STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
THOMAS GORMAN, THERESE BRANDSHAFT AND HERBERT BRANDSHAFT	:	DETERMINATION DTA NO. 814354
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.	:	

Petitioners, Thomas Gorman, Therese Brandshaft, and Herbert Brandshaft, c/o Francis L. Bosco, Esq., 38 Church Street, Patchogue, New York 11772, 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 Arthur S. Bray, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York, on June 13, 1996 at 1:15 P.M. All briefs and documents were submitted by October 7, 1996, which commenced the six-month period for issuing this determination. Petitioners appeared by Howard M. Koff, Esq. The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (Peter T. Gumaer, Esq., of counsel).

ISSUE

Whether the Division of Taxation properly aggregated the consideration received from two transfers of real property so that the $1,000,000.00 threshold for real property transfer gains tax liability was met.

FINDINGS OF FACT

1. Petitioner Thomas J. Gorman became involved in the real estate business shortly after the conclusion of World War II. In the early 1960s petitioner and his associates began erecting buildings. Most of Mr. Gorman's real estate transactions followed the same pattern. It

was Mr. Gorman's practice to select a piece of property, obtain a loan to finance an improvement (such as a service station, fast food restaurant, or post office), and then rent the property in order to obtain rental income. Eventually, the mortgage on the property would be satisfied and the amount of rental income would significantly increase. Mr. Gorman's principal source of income arises from the streams of rental income that his investments generated. Over the years, Mr. Gorman and his associates made more than 200 investments in property located in New York, Pennsylvania, Georgia and Florida. Most of the investments have been retained by petitioner and his partners including the first investment which was made in 1960.

2. In the 1960s Mr. Gorman and his partners assembled a group of vacant lots in order to acquire one large property. The assemblage included the two properties involved in this matter. Neither of the properties was ever listed for sale.

3. Mr. Gorman and his partners were approached by Mr. Mullaney and his associates on behalf of VIA Properties Associates, L.P. ("VIA") to purchase a parcel of property in order to build a Hampton Inn. Mr. Gorman responded that he and his partners would be interested in a long-term lease of the land. It was proposed by Mr. Gorman that VIA could build a Hampton Inn and that petitioner and his partners would receive rental income based on a percentage of the revenues generated by the property. The counterproposal was consistent with the usual business practice of Mr. Gorman and his associates.

4. Mr. Gorman considered the proposal of constructing a Hampton Inn very attractive. A service station, a Howard Johnson's (which is now a Ground Round), a bank and a "strip center" were located adjacent to the property in which VIA was interested. Mr. Gorman and his associates held leases which entitled them to rental income based on a percentage of receipts earned by each of the foregoing properties. It was anticipated that the addition of a Hampton Inn would lead to greater revenues for the businesses which would, in turn, increase their rental income. Mr. Gorman and his associates also reasoned that they could use the proceeds from the sale to acquire other properties to enhance their investment portfolio.

5. Mr. Mullaney and his associates ascertained that a bank was unwilling to provide a mortgage to finance the construction of a Hampton Inn unless they owned a fee interest in the property. Under these circumstances, Mr. Gorman and his partners relented and agreed to sell the land in order for the development to proceed. On December 15, 1986, petitioners, Thomas Gorman, Therese Brandshaft and Herbert Brandshaft, as tenants in common, transferred a fee interest in real property to VIA.

6. At the time Mr. Gorman negotiated the sale of the land for the Hampton Inn, VIA was interested in purchasing a contiguous parcel to provide additional parking in the future and for use as a leaching field. Mr. Gorman countered with a proposal for a 39-year lease with annual cost of living adjustments. Pursuant to the negotiations, the parties agreed on an initial rent of $65,000.00. Mr. Maloney, however, insisted on an option to purchase. Finally, Mr. Gorman agreed that the lessees would be given an option to purchase the contiguous parcel which could be exercised in the sixth year of the lease. Petitioners anticipated that, in the sixth year, the lessees would not be in a position to purchase the property and Mr. Gorman and his associates would retain ownership of the property.

7. In accordance with the foregoing, VIA and petitioners executed an Agreement of Lease, dated December 15, 1986, which granted VIA a 39-year lease on the adjacent property. The lease provided, in part that:

> "Tenant shall have the option, exercisable during the one year period from and after the end of the fifth Lease Year, until the end of the sixth Lease Year, to Purchase the fee title of Landlord in and to the land and improvements constituting the Demised Premises. . . ."

8. Petitioners entered into the transaction of their own free will and were aware of the option to purchase the property in the sixth year.

9. The Division issued a Tentative Assessment and Return, dated March 12, 1986, which asserted that tax was due in the amount of $115,470.70. The amount of tax due was determined by aggregating the purchase price for the parcel of $903,000.00 with the value attributed to the long-term lease. Petitioners remitted the tax at the closing of title in December 1986.

10. When the sixth year arrived, many motels and hotels in the area were being foreclosed upon and, as a result, the bank which held the mortgage on the Hampton Inn insisted that the option be exercised. The bank wanted to protect its interest in the event that the Hampton Inn failed.

11. When the purchasers decided to exercise the option, Mr. Gorman and his son contacted an attorney, Francis L. Bosco. Mr. Gorman and his son explained to Mr. Bosco that there was a piece of property that a party wished to acquire under an option to purchase. Mr. Bosco was asked to examine the lease and determine whether the option to purchase had to be honored. It was Mr. Bosco's understanding that Mr. Gorman was looking for a way to avoid honoring the option to purchase. At this time, Mr. Gorman explained that the lease was originally drafted with the intention of earning a substantial amount of money over the 39-year term of the lease. He also explained that petitioners wished to keep the property which enhanced the value of the remaining properties. After reviewing the documents, Mr. Bosco was of the opinion that the option was valid, that it was properly exercised, and that petitioners were required to transfer title pursuant to the option in the lease.

12. In anticipation of the closing of title, transferee and transferor questionnaires were submitted to the Division indicating petitioners' intent to transfer the subject property to VIA. Thereafter, the Division issued a Tentative Assessment and Return, dated January 11, 1993, which stated that the total amount of tax due was $68,239.14.

13. On January 13, 1993, the real property, which is the subject of this matter, was conveyed by petitioners to VIA. The total consideration for the transfer was $682,391.40.

14. The amount set forth as tax due in the Tentative Assessment and Return was remitted at the closing of title, on January 13, 1993, by tendering a check to Commonwealth Land Title Insurance Company, the purchaser's title insurance company.

15. On February 11, 1993, petitioners filed a Claim for Refund of Real Property Transfer Gains Tax seeking a refund in the amount of $68,239.14. In their refund claim, petitioners asserted that aggregation was improper because the sales occurred more than six

years apart and because the sale was effected pursuant to an option over which petitioners had no control.

16. On March 22, 1993, the Division received the payment of $68,239.14. Since the Division regarded the payment as late, it issued a Notice of Determination, dated May 13, 1993, to Thomas Gorman which asserted that there was a balance due of $8,229.72 consisting of interest of $685.03 and a penalty of $8,119.69 for late payment, less payments or credits of $575.00. The foregoing notice included an attachment which stated that the claim for refund in the amount of $68,239.14 was denied. In the statement, the Division explained, among other things, that "[t]here are no provisions in Section 590.42 to grant an exemption from aggregation based on the amount of time between the sales of contiguous or adjacent parcels." It also stated that section 590.45(d) of the gains tax regulations is inapplicable since this section deals only with the aggregation of entity transfers. The Division further noted that the only cost which was part of the original purchase price and which had been verified was legal fees of $5,750.00.

17. Petitioners filed a request for a conciliation conference which led to the issuance of a conciliation order dated September 8, 1995. In the order, the penalty for late payment asserted in the notice dated May 13, 1993 was cancelled and the amount of interest was recomputed to be $697.08. The conciliation conferee also rejected the refund claim.

18. Petitioners filed a petition which asserted that it was error to aggregate the sales, that the subject sales, which occurred six years apart, were separate and independent, and that it was error to deny the refund claim.

19. Petitioners are long-term investors who seek to acquire properties, improve them, retain ownership and eventually have a property that is debt free and generating substantial income.

20. The 1986 and 1993 transfers were not structured to avoid real property gains tax. There were never any discussions between the owners and the purchasers of the property to structure the property to avoid gains tax.

SUMMARY OF THE PARTIES' POSITIONS

21. Relying upon Matter of Bombart v. Tax Commission of the State of New York (132 AD2d 745, 516 NYS2d 989) and Matter of Sanjaylyn v. State Tax Commn. (141 AD2d 916, 528 NYS2d 948, appeal dismissed 72 NY2d 950, 533 NYS2d 55), petitioners argue that transfers of contiguous properties will not be aggregated where the transfers do not constitute a single sales transaction. According to petitioners, a single sales transaction will not be found where the taxpayers intend to retain the subject parcel citing Matter of General Builders Corporation (Tax Appeals Tribunal, December 24, 1992) and Matter of Armel (Tax Appeals Tribunal, July 23, 1992). In support of their position that a single sales transaction did not occur here, petitioners rely upon the following facts: (1) at the time of the 1986 sale, petitioners entered into a 39-year lease of the subject property, (2) the sales occurred more than six years apart, (3) the second sale took place pursuant to an option over which petitioners had no control, (4) the subject parcels were never placed on the market for sale, (5) petitioners are long-term investors, and (6) petitioners acquired the property, which is the subject of this matter, in the 1960s.

22. In its brief, the Division asserts that the 1986 and 1993 transfers constitute a single transfer of real property pursuant to 20 NYCRR 590.43. The Division submits that the sales were properly aggregated because petitioners failed to demonstrate that the only correlation between the properties was their contiguity and that the properties were not used for a common or related purpose. According to the Division, the testimony shows that Mr. Gorman was aware of the option to purchase in the 1986 lease and that he voluntarily signed the lease that granted VIA the option to purchase the subject property. The Division takes issue with the argument that Mr. Gorman was forced to sell the property. According to the Division, Mr. Gorman was not forced to do anything and he could have retained the subject property if he had chosen to do so.

Also relying upon Matter of Sanjaylyn Company v. State Tax Commission (supra) and Matter of Bombart v. Tax Commission of the State of New York (supra), the Division argues that the transfers of contiguous properties to one transferee are aggregated to constitute a single

sales transaction. It is further submitted that Matter of General Builders Corporation (supra) is inapposite.

CONCLUSIONS OF LAW

A. Tax Law former § 1441, which became effective March 28, 1983, imposes a 10% tax upon gains derived from the transfer of real property located in New York State. Tax Law former § 1443(1) provides for a partial or total exemption if the consideration is less than the $1,000,000.00.

B. The term "transfer of real property" is defined in the first sentence of Tax Law former § 1440(7) as follows:

> "'Transfer of real property' means 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."

The inclusion of the term "transfers" indicates that "the sale of more than one parcel may be treated as a single transaction" (Matter of Iveli v. Tax Appeals Tribunal, 145 AD2d 691, 535 NYS2d 234, 235, lv denied 73 NY2d 708, 540 NYS2d 1003).

C. The primary consideration in determining whether a transaction is subject to tax is the economic reality of the transaction. This principle was explained in Matter of General Builders Corporation (supra) as follows:

> "In determining whether petitioner's transactions are subject to the gains tax, the focus of the analysis is on the economic reality of the transactions (Matter of Bredero Vast Goed, N.V. v. Tax Commn., 146 AD2d 155, 539 NYS2d 823, appeal dismissed 74 NY2d 791, 545 NYS2d 105 [where the court sustained looking through two tiers of entities to find a transfer of real property]). This requires examining the circumstances surrounding the entire transaction including, of course, events which may have occurred many months before the actual closing of title to the property (Matter of Bredero Vast Goed, N.V. v. Tax Commn., supra). In order to analyze whether a taxable transaction has occurred, previous cases have looked at the entire transaction to determine such things as the identity of the transferors or transferees (Matter of Howes, Tax Appeals Tribunal, September 22, 1988, affd 159 AD2d 813, 522 NYS2d 972; Matter of Brooks, Tax Appeals Tribunal, September 24, 1992; Matter of 307 McKibbon St. Realty Corp., Tax Appeals Tribunal, October 14, 1988) or whether adjacent or contiguous parcels are related (Matter of Albany Pub. Markets, Tax Appeals Tribunal, August 27, 1992; Matter of Armel, Tax Appeals Tribunal, July 23, 1992; Matter of Eff & Zee Co., Tax Appeals Tribunal, April 16, 1992)."

D. When there is a transfer of contiguous or adjacent parcels to one transferee, the pertinent section of the Division's regulations is 20 NYCRR former 590.42. This section provides as follows:

> "Question: Is the consideration received by a transferor for the transfer of contiguous or adjacent parcels of property to one transferee added together for purposes of applying the $1 million exemption?
>
> "Answer: Generally, yes. A transfer of real property is defined in section 1440(7) of the Tax Law to mean 'the transfer or transfers of any interest in real property.' Thus, the separate deed transfers of contiguous or adjacent properties to one transferee are, for purposes of the gains tax, a single transfer of real property. It is the consideration for the interests in a single transfer, regardless of the number of deeds used to transfer the property, that is used to determine the application of the $1 million exemption.
>
> "However, if the transferor establishes that the only correlation between the properties is the contiguity or adjacency itself, and that the properties were not used for a common or related purpose, the consideration will not be aggregated.
>
> "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.)"

E. As framed by the foregoing regulation and court precedent, the focus of the inquiry in determining whether the parcels were properly aggregated by the Division is whether they were used for a common or related purpose (see, Matter of Sanjaylyn Company v. State Tax Commission (supra); Matter of Bombart v. Tax Commission of the State of New York (supra). Here, despite petitioners' protestations to the contrary, the evidence supports the conclusion that the foregoing test was satisfied. The record shows that on the same day that petitioners conveyed a deed for the development of a Hampton Inn, they leased an adjoining parcel to the purchasers of the property for use as a parking lot. Clearly, the parcels were used for a related purpose. The record further shows that, at the time that the deed was executed conveying the land for the development of the Hampton Inn, petitioners, of their own volition, gave the lessees an option to purchase the land used as a parking lot in the sixth year of the lease. Thus, the economic reality is that these were not discrete transfers.

F. Petitioners' arguments do not warrant a different result. In resolving the question of whether parcels were used for a common or related purpose, the determinative point in time is

when the contract of sale was executed (Matter of Armel, supra). Therefore, petitioners' arguments that they acquired the property in the 1960s, that they are long-term investors and that the subject parcels were never placed on the market are irrelevant. Petitioners have stressed the fact that at the time of the 1986 sale, they entered into a 39-year lease. However, this argument overlooks the fact that the same lease included the option to purchase which led to the transaction at issue herein. Similarly, petitioners' argument that they had no control over the option to purchase overlooks the fact that petitioners did not have to agree to a contract which contained an option to purchase. It is clear that petitioners made a business decision that it was in their interests to depart from their usual mode of operation in order to have a Hampton Inn erected. Having made this decision, petitioners' claim that it was not their intention to sell the adjoining property is unpersuasive. Lastly, petitioners' focus upon the length of time between sales is of no consequence because the time period is simply a reflection of when the option to purchase could be exercised under the contract. It is noted that Matter of General Builders Corporation (supra) and Matter of Armel (supra) are distinguishable on their facts because in each instance the taxpayer established that there was a different intent with respect to the sales of the contiguous parcels.

G. The petition of Thomas Gorman, Therese Brandshaft and Herbert Brandshaft is denied.

DATED: Troy, New York
April 3, 1997

/s/ Arthur S. Bray
ADMINISTRATIVE LAW JUDGE