NEW YORK CITY TAX APPEALS TRIBUNAL

In the Matter of VESTRY ACQUISITION LLC Petitioner.	DECISION TAT (E) 15-14(RP)

On March 6, 2017, Vestry Acquisition LLC (Petitioner) filed an exception to a Determination of an Administrative Law Judge (ALJ) dated February 7, 2017 (ALJ Determination). The ALJ Determination sustained a Notice of Determination (Notice) asserting New York City Real Property Transfer Tax (RPTT) on the transaction described below except to the extent of the late payment penalty asserted in the Notice, which was abated.

Petitioner was represented by Bob G. Goldberg, Esq., of Meister Seelig & Fein, LLP. The Commissioner of Finance of the City of New York was represented by Amy H. Bassett, Esq., Senior Counsel, New York City Law Department. Under 20 RCNY §1-09(f), Tribunal Rules of Practice and Procedure, the Parties agreed to have this matter determined by the ALJ on submission without the need for appearance at a hearing. The Parties submitted Stipulated Facts and Exhibits.[1] The Parties did not file briefs with the Appeals Division of the Tribunal, choosing to rely on the briefs filed with the ALJ. Neither Party, nor the Tribunal Commissioners, requested oral argument.

On November 21, 2002, Harlan Waksal (Waksal), Charles Dunne (Dunne), and Andreas Kaubisch (Kaubisch) formed Petitioner as a limited liability company under the

[1] Although the Parties submitted Stipulated Facts on December 21, 2015, the Parties merely stipulated to the authenticity of the various documents and, apart from the procedural facts of the matter, did not stipulate to any of the facts directly related to the transaction at issue.

laws of the State of Delaware.[2] On November 22, 2002, Petitioner became authorized to conduct business in the State of New York. Petitioner was the sponsor of a condominium development at 31-33 Vestry Street in New York City, New York 10013 (Condominium). Petitioner's operations were controlled by the LLC Agreement of Vestry Acquisition LLC (Agreement) among Waksal, Dunne, and Kaubisch dated as of November 20, 2002.[3]

Exhibit A to the Agreement lists each member's initial cash capital contribution and Percentages[4] in Petitioner as follows:

Waksal	$275,000.00	50%
Dunne	$137,500.00	25%
Kaubisch	$137,500.00	25%

Section 4.2 of the Agreement provides that, after certain special allocations, losses are to be allocated to the members according to their Percentages. Profits are allocated first in proportion to losses, then up to an amount equal to each member's "cumulative Preferred Returns",[5] then to Waksal up to the amount of his "Special Priority Return"[6] and thereafter according to their Percentages. Section 4.1 of the Agreement provides that distributions, regardless of source, are to be made first to members in proportion to their "cumulative Preferred Returns", then in proportion to their Adjusted Capital Contributions until they have received a return of those amounts, then to Waksal until he has received his "Special Priority Return" and thereafter in accordance with their Percentages.

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[2] Except as otherwise noted, the ALJ's Findings of Fact, although paraphrased and amplified herein, generally are adopted for purposes of this Decision. Certain Findings of Fact not necessary to this Decision have not been restated and can be found in the ALJ Determination.

[3] Stipulation, Ex F.

[4] All terms not otherwise defined in this Decision are as defined in the Agreement.

[5] These amounts represent an annual 7.5% return on each member's unreturned capital contributions. Agreement §I, DEFINED TERMS.

[6] This amount is defined as $1,000,000. *Id.*

Section 4.1.2 of the Agreement provides that, among other interests and rights, each member of Petitioner is entitled to receive a distribution of one or more condominium units, specifically:

> "*Notwithstanding any other provision hereof*, each Interest Holder shall have an option to receive a distribution of one or more condominium units for personal or investment use, if any are created by [Petitioner], provided all other Interest Holders receive equivalent pro rata distributions of cash or property in proportion to their Percentages." (Emphasis added.)

We note that this provision clearly indicates that the distribution of units is to be according to the members' Percentages regardless of any other provision governing distributions.

Section VI of the Agreement outlines the procedures and conditions for transferring a member's interest or rights in Petitioner. Section 6.1.1 of the Agreement provides seven conditions that must be met for a transfer to be given effect by Petitioner. Those requirements include approval by all of the other members (Agreement § 6.1.1.67 [sic]) and compliance with the "Right of First Offer" provision of the Agreement contained in §6.1.4 (Agreement §6.1.1.6).

Under the "Right of First Offer" provision in §6.1.4 of the Agreement, if a holder of an interest in Petitioner wants to transfer "all or any portion of, or any interest or rights in"[7] his interest in Petitioner (selling member), he must notify the other members of Petitioner and the other members then have the option to purchase that portion of the selling member's interest being offered. The price is to be established by appraisal as described in §6.4 of the Agreement. The first offer option must stay open for 30 days from the date the selling member gives notice of his intent to transfer his interest. If no other member exercises the right of first offer, the selling member has 90 days to transfer

[7] Agreement §6.1.4.1.

his interest to an outside person at no less than the established price. Any transfer after that 90-day period is "null and void". Section 6.1.3 of the Agreement further provides:

> "Each Member hereby acknowledges the reasonableness of the prohibition contained in this Section 6.1 in view of the purposes of the Company and the relationship of the Members. The Transfer of any Membership Rights or Interests in violation of the prohibition contained in this Section 6.1 shall be deemed invalid, null and void, and of no force or effect. Any Person to whom Membership Rights are attempted to be transferred in violation of this Section shall not be entitled to vote on matters coming before the Members, participate in the management of the Company, receive distributions from the Company, or have any other rights in or with respect to the Membership Rights."

Section 9.5 of the Agreement provides:

> "This Agreement constitutes the complete and exclusive statement of the agreement among the Members. It supersedes all prior written and oral statements, including any prior representation, statement, condition, or warranty. Except as expressly provided otherwise herein, this Agreement may not be amended without the written consent of all of the Members."

The Condominium contained seven condominium units. By 2012, five of the seven units had been sold, leaving only two remaining units.

Petitioner submitted a copy of a September 5, 2006 letter from Kaubisch to Dunne (2006 Letter)[8] indicating that the two reached an agreement regarding the exercise of their rights to acquire units in the Condominium. The 2006 Letter provides:

> "Reference is hereby made to that certain LLC Agreement of Vestry Acquisition LLC (the 'Vestry Agreement') dated as of the 20th day of November, 2002. All terms not otherwise defined herein shall have the meanings assigned to them in the Vestry Agreement.
>
> "As previously agreed, in connection with the potential development of a building (the 'Vestry Building') to be

[8] Stipulation, Ex. K.

> located at 31-33 Vestry Street, New York, New York, you and I may collectively have the right to retain one residential unit at the Vestry Building (the 'Retained Vestry Unit').
>
> "This letter shall confirm that in consideration for one dollar and other good and valuable consideration, the receipt of which is hereby acknowledged, I hereby relinquish any right I might have to the Retained Vestry Unit to you. As a consequence of such relinquishment, my proportionate share of any additional Capital Contribution required in accordance with Section 3.2.1 of the Vestry Agreement shall be reduced by a fraction, the numerator of which shall be fifty percent (50%) of the square footage of the Retained Vestry Unit, and the denominator of which shall be the square footage of the Vestry Building, all as finally determined. Consequently, your proportionate share of any Capital Contribution required in accordance with Section 3.2.1 of the Vestry Agreement shall be increased by like amount."

The 2006 Letter is signed by Kaubisch and is countersigned by Dunne beneath a line stating "Agreed and Accepted". The record does not indicate whether Kaubisch and Dunne advised Waksal of this arrangement or complied with any of the other terms of the Agreement regarding transfers of interests in Petitioner or amending the Agreement. The record also contains no information regarding the amount paid as consideration for the transfer of Kaubisch's right to receive a distribution of a unit including whether Dunne was required to make an additional capital contribution under §3.2.1 of the Agreement referred to in the 2006 Letter.

On March 27, 2012, Petitioner distributed a condominium unit to Dunne for total consideration of $10,000,000.[9] On April 4, 2012, a RPTT return was filed reflecting the transfer, showing tax due of $71,250.00 on taxable consideration of $5,000,000 (RPTT

[9] While the ALJ Determination states that in 2012, Dunne exercised his rights under §4.1.2 of the Agreement to receive a distribution of a unit in the Condominium, nothing in the record specifically indicates that the March 27, 2012 transfer of a condominium unit to Dunne was made under that provision of the Agreement. We note that §4.1.2 provides that the "designation of condominium units pursuant to this option shall be made *prior to the commencement of any sales or marketing activities* . . . with respect to any condominium units." (Emphasis added.) The transfer at issue took place after all but two of the units were sold and nothing in the record indicates that the unit transferred to Dunne in 2012 was designated in any way consistent with §4.1.2 of the Agreement.

Return). The RPTT Return reported the transaction as 50% exempt as a mere change of ownership.[10] Petitioner paid the reported $71,250 RPTT shown due.

Respondent audited the RPTT Return and issued the Notice asserting additional RPTT due of $35,625 plus interest and a late payment penalty on the grounds that the transaction was only exempt to the extent of 25%.

Petitioner contends that the 2006 Letter modified the Agreement such that only two of the members of Petitioner, Dunne and Waksal, had the right to receive distributions of condominium units and therefore, Dunne's interest in the condominium units to be distributed was increased from 25% to 50% prior to the distribution of the condominium unit to him in 2012. Alternatively, Petitioner asserts that Dunne's beneficial interest in Petitioner for purposes of the exemption was greater than 50% after taking into account Dunne's share of profits, losses and distributions.

Respondent contends that under the Agreement, Dunne's Percentage in Petitioner was 25% and, therefore, the distribution of the condominium unit was eligible only for a mere change of form exemption to the extent of 25%. Respondent argues that the 2006 Letter did not amend the Agreement to increase Dunne's interest in Petitioner or in the condominium unit.

For the following reasons, the ALJ Determination is affirmed and the Notice sustained except to the extent of the penalty asserted therein.[11]

Section 11-2102 of the Administrative Code of the City of New York (Administrative Code) imposes RPTT on all transfers of real property where the consideration is in excess of $25,000. However, Administrative Code §11-2106.b.8 exempts transfers from RPTT to the extent that the beneficial ownership of the real property or economic interest therein remains the same.

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[10] The RPTT exemption provided for in Administrative Code §11-2106.b.8 described more fully below is commonly referred to as the "mere change of form" exemption.

[11] Respondent did not file a cross-exception disputing the ALJ's abatement of the late payment penalty and, therefore, we do not address the issue of penalties further.

Administrative Code §11-2103 provides that all transfers and deeds are presumed to be subject to tax and the burden is on the taxpayer to prove that the presumption does not apply. This provision is consistent with the general principle that tax exemptions exist as matters of legislative grace *(Matter of Grace v New York State Tax Commn.,* 37 NY2d 193, 196 [1975]). Thus Petitioner bears the burden of establishing that the transaction at issue is entitled to an exemption under Administrative Code §11-2106.b.8 in excess of 25%.

Section 4.2.1 of the Agreement states that members are entitled to distributions of condominium units, provided all members receive equivalent distributions of cash or property, in proportion to their Percentages. Exhibit A to the Agreement reports the members' Percentages as 50% for Waksal and 25% each for Dunne and Kaubisch. Petitioner asserts that the 2006 Letter amended the Agreement to increase Dunne's interest in the condominium units to be distributed from 25% to 50% and correspondingly reduced Kaubisch's interest in the units to 0%. However, the Agreement contains clear and unambiguous provisions governing transfers of interests in Petitioner and governing amendments to the Agreement. Nothing in the record indicates that the 2006 Letter satisfied any of the requirements for amending the Agreement or that the requirements of §6.1 of the Agreement governing transfers of interests in Petitioner were met.

Section 6.1.4.7 of the Agreement states that a transfer of any portion of a member's interest or rights in Petitioner "without strict compliance with the terms, provisions, and conditions of this Section and other terms, provisions and conditions of this Agreement, shall be null, void, and of no force or effect." The 2011 federal income tax return for Petitioner, Form 1065, Schedule K-1 (Partner's Share of Income, Deductions, Credits, etc.) for Kaubisch lists his interest in profits and losses as zero but his interest in capital as 25%. Dunne's 2011 Form 1065, Schedule K-1 shows his interest in profits and losses as 100% and his interest in capital as 25%. Waksal's 2011 Form 1065, Schedule K-1 shows his interest in profits and losses as zero and his interest in

capital as 50%. The 2012 Form 1065, Schedules K-1 for the members of Petitioner show the same percentage interests in profits, losses and capital as were reported for 2011.

The capital accounts of the members at the beginning of 2011 as reported on the Form 1065, Schedules K-1 totaled $3,512,757 of which Dunne's share was $878,190, or about 25%. The capital accounts of the members at the end of 2011 as reported on the Form 1065, Schedules K-1 totaled $4,618,088 of which Dunne's share was $1,887,274 or approximately 41%. The capital accounts of the members at the end of 2012 totaled $516,555 of which Dunne's share was $17,307 or less than 4%. None of the federal forms 1065 of Petitioner for 2006, the year when the purported transfer between Dunne and Kaubisch occurred, or for any of the years 2007 through 2010 or after 2012, were submitted.

As noted above, §4.2.1 of the Agreement providing for the distribution of units to the members requires the distributions to be in accordance with each member's Percentage regardless of any contrary provision of the Agreement. The federal Forms 1065, Schedules K-1 report the members' interests in the capital of Petitioner for 2011 and 2012 to be consistent with Exhibit A to the Agreement. Petitioner argues that the 2006 Letter resulted in an increase in Dunne's Percentage in the condominium units to be distributed from 25% to 50%. However, nothing in the record suggests that the members' Percentages in 2012 were other than as described in Exhibit A to the Agreement.

Petitioner argues in the alternative that Dunne's beneficial interest in Petitioner for purposes of Administrative Code §11-2106.b.8 was greater than 50% at the time of the distribution of the condominium unit in 2012. As noted above, Petitioner bears the burden of establishing that Dunne's beneficial interest in Petitioner was greater than 25% before the transfer. Beneficial ownership is broadly defined as the difference between the economic interest prior and subsequent to the transfer and will be determined based on the facts and circumstances of a transfer (Administrative Code §11-2106.b.8; 19 RCNY §23-05[b][8]). Petitioner's 2011 Form 1065 reports $599,072 of gain all of which is

allocated to Dunne. The 2012 Form 1065 of Petitioner reports $46,878 of interest income, of which 50% is allocated to each of Dunne and Waksal, and a net "section 1231" loss of $6,132 all of which is allocated to Dunne. In its brief, Petitioner argues that all of the gain on the sale of the remaining two condominium units would have been allocated to Dunne increasing his capital account to greater than 50% of the total. However, Dunne's capital account at the end of 2011 was about 41% of the total and at end of 2012 was less than 4% of the total.[12] Petitioner opted to proceed on this matter without a hearing and, therefore, without any testimony from the individuals involved. Nor were any affidavits or copies of Petitioner's federal tax returns for the years 2006 through 2010 or years after 2012 submitted.

The 2012 Form 1065 of Petitioner reports a loss, rather than a gain, on a March 27 "sale of apartments", which would appear to include the transfer at issue. That loss was allocated to Dunne as noted above. The reporting of that transaction conflicts with the statements in Petitioner's brief regarding the allocation of gain on the sale of the remaining units.

Based on the foregoing, we conclude that Petitioner has not met its burden of proof as to whether Dunne's beneficial interest in Petitioner was greater than 25% at the time of the transfer.

Therefore, the ALJ Determination is affirmed and the Notice sustained except as to the penalty asserted therein.[13] Commissioner Frances J. Henn did not participate in this decision.

Dated: December 1, 2017
New York, NY

/s/
Ellen E. Hoffman
President and Commissioner

/s/
Robert J. Firestone
Commissioner

[12] Brief of Petitioner at 11.
[13] We have considered all of the other arguments of the Parties and find them unpersuasive.