

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
ANTHONY MARTINEZ	:	DETERMINATION
for Revision of a Determination or for Refund	:	DTA NO. 813568
of Tax on Gains Derived from Certain Real	:	
Property Transfers under Article 31-B of the	:	
Tax Law.	:	

Petitioner, Anthony Martinez, P.O. Box 133, Adirondack, New York 12808, 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, 500 Federal Street, Troy, New York, on October 27, 1995, at 1:15 P.M., with all briefs to be submitted by May 28, 1996, which date began the six-month period for the issuance of this determination. Petitioner appeared by Jessel Rothman, P.C. (Jessel Rothman, Esq., of counsel). The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (Susan Hutchison, Esq., of counsel).

ISSUE

Whether the Division of Taxation properly imposed gains tax under Article 31-B of the Tax Law on the transfer of a one-sixth partnership interest as an acquisition of a controlling interest in an entity with New York real estate, by aggregating such interest with other partnership interests transferred to the same transferees.

FINDINGS OF FACT

1. On December 30, 1987, Anthony Martinez ("petitioner"), entered into an agreement with Eugene and Marcia Leogrande (the "Leograndes"), Edward T. and Linda S. Moore (the "Moore's"), and Vincent Reinhardt to form the partnership known as L & M Investment Associates. The business of the partnership was to consist of the ownership and management of

certain real property located in the Town of Queensbury, Warren County, New York; the construction of certain buildings on such lands; the acquisition of additional lands and the operation, leasing and management of such properties. The purpose of the partnership was the building of a shopping center.

The partnership interest of each partner was represented in the agreement as follows:

Eugene and Marcia Leogrande	33 1/3%
Edward T. and Linda S. Moore	33 1/3%
Vincent Reinhardt	16 2/3%
Anthony Martinez	16 2/3%

2. On or about October 12, 1989, pursuant to a provision of the partnership agreement, petitioner served a Notice of Intention to Arbitrate and Demand for Arbitration upon the Leograndes, the Moores and Vincent Reinhardt, alleging misuse and misappropriation of partnership funds. Petitioner sought the return of misappropriated funds, an adjustment to the stated partnership interests, and a restatement of petitioner's capital contributions.

3. Arbitration proceedings were held in May and June 1990, with a continuation scheduled for July 17, 1990. Before it was continued, the Leograndes, the Moores and Mr. Reinhardt issued a letter of intent dated June 14, 1990 to purchase petitioner's interest in L & M Investment Associates and the real estate known as French Mountain Commons in Lake George, New York. Such purchase was for the sum of \$250,000.00 and was scheduled to be completed by July 12, 1990. One by one, the proposed purchasers subsequently made it clear that they did not desire to purchase petitioner's interest. Although petitioner offered to purchase the interests of the other parties, each refused to sell. As a result, petitioner commenced an action in Supreme Court, Warren County, New York seeking specific performance of the letter of intent.

4. Between July 19 and July 27, 1990, desiring to avoid further arbitration and litigation, Mr. Moore approached petitioner regarding the sale of petitioner's interest to him. On July 27, 1990, petitioner contracted to sell his 1/6th partnership interest to Mr. and Mrs. Moore for \$230,000.00. The agreement specifically stated that the Moores desired to settle all litigation related to petitioner's interest by purchasing petitioner's interest in the partnership. Accordingly,

a deed representing a 1/6th interest in the real estate and a Real Property Gains Tax Affidavit were submitted as evidence of the conveyance from petitioner to the Moores on July 27, 1990. Simultaneously, petitioner executed stipulations of discontinuance for the various actions against the L & M partners. A Certificate of Amendment of the Partnership of L & M was executed reflecting the removal of petitioner as a general partner of the partnership. Likewise, an Amended Business Certificate by L & M Investment Associates was executed by the remaining partners, reflecting the revised partnership interests as follows:

Eugene and Marcia Leogrande	33 1/3%
Edward and Linda Moore	50%
Vincent Reinhardt	16 2/3%

5. A Real Property Gains Tax Transferor Questionnaire was filed by Vincent Reinhardt, and received by the Division on April 2, 1991, reporting a transfer of a 1/6th partnership interest in L & M Investment Associates to the Moores. The real property interest is a shopping center located on Route 9, Queensbury, New York. The date of transfer was reported to be February 28, 1991, and stated consideration was \$500,000.00.

Also during April 1991, the Division received transferee questionnaires indicating transfers of partnership interests in L & M by Eugene Leogrande (33 1/3%) and Anthony Martinez (16.67%). The reported dates of transfer were August 10, 1990 and July 27, 1990, respectively. The purchasers were the Moores.

6. The Division issued correspondence to petitioner dated April 23, 1991 indicating that a review of the Division's records revealed that there was a transfer of a controlling interest in a partnership, which has an interest in real property in New York State. The correspondence further set forth information and documents which the Division requested petitioner to submit.

7. Petitioner's representative responded by correspondence dated May 20, 1991, in which he stated that petitioner had sold his 1/6th partnership interest and did not transfer, nor did the Moores acquire, a controlling interest in any entity with real property.

8. Based upon information supplied by the Moores and Mr. Reinhardt, the original purchase price ("OPP") for the real property was reported to be \$2,702,525.00. The Division

multiplied the OPP by 16.67% (petitioner's partnership interest) to arrive at an original purchase of \$450,000.00. The amount of OPP is not in dispute.

9. The parties herein agree that consideration for the transfer of petitioner's partnership interest to Edward Moore, which occurred on July 27, 1990, was comprised of \$230,000.00 cash and \$450,000.00 of mortgage debt assumed by Moore upon the transfer of the interest and related real estate. The \$450,000.00 mortgage amount represents 1/6th of the principal outstanding on the mortgage loan of \$2,700,000.00, verified by documentation as of August 29, 1990.

10. The Division computed the gains tax at 10% of the difference between consideration of \$680,000.00 and OPP of \$450,000.00, or \$23,000.00, and accordingly issued a notice of determination dated January 17, 1993 in that amount plus penalty and interest.

11. On or about March 31, 1993, petitioner filed a Request for Conciliation Conference. A conference was held on July 14, 1994, and an Order sustaining the statutory notices was issued dated November 10, 1994. On or about February 8, 1995, a petition contesting the conciliation order was filed with the Division of Tax Appeals. The Division of Taxation filed its answer on March 22, 1995.

SUMMARY OF THE PARTIES' POSITIONS

12. Petitioner maintains that the transfer in issue was not a real estate transfer subject to gains tax under Article 31-B. Petitioner believes it is properly treated as the sale of a 1/6th partnership interest in L & M Investment Associates, for total consideration of \$680,000.00. He also believes that it is appropriate for the Division to consider the intent of the petitioner-transferor in this matter, and that, even if it is the intent of the transferee that governs, such intent was centered on the discontinuance of the litigation and arbitration.

13. The Division maintains that the transfer by petitioner was properly subject to gains tax, and that one must look to the acts of the transferee in determining whether a taxable acquisition has occurred.

CONCLUSIONS OF LAW

A. Tax Law § 1441, which became effective March 28, 1983, 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 is less than the \$1,000,000.00 threshold.

Tax Law § 1440(7) defines "transfer of real property" as encompassing an array of transactions, including the "transfer or acquisition of a controlling interest in any entity with an interest in real property."

"Controlling interest", in the case of a partnership, association, trust or other entity, means 50 percent or more of the capital, profits or beneficial interest in such partnership, association, trust or other entity (Tax Law § 1440[2]).

Relevant to how the phrase "acquisition of a controlling interest in an entity with an interest in real property" is applied, 20 NYCRR former 590.44(a), in effect on the date of transfer, provided:

"In the case of a partnership, association, trust or other entity, the acquisition occurs when a person or group of persons, acting in concert, acquires a total of 50 percent or more of the capital, profits or beneficial interest in such entity. Because the statute looks to the acquisition of the controlling interest, it is the act of the transferee which triggers the tax." (Emphasis added.)

20 NYCRR former 590.45(d) provides further guidance with respect to the issue of transfers of controlling interests. It states in part:

"Question: If a shareholder acquires a 50-percent interest in a corporation and gains tax is paid on the transfer, and one year later the same shareholder acquires an additional 20 percent, is there a second acquisition of a controlling interest?"

"Answer: Yes. The interests acquired after March 28, 1983 are added together in determining whether an acquisition of a controlling interest has occurred. No acquisition of stock will be added to another acquisition of stock if they occur more than three years apart, unless the acquisitions were so timed as part of a plan to avoid the gains tax. An example of this would be if T acquired 80 percent of the stock and simultaneously contracted for the purchase of the remaining 20 percent in three years and one day."

B. The transfer of petitioner's interest of 16.67% and acquisition thereof by the Moores occurred on July 27, 1990. Although there did not appear to be any intent on the part of the

Moore to acquire a controlling interest at the time they acquired petitioner's share, within seven months (by February 28, 1991) the Moores had also acquired the shares of the Leograndes (a 33 1/3% partnership interest) and the 16.67% share of Vincent Reinhardt. Applying the statutory provisions and regulations in effect at the time of the acquisitions, the Division of Taxation properly imposed gains tax on the transfer of petitioner's interest in a partnership which clearly had an interest in real property. The acts of the transferees, the only evidence indicating intent in this case, amounted to an acquisition of a controlling interest as defined by the gains tax provisions. In addition, such acquisitions took place within the three-year window referred to in the regulations.

C. In a case with substantially similar facts (Matter of Harris, Tax Appeals Tribunal, December 30, 1993), the same issues were raised by petitioner therein. In that matter, the Tribunal agreed with the Division's argument that the use of the word "acquisition" rather than "transfer" reflects a legislative decision to impose tax in entity transactions based on the acts of the transferee or transferees rather than on the acts of the the transferors. The Tribunal continued by stating:

"The significance of this word choice is emphasized by the fact that the model for the statewide gains tax, the repealed Article 31-A of the Tax Law, which imposed a gains tax in New York City (see, Matter of Old Farm Lake Co., Tax Appeals Tribunal, April 2, 1992), imposed the tax on transfers of controlling interests. Further, in 1989 the Legislature amended the State gains tax to include the transfer, as well as the acquisition of a controlling interest, in the definition of transfer of real property (L 1989, ch 61, § 193). The purpose of this amendment was to expand the imposition of the tax beyond the acquisition of a controlling interest to include transfers of controlling interests, so that syndications and the conversion of private corporations to public corporations would be subject to tax (Memorandum in Support of L 1989, ch 61, Bill Jacket at 39)."

The Tribunal went on to comment on the "intent" issue:

"We do not see how the position urged by petitioner . . . that the transferor's intent determines whether these has been a taxable entity transaction, can be harmonized with the term 'acquisition', which obviously focuses on the acts of the transferee. Further, petitioner's interpretation would drastically reduce the application of the tax, because an acquisition of a controlling interest would only be taxable if acquired from transferors who intended the transferee to acquire a controlling interest. Such a restricted application is inconsistent with the otherwise expansive definition of transfer of real property employed by the statute to maximize revenues" (Matter of Harris, *supra*, citing Matter of Bredero Vast Goed, N.V.

v. Tax Commn., 146 AD2d 155, 539 NYS2d 823, appeal dismissed 74 NY2d 791, 545 NYS2d 105.)

D. Petitioner also erroneously attempts to make the argument that the (current) regulation 20 NYCRR 590.44, which took effect on November 9, 1994, should be applied to petitioner's 1990 transfer. 20 NYCRR former 590.44, in effect at the time of petitioner's transfer, dealt with the acquisition of a controlling interest and emphasized the fact that it is the act of the transferee which triggers the gains tax. Such section was renumbered 20 NYCRR 590.45 (effective November 9, 1994) and remained substantially the same as its predecessor. The new 20 NYCRR 590.44 (in effect currently), which petitioner insists should be applied herein, addresses the aggregation of partial or successive transfers of real property. Such regulation emphasizes that a determination of whether the sales in issue are pursuant to a plan or agreement is dependent upon the intent of the transferor at the time of each transfer. Asserting that the aggregation provisions should apply, petitioner seeks to have petitioner's intent govern in this case.

A regulation not in effect at the time of a transaction is rarely applied in a tax matter. However, even if the date of enactment is disregarded, the application of the current 20 NYCRR 590.44 regulation is in error for two additional reasons: first, the transfers which took place in this matter were of partnership interests, not parcels of real estate; and second, Tax Law § 1440(7) specifically provides for the acquisition of a controlling interest in an entity with an interest in real property, and this more specifically governs the situation at hand. In Matter of Harris (supra) the Tribunal addressed the same argument. In that matter, as here, the aggregation clause is not applicable to determine whether a taxable acquisition has occurred.

E. The petition of Anthony Martinez is hereby denied, and the Notice of Determination, dated January 17, 1993 is sustained.

DATED: Troy, New York
November 27, 1996

/s/ Catherine M. Bennett
ADMINISTRATIVE LAW JUDGE

