STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
EMPIRE OF AMERICA REALTY CREDIT CORP.	:	DETERMINATION DTA NO. 818473
for Revision of a Determination or for Refund of Sales and Use Taxes under Articles 28 and 29 of the Tax Law for the Period June 1, 1991 through August 31, 1995.	:	

Petitioner, Empire of America Realty Credit Corp., 1926 Tenth Avenue North, Suite 400, Lake Worth, Florida 33461, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period June 1, 1991 through August 31, 1995.

A hearing was held before Frank W. Barrie, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York, on May 14, 2002 at 9:30 A.M., with all briefs[1] to be submitted by November 15, 2002, which date began the six-month period for the issuance of this determination. Petitioner appeared by Steven U. Teitelbaum, Esq. The Division of Taxation appeared by Barbara G. Billet, Esq. (Cynthia E. McDonough, Esq. and James Della Porta, Esq., of counsel).

[1] Attached to the Division's brief dated October 15, 2002 was an appendix consisting of 15 pages, in the nature of evidentiary material, to which no weight or consideration was given since the record was closed to additional evidence at the completion of the hearing.

ISSUE

Whether petitioner is liable for sales or use tax on tangible personal property it acquired as part of its overall acquisition of a mortgage banking business, which was the subsidiary of a failed bank under the receivership of the Resolution Trust Corporation.

FINDINGS OF FACT

1. In September of 1996, Midcoast Mortgage Corporation purchased all of the issued and outstanding capital stock of petitioner, Empire of America Realty Credit Corp., and transplanted petitioner's mortgage banking business from Buffalo, New York to its own Florida base of operations. Nonetheless, petitioner remains in existence, albeit under this new ownership, with offices located at the Lake Worth, Florida headquarters of Midcoast Mortgage Corporation, its parent corporation.

2. The mortgage banking business which petitioner operated at 100 Seneca Street in Buffalo during the audit period was acquired by petitioner's predecessor, Empire Acquisition Corporation, from a wholly-owned subsidiary of Empire of America Federal Savings Bank ("failed federal savings bank") also known (to make matters somewhat confusing) as Empire of America Realty Credit Corp. Empire Acquisition Corporation, the purchaser of the failed federal savings bank's mortgage banking subsidiary, was a wholly-owned subsidiary of Carbadon Corporation, a company formed by an investor group solely for the purpose of acquiring substantially all of the assets of the valuable mortgage banking subsidiary of the failed federal savings bank.

3. Empire of America Federal Savings Bank was placed under the control of the Resolution Trust Corporation ("RTC") on January 24, 1990, when RTC was appointed conservator of the failed federal savings bank. An apparent bright spot for the failed federal

savings bank was its wholly-owned subsidiary, Empire of America Realty Credit Corp., whose statements of income and retained earnings reflect a profitable and ongoing enterprise:

Items of Income	Items of Expense	1990	1989
Loan administration		$33,864,708.00	$28,301,987.00
Loan origination		446,359.00	972,134.00
Gain on sale of loans, net		3,433,710.00	3,327,379.00
Interest		9,077,043.00	26,649,219.00
Gain on sale of loan administration contracts		34,458.00	3,434,479.00
Other		2,551,198.00	2,357,002.00
Total Income		$49,407,476.00	$65,042,200.00
	Personnel	$12,118,452.00	$17,891,066.00
	Occupancy and equipment	4,803,276.00	6,116,013.00
	Provisions for losses	4,344,120.00	3,160,000.00
	Other operating	16,769,647.00	16,174,250.00
	Interest	7,167,126.00	18,015,743.00
	Restructuring charges	-0-	1,983,986.00
	Total Expenses	$45,202,621.00	$ 63,341,058.00
Income		$ 4,204,855.00	$ 1,701,142.00

In addition to the ongoing profitability, noted above, of the subsidiary's mortgage banking business, this subsidiary also had significant retained earnings as follows:

	1990	1989
Beginning of year	$25,637,451.00	$24,087,309.00
End of year	$29,443,386.00	$25,637,451.00

Consequently, the subsidiary's mortgage banking business carried a hefty price tag, with the total cost of its acquisition by Empire Acquisition Corp. of $133.1 million.

4. The $133.1 million cost of the acquisition was allocated to the acquired assets and assumed liabilities based on their so-called "fair values" as noted in financial statements prepared by KPMG Peat Marwick for petitioner, Empire of America Realty Credit Corp.,[2] as follows:

Assets acquired	
Mortgage loans held for sale	$ 62,520,998.00
Investor and escrow advances receivable	3,236,818.00
Mortgage foreclosure receivables	1,996,127.00
Purchased servicing	69,741,250.00
Property and equipment	950,000.00
Other assets	803,447.00
Total assets acquired	$139,248,640.00
Liabilities assumed	
Accounts payable and accrued expenses	(6,191,395.00)
Acquisition cost	$133,057,245.00

5. This multi-million dollar acquisition was memorialized in a complex document consisting of a "purchase and sale agreement" dated June 28, 1991 of 76 pages, plus hundreds of pages of attached exhibits. The parties to the agreement were described in the very first paragraph of the lengthy document as follows:

[2] The record does not disclose any detailed information concerning the transformation of Empire Acquisition Corp. into Empire of America Realty Credit Corp., i.e., petitioner. But apparently, the transformation was one only of form and not substance.

> THIS AGREEMENT is made . . . by and among the Resolution Trust Corporation, as Receiver for Empire Federal Savings Bank of America ("*Shareholder*"), Empire of America Realty Credit Corp., a Michigan corporation ("*Seller*"), and Empire Acquisition Corp., a New York corporation ("*Buyer*"). (Emphasis in original.)

Article I of this agreement sets forth definitions of 129 terms in approximately 15 pages including the following pertinent ones:

> "*Assets*" means the assets to be purchased by Buyer hereunder, namely the Accounts Receivable, Assigned Contracts, Books and Records, Intangible Property, Other Assets, Pipeline Commitments, Property, Plant and Equipment, Saleable Warehouse Loans and Servicing Rights.
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> ****
>
> "*Business*" means the mortgage banking business in which Seller is engaged and which is comprised of originating, purchasing, selling and servicing mortgage loans.
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> ****
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> "*Buyer*" means Empire Acquisition Corp., a New York corporation.
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> ****
>
> "*Excluded Assets*" means (i) the Mortgage Investments, REO/REH Property and Unsalable Warehouse Loans, (ii) the accounts receivable set forth on Exhibit 2.3(a)(i), and (iii) all cash on hand and marketable securities [(excluding GMNA mortgage backed securities held for sale)], in each case owned by Seller as of the Cut-off Date.
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> ****
>
> "*Intangible Property*" means the name Empire of America Realty Credit Corp. and all abbreviations thereof, all trade names, servicemarks, including Seller's logo, and copyrights owned by Seller as of the Cut-off Date and all applications therefor and licenses thereof, all trade secrets, know-how, technical information, computer software, proprietary techniques and customer and supplier lists owned by Seller as of the Cut-off Date, and any other intangible property or rights owned by seller as of the Cut-off Date.

"*Other Assets*" means those assets of Seller which fall within the category of "Other Assets" on Seller's June 30, 1990 balance sheet and which are described in Exhibit 2.3(a)(vi).

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"*Property, Plant and Equipment*" means the Facility owned by either Seller or Shareholder as of the Cut-off Date and the Leaseholds and all furniture, fixtures, computers and other equipment owned by Seller as of the Cut-off Date, wherever located.

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"*Purchase Price*" means the aggregate purchase price to be paid by Buyer to Seller's Group for the Assets to be calculated as set forth in Section 2.3(a)

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"*Purchase Price/Seller's Assets*" means the portion of the Purchase Price allocated to Seller's Assets.

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"*Purchase Price/Shareholder's Assets*" means the portion of the Purchase Price allocated to Shareholder's Assets.

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"*RTC Guarantee Agreement*" means the Guarantee Agreement in the form of Exhibit 7.2(h).

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"*Seller*" means Empire of America Realty Credit Corp., a Michigan Corporation.

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"*Seller's Assets*" means all of the Assets except Shareholder's Assets.

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"*Seller's Group*" means Seller and Shareholder.

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> "*Shareholder's Assets*" means the Servicing Rights of Shareholder, all Servicing Agreements of Shareholder, and all Books and Records of Shareholder related thereto and the Facility if it is owned by Shareholder on the Cut-off Date.
>
> (Emphasis in original.)

6. The Division of Taxation ("Division") has never asserted that petitioner's *sales* were subject to the imposition of sales and use tax. The auditor's narrative included in his audit report notes that "All of the vendor's[3] sales were exempt mortgage banking related services." Nonetheless, in the summer of 1998, an audit was commenced of petitioner's *operating expenses* and *capital acquisitions* for the period consisting of just over five years, June 1, 1991 through November 30, 1996,[4] when petitioner operated its mortgage banking business in New York to ensure that sales and use tax was paid by petitioner on such expenses and capital acquisitions.

7. The year 1996 was selected, with petitioner's agreement, as a test year for its operating expenses. The auditor, after performing a detailed review of petitioner's operating expenses for this test year, determined that additional tax was due on its operating expenses for the test year. Such additional tax was projected for the entire audit period resulting in additional sales and use tax due of $14,874.20 plus interest, which petitioner has agreed to and is not at issue in this proceeding.

8. The auditor also performed a detailed review of petitioner's capital acquisitions and determined that sales and use tax totaling $78,367.05, plus interest, was due on such purchases.

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[3] The auditor's use of the term "vendor" to describe petitioner is incorrect since petitioner does not make sales of tangible personal property or services, the receipts from which are subject to sales tax (***see***, Tax Law § 1101[b][8]).

[4] In contrast, the period at issue in this proceeding ends August 31, 1995. The part of the audit which focused on petitioner's operating expenses ran to the end of petitioner's operation in New York in the fall of 1996. The Division's audit of petitioner's purchases of fixed assets did not result in the assertion of sales and use tax on any such purchases after the sales tax quarter ending August 31, 1995 which explains the shortened period at issue herein.

A Statement of Proposed Audit Change for Sales and Use Tax dated April 10, 2000 shows the allocation of the $78,367.05, which the auditor determined was due on petitioner's capital acquisitions, over the audit period as follows:

Period Ending Date	Tax Amount Asserted Due On Capital Acquisitions
08/31/1991	$70,824.16
11/30/1991	44.80
02/29/1992	94.87
05/31/1992	1,501.56
08/31/1992	120.00
11/30/1992	1,169.72
02/28/1993	49.54
05/31/1993	223.88
08/313/1993	0.00
11/30/1993	627.21
02/28/1994	2,897.39
05/31/1994	71.06
08/31/1994	0.00
11/30/1994	41.50
02/28/1995	448.80
05/31/1995	0.00
08/31/1995	252.56
11/30/1995	0.00
02/29/1996	0.00
05/31/1996	0.00
08/31/1996	0.00
11/30/1996	0.00

Total	$78,367.05

A Notice of Determination dated June 15, 2000, which corresponds to the above Statement of Proposed Audit Change for Sales and Use Tax, was issued against petitioner and asserts sales and use tax due of $78,367.05 for the period June 1, 1991 through August 31, 1995.

9. Petitioner has contested $68,565.15 of this total amount of $78,367.05 asserted due by the Division on the basis that its purchase of assets of the failed banking institution under receivership of the Resolution Trust Corporation was not properly subject to tax. The difference of just under $10,000.00, agreed to by petitioner, apparently represented sales and use tax due on its capital acquisitions made subsequent to its acquisition of the failed federal savings bank's mortgage banking business.

10. The auditor computed sales and use tax due on petitioner's capital acquisitions by performing a careful analysis of the company's net book value report dated January 19, 1996, which showed the fixed assets purchased by petitioner. This detailed report consisting of 35 pages showed (i) the purchase date or the "in service date," (ii) the original purchase price or "unadjusted basis," (iii) the current accumulated depreciation and (iv) the net book value of each particular fixed asset on petitioner's books. The total shown for "unadjusted basis" for the thousands of listed items was $2,991,024.38.

11. Petitioner contests the assertion of sales and use tax on the items placed "in-service" on July 1, 1991. A review of the hundreds of items listed in the net book value report discloses the following sample which notes the few items for which the "unadjusted basis" was in an amount greater than $10,000.00:

SYS no.[5]	Desc	In-svc date	Unadjusted basis	Thru date	Current accum depreciation	Net bk value
000090	Furniture	07/01/91	22,501.65	12/95	14,465.37	8,036.28
000094	Furniture	07/01/91	12,421.13	12/95	7,985.01	4,436.12
000103	Furniture	07/01/91	18,618.38	12/95	11,968.98	6,649.40
000113	Furniture	07/01/91	33,353.50	12/95	21,441.55	11,911.95
000114	Furniture	07/01/91	26,358.31	12/95	16,944.64	9,413.67
000120	Furniture	07/01/91	13,192.45	12/95	8,480.85	4,711.60
000121	Furniture	07/01/91	17,049.11	12/95	10,960.16	6,088.95
000122	Furniture	07/01/91	15,426.68	12/95	9,917.16	5,509.52
000123	Furniture	07/01/91	18,286.64	12/95	11,755.71	6,530.93
000588	Panels, Ch	07/01/91	13,131.14	11/95	8,285.12	4,846.02
000691	Office Fur	07/01/91	12,388.52	11/95	7,816.57	4,571.95

In addition to "furniture," other items listed in the report include computer equipment and software, printers, typewriters, telephones, and artwork.

SUMMARY OF THE PARTIES' POSITIONS

12. Petitioner contends that "Mortgages, Accounts Receivable, Assigned Contracts, Pipeline Commitments, etc. are clearly not services or property of a kind ordinarily sold by private persons" (Petitioner's brief, p. 8). Consequently, according to petitioner, under Tax Law § 1116(a)(2), the sale of the mortgage banking business to petitioner was not subject to sales and use tax because "RTC as receiver for Empire Federal was selling to Empire Acquisition the right to acquire certain but not all of the Assets of the [mortgage banking subsidiary], i.e., the origination, purchase, sale and servicing of mortgage loans" (Petitioner's brief, p. 6). In the

[5] Each of the thousands of items is referenced by a "SYS no." The column headings used above duplicate the actual abbreviations in the net book value report received into evidence.

alternative, petitioner argues that "even should the transaction be deemed subject to sales and compensating use tax, the audit and claim by the Department is time barred by Statute and the Financial Institutions Reform, Recovery and Enforcement Act of 1989" which strictly limits claims by creditors and gives the Resolution Trust Corporation the power to disallow claims not made in a timely fashion. The current ownership of petitioner, which did not own petitioner at the time of the transaction at issue, objects to the Division's proceeding against it since "5 years transpired between the initial transaction and the stock purchase by [the current owners of] petitioner" (Petitioner's brief, p. 13). In its reply brief, petitioner rejects the Division's contention that the mortgage banking subsidiary was the "seller": "Although [the mortgage banking subsidiary] is listed as the seller, it, as wholly owned subsidiary of Empire Federal has no right to sell itself" (Petitioner's reply brief, p. 4). Petitioner maintains that the Resolution Trust Corporation is the party in interest, and "there is no sales tax due as a result of Federal Preemption" (Petitioner's reply brief, p. 4).

13. The Division counters that the Resolution Trust Corporation was not the seller of the tangible personal property at issue, and consequently "*The tangible personal property at issue would not be exempt from sales tax under Tax Law § 1116(a)(2)*" (Division's brief, p. 11; emphasis in original). It also rejects petitioner's position, which it considers a "tortured" reading of the 1991 contract, that tangible personal property was not part of the sale. Further, the Division maintains that the sales tax liability arising from the 1991 transaction at issue survived the sale of the mortgage banking business to Midcoast Mortgage Corporation in 1996. Further, the audit methodology used was reasonable especially in light of the fact that the 1991 contract was not provided to the Division until the hearing and "even if the 1991 contract was available on audit, it does not provide an allocation of the purchase price between the tangible personal

property sold and the other assets sold" (Division's brief, p. 19). According to the Division, pursuant to Tax Law § 1133(b), petitioner was liable for sales and use tax which was not paid to the State by the seller, i.e., the mortgage banking subsidiary of the failed federal savings bank.

CONCLUSIONS OF LAW

A. Tax Law § 1141(c) provides in pertinent part:

> Whenever *a person required to collect tax* shall make a sale, transfer or assignment in bulk of any part or the whole of his business assets, otherwise than in the ordinary course of business, the purchaser, transferee or assignee shall at least ten days before taking possession of the subject of said sale . . . notify the tax commission by registered mail of the proposed sale . . . . (Emphasis added.)

Petitioner may not be deemed liable for the taxes in dispute as a *bulk sale purchaser* under the above cited provision. The sale of the fixed assets at issue to petitioner's prior owners by the mortgage banking subsidiary of the failed federal savings bank may not be subjected to the bulk sales treatment specified at Tax Law § 1141(c) (***see***, ***Matter of Great South Bay Delicatessen, Inc.***, Tax Appeals Tribunal, July 5, 1990 [wherein the Tribunal discusses the purpose and scope of this statutory provision]). Most important, as noted in Finding of Fact "6", the Division concurs that revenues from mortgage banking related services are not subject to sales and use tax. Consequently, the State did not require any time to determine whether there were any sales and use taxes due from the seller of the mortgage banking business since such business did not provide services subject to sales and use tax. Nor was the State's ability to collect the seller's liability for taxable sales and services from the consideration being paid for the assets of the business at issue since the seller had no such sales and services subject to tax. In short, the liability at issue is not that of a purchaser in a bulk sale because the seller in the transaction at issue was simply not "a person required to collect tax" as an operator of a mortgage banking business.

B. However, it is concluded that petitioner may yet be deemed liable for the taxes in dispute under the Tax Law provisions in Article 28 which impose a compensating use tax[6] (***cf.***, ***Matter of Fannon & Osmond Photography***, Tax Appeals Tribunal, July 19, 1990, ***confirmed*** 176 AD2d 1014, 574 NYS2d 866, ***lv denied*** 79 NY2d 759, 584 NYS2d 447). Initially, it is noted that Tax Law § 1105(a) imposes a sales tax on the receipts from *every retail sale of tangible personal property*, except as otherwise provided in the sales and use tax article. In turn, Tax Law § 1101(b)(4)(i) defines very broadly, in relevant part, a retail sale as "A sale of tangible personal property to any person for any purpose . . . ." Finally, a compensating use tax is imposed by Tax Law § 1110 which provides as follows:

> Except to the extent that property or services have already been or will be subject to the sales tax under this article, there is hereby imposed on every person a use tax for the use within this state . . . (A) of any tangible personal property purchased at retail . . . .

C. There is no doubt that the sale by the mortgage banking subsidiary of the failed federal savings bank to petitioner's prior owners of the fixed assets detailed in Finding of Fact "11" constituted the "sale of tangible personal property to any person for any purpose" or a "retail sale" for purposes of the Tax Law. Since this sale of fixed assets has not already been subject to the sales tax, a use tax for the use of such assets within New York may properly be imposed on petitioner (***see***, ***Matter of Datascope Corporation***, Tax Appeals Tribunal, August 8, 1992, ***confirmed*** 196 AD2d 35, 608 NYS2d 562; ***cf., Matter of WIXT-TV, Inc.***, Tax Appeals Tribunal, August 2, 1990 [wherein, the Tribunal noted that the purchaser was liable not only as a bulk sale

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[6] An administrative law judge may properly address legal issues raised by the facts although the parties did not identify them (***Matter of Chamberlin***, Tax Appeals Tribunal, January 30, 1992). Here, although neither party identified the use tax provisions of the Tax Law as a basis for analyzing the liability at issue, since the facts raise such matter, it has been addressed.

purchaser but because receipts from the sale of tangible personal property are generally subject to tax]).

D. Petitioner's frustration at the imposition of the tax at issue (i) at such a late date and (ii) as the result of a failure to pay tax by its *prior owners* over whom it had no authority is understandable. Further, petitioner's surprise that the well-reputed law firm which represented its prior owners in the transaction at issue would somehow not realize that sales and use tax would be due on the acquisition of the fixed assets can be appreciated especially given the esoteric nature of the Tax Law and the minor liability at issue in relation to the multi-million dollar nature of the underlying transaction. Nonetheless, the Division has broad discretion to impose use tax as detailed in Conclusion of Law "B", and the record contains absolutely no evidence that the Division has selectively enforced the imposition of use tax on petitioner (***cf.***, ***Matter of Goetz Energy***, Tax Appeals Tribunal, November 18, 1999). Rather, as reflected in Finding of Fact "6", the Division conducted an audit of the operating expenses and capital acquisitions of the substantial New York operation of petitioner under its prior owners in its regular course. Moreover, as noted in Finding of Fact "9", petitioner has agreed to liability for sales and use tax in an amount just under $10,000.00 on fixed assets acquired after the transaction at issue, which shows recognition that the acquisition of fixed assets which have not already been subject to sales tax, may yet be subject to tax for their use within New York.

E. Finally, turning to petitioner's various arguments, it is concluded that they are without merit. It has not established the affirmative defense of statute of limitations (***see, Matter of Pittman***, Tax Appeals Tribunal, February 20, 1992). Notably, since no sales and use tax return was ever filed by petitioner's prior owners, this defense would be impossible to sustain since the period of limitations never began to run (***see, Matter of East End Student Transportation Corp.***,

Tax Appeals Tribunal, March 26, 1992). Consequently, its complaint that the Division has sought to impose tax for a transaction now nearly 12 years old on new owners of the buyer involved in the transaction at issue provides no basis for relief. Further, its argument that the Division failed to properly proceed in asserting a claim with the Resolution Trust Corporation as required by applicable Federal law is specious given the fact that the "seller" for purposes of the transaction at issue, as detailed in Finding of Fact "5", was by definition "Empire of America Realty Credit Corp., a Michigan Corporation" not the Resolution Trust Corporation. As also noted in Finding of Fact "5", the Resolution Trust Corporation was the "receiver," not the "seller." Petitioner's contention that "Although [the mortgage banking subsidiary] is listed as the seller, it, as wholly owned subsidiary of Empire Federal has no right to sell itself" ignores the form of the transaction at issue. It is a well-established principle that a taxpayer's ability to challenge the form of a transaction as devoid of economic reality is strictly limited (***see, Matter of Gropper***, Tax Appeals Tribunal, December 19, 2002). Consequently, Tax Law § 1116(a)(2) which sets forth an exemption from sales and use tax for the United States and its agencies and instrumentalities is inapposite. Finally, the Division is correct that petitioner's position that tangible personal property was not part of the sale is based upon a "tortured" reading of the 1991 contract. The provision focused upon by petitioner merely excluded personal property affixed or attached to realty from the sale. As noted in Finding of Fact "5", the "assets" purchased pursuant to the 1991 contract clearly included the items delineated in Finding of Fact "11".

F. The petition of Empire of America Realty Credit Corp. is denied, and the Notice of Determination dated June 15, 2000 is sustained.

DATED: Troy, New York
March 20, 2003

/s/ Frank W. Barrie
ADMINISTRATIVE LAW JUDGE