acquire the land, $1,775,000.00 for the development rights and a total of $1,618,198.00 for the leaseholds or tenant buyouts. The portion of the costs to develop Park Belvedere attributable to the residential condominium units in the building is 91.165 percent. Thus, the costs to acquire the land, the development rights and the leaseholds, attributable to the residential condominium units, were as follows:

Land	$5,589,668.00
Development rights	1,618,179.00
Leaseholds	1,475,230.00

After acquiring the contract to purchase the real property, the development rights and the tenant buyout agreements and preparing a construction budget, petitioner went to the banks to obtain what Mr. Socher labelled "construction loans". He explained the loans as follows:

> "[B]anks wanted, especially at that time, to know they were going to get out. This was not a permanent type of financing; it was a construction loan with a period of time that they would be paid off their loan and get a one percent over prime on that or whatever interest it was." (Tr., p. 17.)

The amount of the financing needed for the project was determined by petitioner in consultation with its lenders based on the projected costs associated with the project.

Among the costs taken into consideration by both petitioner, as developer, and its lenders was the projected interest cost to carry the land and to carry the interest expenses on expenditures for the development rights and the tenant buyouts during the construction period.

The interest on the loans was considered by petitioner and the lenders to be a key cost of the building project. Mr. Socher testified that it is one of the most important costs since interest rates can vary during the course of construction making it impossible to know the actual interest expense until the project is completed. Because of this, Mr. Socher stated, completing the project as soon as possible is the key to success in developing.

According to Mr. Socher's testimony, the banks extended petitioner the money to

acquire the land, the development rights and the leaseholds on the initial day of the loan. After that, the banks would advance funds to pay construction costs and associated development expenses until the building was completed. As the units were sold, the bank loans were paid down until the entire amount was paid.

Petitioner obtained two loans to finance the Park Belvedere project--a $36,000,000.00 loan from Manufacturers Hanover and a $5,000,000.00 loan from Lincoln Savings Bank. These loans were secured by a recorded mortgage, and petitioner paid mortgage recording tax of approximately $900,000.00 upon recording of that mortgage. The mortgage recording tax paid by petitioner included a special additional mortgage recording tax in the amount of $93,471.00.

On petitioner's sales of the residential condominium units to unit purchasers, the condominium offering plan specified that the New York City transfer taxes and New York State documentary stamp taxes (also real estate transfer taxes) on the sales were to be paid by the purchaser. The relevant provisions of the offering plan state as follows:

> "(e) New York City Real Property Transfer Taxes, currently one percent (1%) of the purchase price of a Residential Unit when the purchase price is less than $500,000 and two [percent] (2%) of the purchase price of a Residential Unit when the purchase price is $500,000 or greater, will be the sole responsibility of the Purchaser. The City of New York Department of Finance has taken the position that when Purchaser assumes the obligation to pay the New York City Real Property Transfer Tax, the amount of such tax will be included in the consideration subject to tax. The steps to compute the tax are:
>
> "(1) Multiply the purchase price by the City tax rate to compute a tentative tax.
>
> "(2) Add the tentative tax to the purchase price.
>
> "(3) Multiply that sum by the City rate.
>
> "Example:
> Purchase price = $600,000
> (1) $600,000 x 2% = $12,000.00
> (2) $600,000 + $12,000 = $612,000.00
> (3) $612,000 x 2% = $12,240.00; and
>
> "(f) New York State Documentary Stamp Taxes, presently $4.00 per $1,000.00 of the Purchase Price of a Residential Unit less existing and continuing mortgages, will be the sole responsibility of the Purchaser."

It is common in sales of New York City residential condominium units pursuant to

condominium offering plans for the purchaser to pay the State and City real estate transfer taxes.

Petitioner complied with the gains tax pre-transfer audit procedure, and during the course of the pre-transfer audit made certain adjustments to its calculation of original purchase price ("OPP") as required by the Division. Specifically, petitioner was not allowed to include in OPP construction period interest attributed to land or the amount of the special additional mortgage recording tax.

Petitioner's pre-transfer audit filing disclosed that the purchasers of petitioner's condominium units were paying the New York City and State transfer taxes on such sales, but the Division did not at this time instruct petitioner to treat those payments as consideration.

Petitioner sold all of the residential condominium units sometime after May 1985. All of the revenues derived by petitioner from the residential units were derived from sales of the units, and all sales were subject to the gains tax. There were no rentals of residential units.

As the result of a field audit on the entire project after sellout, the Division issued to petitioner a Notice of Determination dated June 27, 1991 assessing real property transfer gains tax under Article 31-B of the Tax Law in the amount of $190,817.66. The Division also imposed a 35 percent penalty on the tax due and assessed interest.

On audit, the total OPP allowed by the auditor was $40,795,378.00. Regarding interest expenses disallowed by the auditor in the calculation of OPP, the parties stipulated as follows:

> "Out of the total construction period interest expense incurred by the taxpayer and disallowed by the auditor, $705,088.00 is attributable to land."
>
> "Out of the total construction period interest expense incurred by Petitioner and disallowed by the auditor, $321,015.00 is attributable to development rights."
>
> "Out of the total construction period interest expense incurred by Petitioner and disallowed by the auditor, $1,488,877.00 is attributable to the lease buyouts."

The field audit of petitioner was on the entire project. The auditor reviewed all books and records associated with the Park Belvedere conversion. Apparently, petitioner did not maintain a separate accounting of interest expenses attributable to the development rights, tenant buyouts and land treating them all as construction period interest. Since the auditor

determined that these were not includible in original purchase price, it was necessary for her to calculate the amount of each of those interest expenses (and to give petitioner credit for interest expenses attributable to the land already accounted for in the pre-transfer audit). The methodology the auditor used was somewhat complex, although it appears from Mr. Socher's testimony that he did understand the actual calculations utilized by the auditor in arriving at her determination. Since the parties have stipulated to the amounts in issue, there is no need to set forth the numerics here.

The auditor disallowed the special additional mortgage recording tax, in the amount of $93,471.00, in computing OPP.

The total consideration determined by the auditor was $61,596,299.00. The auditor included in consideration the transfer taxes paid by condominium unit purchasers. The aggregate amount of transfer taxes paid by the condominium unit purchasers was $850,442.00. This total is comprised of New York State real estate transfer tax of $242,983.00 and New York City real estate transfer tax of $607,459.00.

In computing their Federal taxable income, petitioner's partners did not take a current deduction for any portion of the construction period interest expense, but instead capitalized such expense and amortized it over the sales of condominium units or, if shorter, the 10-year amortization period prescribed in the Internal Revenue Code. This treatment was required by Federal law for the pertinent years.

Petitioner submitted in evidence a copy of "Statement of Financial Accounting Standards No. 34, Capitalization of Interest Costs" ("FASB") (Financial Accounting Standards Board, October 1979). It establishes financial standards for capitalizing interest cost as part of the historical cost of acquiring certain assets. Point 11 of the FASB states:

> "Land that is not undergoing activities necessary to get it ready for its intended use is not a qualifying asset. If activities are undertaken for the purpose of developing land for a particular use, the expenditures to acquire the land qualify for interest capitalization while those activities are in progress. The interest cost capitalized on those expenditures is a cost of acquiring the asset that results from those activities. If the resulting asset is a structure, such as a plant or a shopping center, interest capitalized on the land expenditures is part of the acquisition cost of the structure. If the resulting asset is developed land, such as land that is to be sold as developed

lots, interest capitalized on the land expenditures is part of the acquisition cost of the developed land."

Mr. Socher testified that in the pre-transfer audit filings, he allocated roughly $1,500,000.00 to interest expenses attributable to the land at the direction of the Division. He also stated that the Division was aware of the costs associated with the acquisition of development rights and other expenses and raised no questions regarding their inclusion in original purchase price at that time. Mr. Socher had no conversations during the course of the pre-transfer audit regarding the special additional mortgage recording tax and treated it as he did the mortgage recording tax. Regarding the addback of transfer taxes paid by the condominium unit purchasers, Mr. Socher testified that, in transfers involving other condominium projects in later years, he was instructed to add the amount of the transfer tax to consideration, but he was not instructed to make the addback at the time of the Park Belvedere pre-transfer audit. The auditor never provided petitioner with any written guidelines or policy statements to explain the adjustments she made to petitioner's gains tax filings.

In incurring costs to acquire land, buy out tenants and acquire development rights, and in incurring interest expenses to carry such acquisition costs during the construction period, petitioner was following a common pattern of property development in New York City.

The gains tax paid by petitioner upon the sales of the residential condominium units constituted approximately 90 percent of the gains tax the Division asserts as due.

PROPOSED FINDINGS OF FACT

Petitioner submitted 29 proposed findings of fact. The Division did not raise an objection to any of them. Proposed findings of fact "1" through "10", "13", "14", "15", "17" through "27 and "29" were adopted and substantially incorporated into the Findings of Fact above. Proposed findings of fact "11" and "12" were adopted, with some modification, as Findings of Fact "7" and "12". Petitioner refers to the bank loans it received as "construction loans" and "construction financing". Since interest on a "construction loan" is includible in OPP under 20 NYCRR former 590.16(d), referring to the loans in this manner gives the impression of pre-judging a legal issue. For that reason, petitioner's language has been

modified. Proposed finding of fact "16" has been rejected as it asks for the finding of a conclusion of law. Findings of Fact "9, "10" and "11" relate to proposed finding of fact "16" and summarize Mr. Socher's testimony without reaching an ultimate conclusion of law. Proposed finding of fact "28" was accepted with some modification to more accurately reflect the record and incorporated into Findings of Fact "20" and "25".

SUMMARY OF THE PARTIES' POSITIONS

Petitioner asserts that the interest expenses paid during the construction period, whether attributable to the acquisition of the land, the development rights or the leasehold interests, are properly includible in OPP pursuant to Tax Law § 1440(5)(former [a][ii]) and 20 NYCRR former 590.16(d) as customary, reasonable and necessary costs of construction.[1] Petitioner notes that the regulations in effect during the subject years (20 NYCRR 590.15[b] and former 590.16[b]) specifically allow mortgage recording taxes to be included in OPP and contends that the special additional mortgage recording tax should be includible in OPP under the same provision.

Petitioner alleges that by increasing consideration by the transfer taxes paid by condominium buyers the Division fails to take into account the joint and several nature of the liability for these taxes. According to petitioner, the addback of the taxes paid by the condominium unit purchasers overstates petitioner's consideration.

Petitioner claims that it acted reasonably with respect to each of the disputed issues in that petitioner's treatment of each item was supported either directly by gains tax authority or by closely-related

income tax law or accounting principles. In addition, petitioner notes that it revealed its position on each issue on the pre-transfer filings and adjusted its own calculations to conform to

[1]The gains tax regulations pertaining to the calculation of OPP were amended after the subject transfers occurred and the Notice of Determination was issued. These amendments were proposed on February 23, 1994 and became effective November 9, 1994. Neither party addressed the amended regulations.

whatever instructions it was given by the Division at that time.

The Division contends that its disallowance of the disputed interest expenses is consistent with the Tax Law and former gains tax regulations. It is the Division's position that the interest expenses in question were excluded from OPP pursuant to 20 NYCRR former 590.15(c).

The Division states that it "properly disallowed the amount of the special additional mortgage recording tax imposed upon petitioner because such tax can be taken as a credit against franchise tax and personal income tax." The Division also contends that the amendment of Tax Law § 1440(5)(former [a]) provides evidence that the original statute did not include the special additional mortgage recording tax as part of OPP.

The Division states that under Tax Law § 1404(a) it is the obligation of the grantor to pay the real estate transfer tax and, consequently, that the condominium unit purchasers assumed an obligation of the transferor when they paid the tax. The assumption of an obligation by a transferee is defined as consideration. The Division also notes that section 590.15(b) of the regulations specifically states that the payment of New York City or New York State real estate transfer taxes by the buyer is deemed to be additional consideration to the seller.

It is the Division's position that petitioner has not shown that its position with regard to any item is reasonable because petitioner has not cited any gains tax case law in support of its legal interpretations.

CONCLUSIONS OF LAW

A. Article 31-B of the Tax Law provides for the imposition of a tax at the rate of 10 percent upon gains derived from the transfer of real property within the State of New York (Tax Law § 1441). Tax Law § 1440.3 defines "gain" as:

> "the difference between the consideration for the transfer of real property and the original purchase price of such property, where the consideration exceeds the original purchase price."

Tax Law § 1440(5)(former [a]), in effect at the time of the transfers in issue, provides, in

pertinent part, as follows:

> "'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."

Tax Law § 1440 was amended by the Laws of 1993, and, as pertinent to this issue, now provides as follows:

> "Original purchase price shall also include any interest paid or required to be paid by the transferor on a loan which was used to acquire the real property; provided that such amount of interest shall be limited to the interest which accrues during a construction period, as defined in paragraph (h) of this subdivision and subject to rules and regulations prescribed by the commissioner, and which is attributable to that portion of the real property which is the subject of the construction of a capital improvement during such construction period" (Tax Law § 1440[5][a][iv], added by L 1993, ch 57, § 61).

The new provision was made applicable to taxable years beginning on or after January 1, 1993 and to transfers occurring on or after April 15, 1993 (L 1993, ch 57, § 418[8]). If the transfers in issue had occurred on or after that date, there would be no question that the construction period interest in dispute was includible in OPP. Petitioner argues that under the authority of the statute and regulations in effect at the time of the transfers these interest expenses were also includible in OPP. The Division contends that the 1993 amendment represents a change in the law and that prior to amendment of the statute interest paid on a loan to acquire real property was not includible in original purchase price as a cost of a capital improvement.

B. Tax Law § 1440(5)(former [a]) states that OPP includes "costs which are customary, reasonable, and necessary" for the construction of capital improvements. This provision does not contain any illustration or example of such costs, but rather vests in the State Tax Commission (now the Commissioner of Taxation and Finance) the power to determine, by regulation, which costs are customary, reasonable and necessary costs of construction. Given this explicit grant of power, the regulations of the Commissioner of Taxation and Finance ("Commissioner") are entitled to great deference (see, Matter of Mattone v. Dept. of Taxation &

Fin., 144 AD2d 150, 534 NYS2d 478). Under this grant of authority, the Division promulgated regulations (20 NYCRR former 590.16) which provide guidance in determining which costs associated with the construction of a capital improvement may be included in OPP. 20 NYCRR former 590.16 (b) sets forth an illustrative list of items includible in OPP, none of which are mentioned in the statute. In addition to these specific costs, 20 NYCRR former 590.16(d) provides that certain additional costs may be allowed if incurred during a construction period. 20 NYCRR former 590.16(d) provides, in pertinent part, as follows:

> "Other costs that are clearly associated with construction of a real estate project can also be included as a cost of constructing a capital improvement. If the capital improvement requires a construction period, a period of time in which necessary activities are conducted to bring the improvement on the real property to that state or condition necessary for its intended use, the interest cost paid during that period on a construction loan, real property taxes, insurance or similar items are includible as a cost of construction. Amounts designated as points or loan processing fees on a construction loan also are includible in original purchase price so long as the fees were paid by the borrower for the receipt of the loan funds and were not paid for specific services.
>
> "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:
>
> -- accounting fees
> -- fees for appraisals required by construction lender
> -- interest paid during the construction period on loans where the proceeds of such loans were used to make capital improvements to real property
> -- construction period real property taxes
> -- mortgage recording tax (building and loan mortgage only)
> -- construction period insurance
> -- construction period security" (emphasis added).

The essence of petitioner's position is that interest attributable to land acquisition, when accrued during a construction period, is sufficiently like interest paid on a construction loan, real property taxes and insurance to warrant treating them as "similar items" under the authority of the former regulation. Petitioner offers a number of reasons for doing so.

First, petitioner characterizes the full amount of the loans as "construction loans" based primarily on Mr. Socher's testimony. Accepting this characterization would settle the issue since interest on construction loans is clearly a cost includible in OPP under the regulation. I cannot accept that characterization at face value. Even if petitioner and its lenders saw the loans

as short-term financing, portions of the loan funds were intended to be used, and were used, to acquire the land, the development rights and the leasehold buyouts. The interest expense attributable to these acquisitions can be determined as demonstrated by the stipulation. Thus, the entire amount of each loan was not for the construction of a capital improvement. However, the nature of the loan agreements as described by Mr. Socher (testimony that was not challenged by the Division) lends weight to petitioner's contention that some of the interest from those loans was clearly associated with the cost of construction. The loans were made with the understanding that land and other property rights would be acquired for the purpose of construction. The loans were part of a total package: petitioner did not first purchase land and then seek financing to construct a capital improvement or seek separate financing for the land and the construction. The cost of borrowing, including interest expenses associated with the acquisition of real property, was taken into consideration by petitioner and its lenders in creating a construction budget. In sum, the overall nature of the loans and Mr. Socher's testimony establish that petitioner and its lenders considered the interest expense from these loans to be customary, reasonable and necessary costs of construction. The Division presented neither evidence nor legal argument to explain why the interest expenses should not be categorized as costs which are "customary, reasonable, and necessary" as those terms are used in Tax Law § 1440(5)(former [a]).

Petitioner also argues that the exclusion from OPP of construction period interest on land is inconsistent with the treatment of such costs under other disciplines. Treatment of construction period interest in contexts other than gains tax is not dispositive of the gains tax issue (Matter of V & V Properties, Tax Appeals Tribunal, July 16, 1992; Matter of SKS Assoc., Tax Appeals Tribunal, January 12, 1991). I will note, however, that petitioner's individual partners capitalized all of the construction period interest for the years 1984, 1985 and 1986, including interest on funds used to acquire real property. Their treatment of the interest expense was consistent with Federal law (IRC § 189[e][1], as in effect prior to 1986; IRC § 263A). Also, FASB 34, in articulating the rules that account for the total cost of real property

construction, provides for a developer to treat as part of such cost the costs incurred to carry the land while it is under construction. These facts demonstrate that petitioner's construction of 20 NYCRR former 590.16(d) is reasonable when set in the context of other disciplines which treat the same items.

Petitioner also argues that the Division's exclusion of construction period interest on land is inconsistent with its treatment of other construction period costs relating to land. According to petitioner, there is no rational basis for distinguishing between construction period acquisition interest and construction period taxes, inasmuch as both are a cost of carrying the land in an unproductive state during the period of construction. The Division did not address this argument.

As petitioner points out, 20 NYCRR former 590.16(d) does not exclude interest expenses on a loan used to acquire real property from construction period OPP, while 20 NYCRR 590.15(c) explicitly excludes such expenses from the calculation of consideration to acquire real property. Furthermore, 20 NYCRR former 590.16(d) includes in construction costs such "soft" costs as construction loan interest, property taxes, insurance and "similar items" if incurred during a period of construction. Petitioner contends that there is no rational basis for excluding acquisition loan interest from construction costs while including other soft costs like real property taxes. Petitioner explains its position as follows:

> "[I]nterest is a periodic cost incurred to own or 'carry' property. Interest on land is like property taxes on land -- it is a cost one bears as the day-to-day price of owning real property and earning a return from the property. And Regulation §590.16 tells us that when such periodic costs of ownership are incurred during a construction period, such that the 'return' that will compensate the owner for her economic outlay is expected to be realized from the constructed asset, then those periodic costs of ownership are included in OPP as a construction cost. Interest costs incurred during the construction period -- whether attributable to the cost of acquiring the land, the development rights, the tenants' remaining lease terms, the concrete, the steel, the nails or the light fixtures -- are a cost of construction and should properly be reflected in the OPP of the constructed asset" (Petitioner's Reply Brief, pp. 5-6).

C. Petitioner's construction of 20 NYCRR former 590.16(d) is both reasonable and persuasive. In contrast, the Division gave no reason why acquisition loan interest should not be treated as an item similar to construction loan interest, property taxes or insurance for purposes

of determining the capital improvement calculation of OPP. Instead, the Division relies on the following arguments: (1) the Division takes the position that interest paid on a loan used to acquire real property is barred from inclusion in OPP (either as an acquisition cost or a construction cost) by 20 NYCRR 590.15(former [c]); (2) the Division contends that this interpretation of the regulation was adopted by the Tax Appeals Tribunal in Matter of British Am. Dev. Corp. (Tax Appeals Tribunal, January 6, 1994); and (3) the Division argues that the amendment of Tax Law § 1440(5)(former [a]) supports its contention that "prior to such amendment, interest on a loan used to acquire real property was not an allowable cost within the meaning of former Tax Law §1440(5)(a)" (Division's brief, p.8). I will consider each of these arguments next.

I will first address the Division's contention that interest paid on a loan used to acquire real property is barred from inclusion in OPP by 20 NYCRR 590.15(former [c]), in effect at the time of issuance of the notice of determination. As relevant, it provides that "[i]nterest paid on a loan where the proceeds of such loan were used to acquire the real property or interest therein" is "not allowable as a cost to acquire real property for purposes of determining original purchase" (emphasis added).

There is no question that loan proceeds were used to acquire real property including the land, development rights and leasehold interests; however, it does not follow that interest expenses incurred to service those loans were likewise a cost of acquisition. As petitioner points out, that is precisely what regulation 590.15 former (c) says--interest expenses incurred on a loan used to acquire real property are not allowable as acquisition costs because they are a cost of carrying the property, not a cost of acquiring it. Since the disputed interest expenses were not costs of acquisition, they were not includible in OPP as "consideration paid . . . to acquire the interest in real property" (Tax Law § 1440[5][former (a)(i)]). However, 20 NYCRR 590.15(former [c]) does not exclude interest expense attributable to land acquisition from being included in OPP as a cost of construction; it does not address the capital improvement element of OPP at all. Therefore, 20 NYCRR 590.15(former [c]) cannot be the basis for determining

whether interest associated with real property acquisition may be included in OPP as a "customary, reasonable, and necessary" cost of constructing capital improvements (Tax Law § 1440[5][former (a)(ii)]).

Next, it must be determined whether the decision of the Tax Appeals Tribunal in Matter of British Am. Dev. Corp. (supra) settled the issue raised by petitioner here.

The taxpayer in British American was the developer of a residential subdivision plan which eventually resulted in the sale of at least 18 lots for a gross consideration of over $1,000,000.00. The taxpayer failed to make any gains tax filings even after being requested to do so by the Division. The Division determined the taxpayer's gains tax liability based on information available; in doing so, the Division determined an original purchase price of zero. The Tax Appeals Tribunal, affirming the determination of an Administrative Law Judge, found that the taxpayer failed to prove that it had paid any amount to acquire the land. As a consequence, the Tribunal upheld the Division's determination that land acquisition costs were zero. In addition, the Tribunal found that deeds to the real property were recorded on January 2, 1981. A mortgage of $1,100,000.00 to develop the property was obtained and recorded on September 18, 1981, after the property was acquired. The taxpayer claimed construction period interest expenses of $684,356.00. The cost of the capital improvements was $789,675.00. Following a conciliation conference, the Division allowed an interest expense of 20 percent of the amount claimed, reasoning that the interest expense was so out of proportion to the actual capital improvements that interest must have accrued on loans where only a part of the proceeds was used to make the capital improvements. These facts are recited, in part, to demonstrate how sparse and confusing the factual record in British American was. Moreover, the petitioner waived a closing statement in front of the Administrative Law Judge and did not file a brief at the Administrative Law Judge level or on exception to the Tax Appeals Tribunal.

Conclusion of Law "H" of the Administrative Law Judge's determination in Matter of British Am. Dev. Corp. (February 18, 1993) states:

> "Petitioner has also failed to sustain its burden of proof to show that it is entitled to additional interest paid on funds borrowed for the construction of capital

> improvements. Petitioner's schedule of 'Capitalized Costs' is patently erroneous with respect to the reconstructed interest calculations. First of all, the schedule allocates interest for land acquisition costs, which interest is not allowable under 20 NYCRR 590.15(c); secondly, it allocates interest to the period prior to the date of the mortgage. The mortgage was dated September 18, 1981, but interest is shown accruing as early as January 1980. There is no evidence in the record that there was a loan prior to the date of the mortgage. Comparison of the aforementioned schedule with petitioner's cancelled checks for the period at issue seems to confirm the payment of the development costs stated in the schedule; however, because of the foregoing errors it is virtually impossible to determine whether petitioner is entitled to more interest than was allowed by the conferee."

In sustaining the Administrative Law Judge's determination for the reasons stated in that determination, the Tax Appeals Tribunal stated:

> "First, the Administrative Law Judge found that the schedule included interest paid for land acquisition costs which is not a cost allowable in computing original purchase price (see, 20 NYCRR 590.15[c])" (Matter of British Am. Development Corp., Tax Appeals Tribunal, January 6, 1994).

It would be wrong to read this statement broadly, as the Division does, to mean that interest paid for land acquisition costs are not allowable in computing original purchase price under either the acquisition provision (Tax Law § 1440[5][former (a)(i)]) or the capital improvement provision of (Tax Law § 1440[5][former (a)(ii)]) of the gains tax law. First, the reference in the Tribunal's decision to 20 NYCRR 590.15(c) (the acquisition costs regulation) indicates that the Tribunal did not fully consider the issue of construction period interest expenses as raised by petitioner in this proceeding. Second, Conclusion of Law "H" and the Tribunal's statement regarding that Conclusion of Law indicate that the petitioner's schedule of "Capitalized Costs" included interest paid for land acquisition costs before the start of the construction period. It cannot be determined from these statements whether petitioner claimed that the interest was a cost of construction. Finally, it does not appear from a full review of the Administrative Law Judge determination or the Tribunal decision that the interpretation of Tax Law § 1440(5)(former [a][ii]) regarding construction period interest on land acquisition costs was before the Tribunal. Accordingly, the Tribunal's decision in Matter of British Am. Development Corp. (supra) is not dispositive of the issue raised here.

Finally, I will address the Division's argument concerning the effect of the amendment of Tax Law § 1440(5)(former [a]) by the Laws of 1993. The Division notes that the enabling

legislation states that the amended statute is applicable to transfers occurring on or after April 15, 1993 (L 1993, ch 57, § 418[8]). It then argues as follows:

> "Where the amendment sets forth a specific effective date in the future, it is an indication against retroactive application (Silverman v. State of New York, [48 AD2d 413, 370 NYS2d 234]). Accordingly, since the amended statute is more expansive and since the statute directly states that it applies only to transfers occurring on or after April 15, 1993, petitioner is not entitled to retroactive application of the statute. Thus, the Division correctly disallowed such interest costs from the calculation of original purchase price" (Division's brief, p. 9).

In response, petitioner contends that it is not requesting a retroactive application of the amended statute. It states its position as follows:

> "The 1993 amendments do not tell us what the law was before April 15, 1993; and . . . the fact that these amendments were enacted does not mean that the items covered were not previously included in OPP. Petitioner simply asks the Court to decide this issue by reference to the law in effect at the time of the transfers, and without drawing inferences from later enactments."

Generally, it is assumed that an amendment to a statute was made to effect some purpose or to make some change in the existing law (McKinney's Cons Laws of NY, Book 1, Statutes § 191). In this instance, however, I do not believe that the amendment brought about the change the Division perceives.

The subject transfers occurred before the Notice of Determination was issued to petitioner on June 27, 1991; therefore, the law applicable to this matter is Tax Law § 1440(5)(former [a]), the law in effect at the time the notice was issued. That statutory provision explicitly vests in the Commissioner the power to determine which costs are "customary, reasonable, and necessary" for the construction of capital improvements. Chapter 57 of the Laws of 1993 amended the definition of original purchase price by explicitly including within it (1) "any customary, reasonable and necessary advertising and marketing costs not included in customary brokerage fees paid by the transferor incurred to sell the property" (Tax Law § 1440[5][a][ii]); (2) "any tax paid by the transferor to record a mortgage" (Tax Law § 1440[5][a][iii]); and interest paid on a loan to acquire real property provided that the amount of interest shall be limited to the interest which accrues during a construction period (Tax Law § 1440[5][a][iv]). It cannot be emphasized too strongly that prior to its amendment section 1440(5)(former [a])

neither included nor excluded any of these costs from OPP; rather it was left to the Commissioner to determine by regulation which costs were to be considered "customary, reasonable and necessary". By amending the statute, the Legislature effectively restrained the discretion of the Commissioner by requiring the inclusion of certain items in OPP. It did not add as allowable items of OPP items previously excluded by statute. Therefore, in order to determine whether a particular item was allowed prior to the amendment of the statute, it is necessary to look to the Commissioner's regulations. In at least one case, it is very clear that the statute merely codified and clarified an existing regulation. That is the provision applying to the mortgage recording tax.

The Laws of 1993 added the following provision to Tax Law § 1440(5)(former [a]):

> "(iii) Original purchase price shall also include any tax paid by the transferor to record a mortgage: (A) securing a debt incurred by the transferor to acquire the real property, (B) securing a debt incurred by the transferor to construct a capital improvement on such property, or (C) created as a result of the conveyance of title to a cooperative housing corporation" (L 1993, c 57, § 61).

Thus, the amended statute explicitly included mortgage recording tax as an allowable cost in computing OPP, whereas the former statute vested in the Commissioner the power to determine whether mortgage recording tax should be included. Exercising that power, the Commissioner promulgated regulations which included mortgage recording tax as an allowable cost to acquire property (20 NYCRR former 590.16[b]) and as an additional cost of a capital improvement if incurred during a construction period (20 NYCRR former 590.16[d]). In short, mortgage recording tax was includible in OPP before the statute was amended and after the statute was amended. This amendment, like the amendment applying to construction period interest costs, was made applicable to tax years beginning on or after January 1, 1993 and to transfers occurring on or after April 15, 1993 (L 1993, ch 57, § 418[8]). However, the effective date of the statute did not eviscerate the regulation then in effect. It codified the regulation and added clarifying language.

The critical question in this proceeding is whether, by adding subparagraph (iv) to section 1440(5) (former [a]), the Legislature intended to bring about a change in the existing law or to

clarify it. To answer that question it is necessary to examine former section 590.16(d) of the Commissioner's regulations and determine whether it can reasonably be construed to include in OPP interest accrued during a construction period on a loan to acquire the real property which is the subject of the capital improvement.

As relevant, 20 NYCRR former 590.16(d) provides that "costs that are clearly associated with construction of a real estate project can also be included as a cost of constructing a capital improvement" and listed among such costs "interest cost paid during [the construction period] on a construction loan, real property taxes, insurance or similar items" (20 NYCRR former 590.16[d]; emphasis added). The Division did not cite to this regulation in its brief and offered no rationale for construing it in such a way as to exclude interest expenses on land acquisition from other costs associated with construction of a capital improvement. As noted, petitioner gives several reasons for construing this regulation so as to include these interest costs in OPP if incurred during a construction period. Since petitioner's was the only reasonable construction of 20 NYCRR former 590.16(d) offered, I conclude that under the former regulation interest paid on a loan to acquire real property which was the subject of a capital improvement was an item similar to interest paid on a construction loan, real property taxes and insurance. As a similar item, such interest was allowable as a "customary, reasonable, and necessary" cost of construction of a capital improvement under the regulation. It follows then that the amendment of Tax Law § 1440(5)(former [a]) was intended to codify and clarify the existing regulation and not to bring about a change in law or policy. Accordingly, construction period interest expenses associated with land acquisition in the amount of $705,088.00 were improperly disallowed by the Division.

D. As noted, section 590 of the gains tax regulations were amended effective November 9, 1994 "to reflect recent statutory amendments to Articles 31-B and 31 of the Tax Law, to clarify and/or modify policy with respect to certain issues, and to make several technical and editorial changes to such regulations" (Notice of Adoption, NY Reg, November 9, 1994). The amended regulations provide that interest paid on a loan to acquire real property may be

included in original purchase price to the extent that the interest paid or required to be paid accrues during a construction period and is attributable to that portion of the real property which was the subject of the capital improvement (20 NYCRR 590.15[c]; 590.17[d]). The regulations also state that the amended language is "effective for transfers occurring on or after April 15, 1993" (20 NYCRR 590.15[c]; 590.17[d]). From this language, it can be inferred that the Division construed 20 NYCRR former 590.16(d) to not include such interest expenses in the calculation of OPP. I assume this is the case. Nonetheless, it was incumbent upon the Division to offer a reasonable explanation of its construction of former section 590.16(d) to counter petitioner's arguments. If there was no rational basis for excluding the construction period interest expenses on land acquisition from OPP under the former regulation, the effective date of the amended regulation cannot be used to supply that basis.

E. Petitioner argues that even if interest expense on land acquisition costs is disallowed, the interest attributed to development rights and tenant buyouts should be allowed because both are closely associated with the construction of the capital improvements. Petitioner maintains that both types of costs were incurred to facilitate and achieve the construction of capital improvements. Mr. Socher's testimony provides a factual basis for these assertions. He testified that development rights were acquired for the purpose of expanding the FAR of the building being constructed and that the leasehold rights were purchased to move the demolition and construction process along as quickly as possible. There is no basis for rejecting this testimony. The Division did not distinguish between interest expense incurred on funds used for land acquisition and interest incurred on funds used for development rights or tenant buyouts, since all three are defined as real property pursuant to Tax Law § 1440.4.

For the reasons stated in Conclusion of Law "C", I find that construction period interest expenses attributable to the development rights and the lease buyouts are properly includible in OPP pursuant to Tax Law § 1440(5)(former [a][ii]). Moreover, I agree with petitioner that interest attributed to funds expended to procure the development rights and lease buyouts are closely associated with the costs of construction under 20 NYCRR former 590.16(d).

Accordingly, petitioner's OPP is properly calculated by inclusion of these interest expenses.

F. The next issue to be addressed is whether petitioner's OPP properly included the special additional mortgage recording tax imposed by Tax Law § 253(1-a). For the years in issue, the Commissioner's regulations specifically identified mortgage recording tax as a cost includible in OPP under both the acquisition leg of OPP (20 NYCRR 590.15 [former (b)]) and the capital improvement leg of OPP (20 NYCRR 590.16 [former (d)]). According to the Division, this meant the mortgage recording tax imposed by Tax Law § 253(1), but not the special additional mortgage recording tax imposed by Tax Law § 253(1-a). The reason the Division gives for construing the regulation as it does is as follows:

> "The Division properly disallowed the amount of the special additional mortgage recording tax imposed upon petitioner because such tax can be taken as a credit against franchise tax and personal income which petitioner acknowledges in its brief at page 12 (Tax Law §§ 210[17] and 606[f]) . . . . The failure to disallow it as part of the original purchase price will produce a windfall not authorized by the Tax Law."

If the regulation explicitly excluded the special additional mortgage recording tax from inclusion in OPP, the Division's reasoning would have a direct bearing on whether the regulation was a reasonable construction of the statute. The regulation does not contain such an exclusion. It merely states that "mortgage recording tax" is one of the costs that may be included in OPP. The question then is whether the unambiguous language of the regulation can be construed to exclude the special additional mortgage recording tax. I agree with petitioner that it cannot.

As pertinent, Tax Law § 253(1) imposes "[a] tax of fifty cents for each one hundred dollars and each remaining major fraction thereof of principal debt or obligation which is . . . secured by a mortgage." In addition to the tax imposed by section 253(1), a special additional tax is imposed on each mortgage recorded on or after January 1, 1979 in the amount of 25 cents per $100.00 and each remaining major fraction thereof (Tax Law § 253[1-a]). The mortgage recording tax and the special additional mortgage recording tax are imposed by the same section of the Tax Law. They are both a tax on the privilege of recording a mortgage. The tax base for each is the same (each $100.00 or major fraction thereof of principal debt secured by the

mortgage). A regulation, like a statute, should be generally construed according to its natural and most obvious sense without resorting to an artificial or forced construction (Cooper-Snell v. State of New York, 230 NY 249, 129 NE 893; Terino v. Levitt, 44 AD2d 167, 354 NYS2d 166, 168). Construing the term "mortgage recording tax" according to its natural and most obvious sense, I find that the term includes the special additional mortgage recording tax. There is no language in 20 NYCRR 590.15 (former [b]) which would alert a reader to the Division's interpretation of the regulation, or cause a reader to analyze the regulation as the Division does, by reference to sections of the corporation franchise and personal income tax laws.

Although a plain language reading of the regulation supports petitioner's position, the Division's "windfall" argument must be addressed since it is essential to its argument. As petitioner notes, many types of expenditures which are includible in OPP have the potential to produce a credit or deduction under some article of the Tax Law other than Article 31-B. The gains tax statute and regulations do not contain a general rule disallowing from OPP any item of expenditure claimed as a credit under another article of the Tax Law. I do not understand how that principle can be read into 20 NYCRR 590.15 (former [b]) without any explicit direction in the regulation.

A comparison of the Division's "windfall" argument with an Appellate Division, First Department, case involving the special additional mortgage recording tax is instructive. Insofar as it relates to mortgages on property improved by a structure containing six or more residential units, the special additional mortgage recording tax is imposed on the lender and cannot be passed on to the seller, real estate broker or any other third person (Tax Law § 253[1-a]). In a successful suit for restitution brought against a lending institution by sellers who had paid the special tax, the court reduced the amount of restitution to be paid to the sellers by the amount of any tax credit they received. In that case, the court stated:

> "If a seller or other person who has paid the special tax has received the dollar for dollar tax credit [provided for in Tax Law §§ 606(f) and 210(17)], it would be giving a windfall to such taxpayer if the mortgagees are required again to pay such seller or other person an amount equal to the special tax paid" (Abrams v. Intercounty Mortgagee Corp., 87 AD2d 748, 448 NYS2d 675, 677).

Superficially, the Division's reasoning seems similar to that adopted in the Abrams decision. In both cases, a potential "windfall" is said to result from the corporation franchise tax and personal income tax credits for the special additional mortgage recording tax. But the court's reasoning in Abrams is not applicable to construing the Division's regulation because inclusion of the special additional mortgage recording tax in OPP is not the equivalent of seeking restitution of tax paid. The first results in a reduction of the base upon which the gains tax is calculated; the second results in a dollar-for-dollar payment based on the amount of tax paid. Moreover, the sellers in the Abrams case were not denied restitution because of the existence of the credit; rather, the amount of the restitution was reduced by the amount of the credit received. The "windfall" the court was seeking to prevent was a direct dollar-for-dollar restitution of amounts which had already been given back to the sellers in the form of a tax credit. No such "windfall" exists for petitioner. Petitioner merely seeks to include in OPP the amounts it paid for mortgage recording tax, as it is allowed to do by the regulation. If all, or some, of petitioner's partners also receive a tax benefit as a result of the credit provided for in Tax Law § 606(f), that is a result of a legislative enactment and does not represent a windfall to petitioner.

Finally, I reject the Division's claim that the amendment of Tax Law § 1440(5)(former [a]) by the Laws of 1993 (ch 57, § 61) supports its interpretation of the regulation. As relevant to this issue, Tax Law § 1440(5)(a)(iii), provides that "[o]riginal purchase price shall also include any tax paid by a transferor to record a mortgage." The statute makes no mention of the special additional mortgage recording tax; however, in a memorandum in support of the legislation, the Division stated:

> "Section one of the bill amends the definition of 'original purchase price' in Tax Law section 1440.5(a) to include customary, reasonable and necessary advertising and marketing costs incurred to sell real property; mortgage recording taxes, including the special additional mortgage recording tax, paid by the transferor in connection with the acquisition of real property, the conversion of real property to cooperative form or the construction of a capital improvement." (Bill Jacket, Governor's Budget Bill, Memorandum in Support of S. 865, A. 1465, L 1993, ch 57, § 61; emphasis

added.)[2]

Prior to the amendment of the statute, the Division had, by regulation, determined that OPP includes mortgage recording tax; therefore, the later amendment of the statute to include mortgage recording tax in OPP did not bring about a change in the law. As already noted, mortgage recording tax was an allowable cost in the computation of OPP before the 1993 amendments and after them. The only difference is that the Division construes the term "mortgage recording tax" as used in the statute to include the special additional mortgage recording tax (see, 20 NYCRR 590.15[b] as amended, effective November 9, 1994)[3] but claims that the same term, when used in its own regulations, did not include the special additional mortgage recording tax. This is an arbitrary and unreasonable construction. Accordingly, the Division is directed to recalculate OPP by including therein the special additional mortgage recording tax paid by petitioner of $93,471.00.

G. 20 NYCRR 590.15 (former [b]) provides that the payment of the New York State real estate transfer tax and the New York City real estate transfer tax by the buyer is deemed to be additional consideration to the seller. The Division maintains that this regulation is a reasonable interpretation of Tax Law § 1440(1) which, as pertinent, defines consideration as:

> "the price paid or required to be paid for real property or any interest therein . . . . Consideration includes the cancellation or discharge of an indebtedness or obligation."

---

[2] No mention is made of the "windfall" that might accrue to the taxpayer as a result of this change, and the credits provided for in Tax Law §§ 210(7) and 606(f) remain in effect.

[3] Again, neither party referred to the amended regulation in support of its own position. 20 NYCRR 590.15(b) and 590.17(d) include the mortgage recording tax in allowable costs of OPP, including the special additional mortgage recording tax. However, both provisions contain a proviso which states that the special additional tax is includible only for transfers occurring on or after April 15, 1993. Obviously, this determination calls into question the legitimacy of that proviso.

Tax Law § 1404 (former [a]), in effect prior to 1989, states:

> "The real estate transfer tax shall be paid by the grantor. If the grantor has failed to pay the tax imposed by this article or if the grantor is exempt from such tax, the grantee shall have the duty to pay the tax."[4]

According to the Division, Tax Law § 1404 (former [a]) places the obligation to pay the transfer taxes on the grantor, and the payment of transfer taxes by the transferee is thus an assumption of an obligation of the transferor by the transferee (see, 20 NYCRR 590.15 [former (b)]. Under Tax Law former § 1440(1), when a transferee assumes an obligation of the transferor, the value of the obligation assumed is deemed to be additional consideration to the transferor.

Petitioner challenges the Division's interpretation of Tax Law § 1404(a) and the correctness of the Division's regulation. It contends that section 1404(a) imposes joint and several liability for payment of the State and City transfer taxes on the grantor and grantee. As a consequence, petitioner argues, the transferees did not assume an obligation of the transferor (petitioner in this case) when they paid those taxes at closing. Petitioner claims that the Division's gains tax regulation is based on a faulty interpretation of the real property transfer tax law.

Joint and several liability may be defined as follows:

> "A liability is said to be joint and several when the creditor may sue one or more of the parties to such liability separately, or all of them together at his option" (Black's Law Dictionary, 5th ed).

In 1989, Tax Law § 1404 (former [a]) was amended by addition of the following provision:

> "Where the grantee has the duty to pay the tax because the grantor has failed to pay, such tax shall be the joint and several liability of the grantor and grantee" (L 1989, ch 61, § 169).

---

[4] Former section 1146-4.0 of the Administrative Code of the City of New York, effective prior to September 1, 1986, and section 11-2104 of the Administrative Code of the City of New York, in effect for the period after September 1, 1986, contain substantially the same provisions.

The Governor's Memorandum in Support of the bill provides as follows:

> "Bill section 169 amends section 1404 of [the Real Estate Transfer Tax] law to clarify that where the grantor fails to pay the tax, the tax becomes the joint and several liability of the grantor and grantee" (Governor's Budget Bill, Memorandum in Support of S.2408-A and A.3608-A).

I conclude that petitioner is only partially correct in saying that the liability for the real estate transfer tax is joint and several. The obligation to pay the real estate transfer tax is placed initially on the grantor. The liability for the tax becomes joint and several only if the grantor does not pay the tax. In this case, the condominium unit purchasers agreed to pay the City and State transfer taxes as a condition of purchase. By their agreement, they assumed an obligation which, in the first instance, was that of petitioner. Consequently, petitioner was required to include in the calculation of consideration the amount of the tax paid by the transferees.

H. Finally, petitioner requests abatement of penalties on the ground that any failure to pay tax when due was due to reasonable cause. I will address each area of assessment separately.

Mr. Socher testified that he was told at the time of the pre-transfer audit that he should not include interest expenses associated with land acquisition in OPP. He estimated those expenses at the time of the pre-transfer filing. Apparently, the tax due in this area flows from his failure to estimate accurately. Petitioner argues that the field auditor's calculations were "arcane" (Petitioner's Brief, p. 37) and were not suggested by the pre-transfer auditor. Petitioner also contends that in 1985 even the Division did not know the proper method of estimating which portions of the loans were attributable to the land. Petitioner maintains that the confusion over the calculation justifies abatement of penalty.

Since I have already found that the interest expenses on real property acquisition, incurred during the construction period, are includible in OPP, a discussion of penalties in this area is academic. I would note, however, that petitioner never offered any evidence to show how Mr. Socher estimated the interest expenses on land, nor is there any evidence in the record that the Division instructed Mr. Socher on how to make such an estimate. The record merely shows that Mr. Socher was directed to exclude land acquisition interest expenses from OPP. Therefore,

petitioner has not offered an explanation which would justify cancelling penalties if such expenses are not included in OPP.

My conclusion with respect to penalties relating to petitioner's treatment of interest expenses associated with the development rights and tenant buyouts is different. The Division's regulations state that interest costs incurred on a construction loan during a period of construction is includible in OPP. It was petitioner's understanding that the loans it received to develop the Park Belvedere project were construction loans. It viewed the interest expenses it incurred during the construction period as one of the necessary costs it incurred while construction proceeded. Moreover, Mr. Socher testified that the Division was aware at the time of the pre-transfer audit that a portion of the interest was attributable to loans used to acquire development rights and to buy out existing tenants, but it did was not directly instruct him to exclude those expenses from OPP. Mr. Socher credibly testified that he was not apprised of the Division's position until the time of the field audit. In light of the conclusions reached here, that petitioner's interpretation of the regulation was correct, I find that petitioner's inclusion of these interest costs in OPP was at least reasonable under the circumstances. Likewise, petitioner acted reasonably in interpreting the term "mortgage recording tax" as used in the regulation to include the special additional mortgage recording tax. Again, Mr. Socher credibly testified that he was not informed at the time of the pre-transfer audit of the Division's position concerning the additional tax.

Petitioner's failure to include the State and City real estate transfer tax in its calculation of consideration was in direct contravention of the Division's regulations. Petitioner states that the regulation was "new" at the time of the pre-transfer filing and conflicted with practices followed in sales of new residential condominiums by New York City developers. At the time of the pre-transfer filing, the Division's position regarding the addback of these taxes had been promulgated either through Publication 588 (Gains Tax on Real Property Transfers, a 1983 booklet published by the Division setting forth the Division's preliminary interpretation of the gains tax law) or the Division's regulations. Furthermore, the Park Belvedere offering plan

demonstrates that petitioner was aware of New York City's position on this issue. Consequently, petitioner has not shown that it had reasonable cause for not including the amount of the real estate transfer taxes in consideration.

I. The petition of Zeckendorf Columbus Co. is granted to the extent indicated in Conclusions of Law "C", "E" and "F"; the Notice of Determination dated June 27, 1991 shall be modified accordingly; and in all other respects, the petition is denied.

DATED: Troy, New York
May 11, 1995

/s/ Jean Corigliano
ADMINISTRATIVE LAW JUDGE