

**New York State Department of Taxation and Finance**  
**Taxpayer Services Division**  
**Technical Services Bureau**

TSB-A-96 (12) R  
Real Estate  
Transfer Tax  
Gains Tax  
September 18, 1996

STATE OF NEW YORK  
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. M960426A

On April 25, 1996 the Department of Taxation and Finance received a Petition for Advisory Opinion from Metropolitan Life Insurance Company, 1 Madison Avenue, New York, New York 10010.

The issues raised by Petitioner, Metropolitan Life Insurance Company, are:

1. Whether the conveyance and transfer of certain condominium units by Petitioner to the New York City Industrial Development Agency (the "IDA") are subject to the Real Estate Transfer Tax imposed by Article 31 of the Tax Law (the "transfer tax") and the Real Property Transfer Gains Tax formerly imposed by Article 31-B of the Tax Law (the "gains tax").
2. Whether the reversion or reconveyance of the same condominium units by the IDA to the Petitioner are subject to the transfer tax and the gains tax.
3. Whether the creation or termination of the Overlease, creation of the Prime Lease or the addition or deletion of the additional Units in the IDA Units under either the Overlease or the Prime Lease is subject to the transfer tax and the gains tax.

Petitioner submits the following facts as the basis for this Advisory opinion.

Petitioner is currently the fee owner of the premises known as 11 Madison Avenue (the "Building"), in the Borough of Manhattan, block #854, lot #1. Petitioner has been advised that, pursuant to a resolution adopted by the IDA, certain economic development benefits were authorized in order to induce CS First Boston Corporation (the "Company") to retain its offices in New York City (the "City"). The IDA has agreed to participate in the transaction described herein and to confer tax benefits upon the Company and certain of its affiliates (the "Company Group") in order to reduce the Company's costs of operating and maintaining its City offices and in order to help finance the Company Group's cost of acquiring equipment and leasehold improvements (the "IDA Benefits"). The Company has entered into various agreements with the IDA in order to facilitate these transactions.

In order to secure certain IDA Benefits the IDA must have a legal ownership interest in the property benefitted. Accordingly, as an accommodation to the Company, the Building has been converted into a condominium and Petitioner has conveyed title to those units representing the portion of the Building that the Company will occupy (the "IDA Units") to the IDA for a nominal amount. Title to the IDA Units will automatically revert back to Petitioner on the earlier of

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December 31, 2016, or when the benefits being afforded to the Company, or any of the related financing leases or subleases entered into among the Company Group, and the IDA, terminate.

Simultaneously with the conveyance by Petitioner of the IDA Units to the IDA, the IDA leased the IDA Units back to Petitioner for a nominal rent pursuant to a lease agreement between the IDA and Petitioner (the "Overlease"). The term of the Overlease will be coextensive with the term of the IDA's title to the IDA Units.

While the IDA holds record title to the IDA Units, the Overlease contemplates, and the parties to the transaction intend, that Petitioner is the beneficial owner of the IDA Units. Under the terms of the conveyance and the Overlease, Petitioner is entitled to all of the benefits and bears all of the burdens of ownership of the IDA Units. Under the Overlease, the IDA has no obligation to improve, replace, service, adjust, repair, or maintain any portion of the IDA Units. Moreover, Petitioner and the Company agreed (pursuant to and in accordance with separate agreements with the IDA) to indemnify the IDA and its directors, officers and employees for liabilities arising from the operation of the IDA Units. Petitioner, as the beneficial owner of the IDA Units, will have the right in its own name to initiate contests regarding legal requirements applicable to the IDA Units.

The IDA has no beneficial interest in the IDA Units. The Overlease provides that the IDA will have no interest in any condemnation awards with respect to the IDA Units or any proceeds from insurance maintained by Petitioner or the Company; as between the IDA and Petitioner all condemnation awards or insurance proceeds will be the sole property of Petitioner.

Petitioner has the right to sell or otherwise transfer the IDA Units. Petitioner may assign or transfer its interest in the Overlease, subject to then existing tenancies and subtenancies, provided that (1) Petitioner transfers all its interests in the IDA Units including any reversionary interests; (2) notice is given to the IDA of the assignment and transfer and the identity of the transferee or assignee; and (3) the assignee or transferee certifies that it is not among the groups proscribed from entering into transactions with the IDA. Petitioner may also mortgage its interest in the IDA Units and the Overlease. The Overlease contemplates that at Petitioner's request the IDA will subject its title to the IDA Units to any such mortgage, subject to certain restrictions. The IDA will not have the right to sell, assign, convey, lease, mortgage, or otherwise transfer or encumber its title to the IDA Units without Petitioner's prior written consent. Any attempt by the IDA to dispose of the IDA Units without Petitioner's prior written consent will be void.

In the Declaration of Condominium filed in connection with the conversion of the Building to a condominium form of ownership, "Unit Owner" is defined as the person or persons owning the fee simple interest in any Unit and the common interest appurtenant thereto, except that for any period during which record title to any unit is held by the IDA and leased by it to the Petitioner pursuant to the Overlease the owner of such unit is for all purposes deemed to be the Petitioner.

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Therefore, Petitioner will be the "owner" of the IDA Units for all purposes of the Condominium's by-laws. Petitioner also has the right to make any alterations, additions, installations improvements and substitutions to the IDA Units, provided that the same are made in compliance with law.

Petitioner has leased the premises that will comprise the IDA Units to the Company pursuant to a lease agreement dated as of July 28, 1995 (the "Prime Lease"). Pursuant to the Prime Lease, Petitioner has granted the Company the right to lease additional space in the Building. (All space leased from time to time by Petitioner to the Company under the Prime Lease is referred to as the "Project Premises".) Under the Prime Lease, Petitioner has granted the Company the right to use and occupy the Project Premises for a period that for certain space at the Project Premises is up to twenty years. The Company has three renewal options under which the Company can add up to fifteen years to the lease term with respect to certain space at the Project Premises. The exercise of these renewal options will not prolong the IDA's legal title to the IDA Units. The Overlease states that the IDA is deemed not to have assumed, or be responsible for, any obligations of the Company under the Prime Lease.

The Prime Lease defines "rent" as including fixed rent and additional rent. Fixed rent is an amount specified in the Prime Lease. Petitioner has been advised by its financial advisors that the fixed rent represents the fair market rental value of the Project Premises. During a renewal term, fixed rent will be either set by agreement between Petitioner and the Company or based on the results of an appraisal process provided for in the Prime Lease. Additional rent generally includes operating expenses and taxes, including real estate taxes and special additional rent. The failure of the Company to pay fixed or additional rent constitutes an event of default under the Prime Lease.

From and thereafter the applicable rent commencement date specified in the Prime Lease and until such time that a condominium unit subject to the Prime Lease becomes an IDA Unit and becomes exempt from the New York City Real Property Tax under Section 874 of the New York General Municipal Law and Section 412-a of the New York Real Property Tax Law, the Company will pay the real estate taxes attributable to that unit. Thereafter, as is customary in such arrangements, the Company will make payments in lieu of real estate taxes ("Pilots") under a separate agreement with the IDA (the "Pilot Agreement"). Petitioner has been advised by the Company that the amount of each Pilot will be equal to the lesser of (i) scheduled amounts agreed to between the IDA and the Company, or (ii) the amount of real estate taxes that would have been payable on the IDA Units were they not exempt from those taxes. Petitioner has been further advised by the Company that the Company must make Pilots to a trustee (the "Pilot Trustee") by the date when property taxes must be paid to the City. The Company's obligation under the Pilot Agreement to make Pilots will be secured by a form of security acceptable to the IDA. The Company's payment of Pilots to the Pilot Trustee is not fixed or additional rent under the Prime Lease, and the Company's

failure to make these payments is not an event of default, nor does it otherwise affect the Company's right to use or occupy the Project Premises, under the Prime Lease.

Petitioner has been advised that the IDA will provide certain financial benefits to the Company Group. In order to provide these benefits, Petitioner has been informed that it is necessary for the IDA to acquire a leasehold interest in the Project Premises. Accordingly, the Company has sub-subleased the Company's leasehold interest in the Project Premises to the IDA for a nominal rent (the "Facility Lease"). The IDA, in turn, sub-sub-subleased the Project Premises, together with improvements thereto and certain equipment, to designated agents with the Company Group (the "Financing Lease"). (Designated agents within the Company Group must be used for sales tax reasons; those designated agents are referred to herein as "Group Agents".) The Facility Lease and the Financing Lease will terminate approximately four months before the expiration of the initial term of the Prime Lease. The cost of certain improvements and equipment to be installed by the Company in the Project Premises will be financed by Bonds issued by the IDA. The amount of rent that the Company Group will pay under the Financing Lease will equal the amount of interest on, and principal of, the Bonds.

Petitioner has been advised that the Company has generally agreed to indemnify the IDA, the Trustee, and other parties for liabilities arising out of the Financing Lease and related agreements and to pay the Trustee's expenses to the extent that they are not paid out of the proceeds of the Bonds. The Company must pay operating costs and maintain, repair, and insure the Project Premises at its own expense, subject to the terms of the Financing Lease. If the Project Premises are destroyed or condemned, the Company need not replace them but the Group Agents must continue to pay rent under the Financing Lease.

The Group Agents can terminate the Financing Lease early by paying an amount sufficient to retire all outstanding Bonds. In that event, the Facility Lease, the Pilot Agreement, and the Overlease will also terminate and formal legal title to the IDA Units will automatically revert to Petitioner.

Neither the Facility Lease, the Financing Lease, the Overlease, nor the conveyance of the IDA Units to the IDA will affect the Company's obligations to Petitioner pursuant to and in accordance with the Prime Lease and each of the Facility Lease and the Financing Lease are subject and subordinate to the Overlease.

Petitioner represents that for financial reporting and federal, state, and local income tax purposes, it will be the owner of the IDA Units for as long as it holds a leasehold position under the Overlease and a reversionary interest in the Units.

All transactions described herein, except for the reversion of the condominium units by the IDA to the Petitioner and the termination of the Overlease, occurred prior to June 15, 1996.

Section 1402 of the Tax Law imposes the transfer tax on each conveyance of real property or interest therein at the time that the instrument effecting the conveyance is delivered by a grantor to a grantee when the consideration for the conveyance exceeds five hundred dollars.

Part 575 of 20 NYCRR (the transfer tax regulations) at Section 575.7 provides that the creation of a lease or sublease not coupled with an option to purchase constitutes a conveyance of an interest in real property only where:

- (1) the sum of the term of the lease or sublease and any options for renewal exceeds 49 years; and
- (2) substantial capital improvements are or may be made by or for the benefit of the leasee or sublessee; and
- (3) the lease or sublease is for substantially all of the premises constituting the real property. Substantially all means ninety percent or more of the total rentable space of the premises, exclusive of common areas ....

Also, Section 575.9(c) of the transfer tax regulations, provides in part as follows:

- (c) In addition to the exemptions described in subdivision (b) of this section, certain transactions are not subject to the real estate transfer tax. These include:
- (1) conveyances to any of the governmental organizations or entities described in subdivision (b) of this section, including any instrumentality or agency of the United Nations; ....

Also, Section 575.11 of the transfer tax regulations provides, in part, as follows:

- (a) The following are examples of conveyances which are subject to real estate transfer tax ....
- (13) A conveyance of real property to an industrial development agency (IDA) by a person who is not the beneficiary of the IDA financing, at the direction of such beneficiary, with such beneficiary subsequently leasing the property from the IDA, is subject to tax. In such a conveyance, the beneficiary of the IDA financing and not the IDA is deemed to be the grantee, and therefore the exemption described at section 575.9(c)(1) of this Part does not apply.

(14) A conveyance of real property by an IDA to a person who is not the beneficiary of the IDA financing where such conveyance is made at the direction of such beneficiary is subject to tax. In such a conveyance, the beneficiary of the IDA financing is deemed to be the grantor of the conveyance ....

(b) The following are examples of conveyances which are not subject to the real estate transfer tax.

(1) A conveyance of real property by the beneficiary of the industrial development agency (IDA) financing to the IDA, in connection with the receipt of such financing is not subject to tax.

(2) A conveyance of real property by the IDA, as grantor, to the beneficiary of the IDA financing, as grantee is not subject to tax.

Section 1441 of the Tax Law imposed the gains tax on the gain derived from the transfer of real property or an interest therein, where the real property or interest therein is located in New York State and where the consideration is \$1 million or more.

Chapter 309 of the Laws of 1996 repealed the gains tax for transfers of real property that occurred or occur on or after June 15, 1996.

Section 590.5(a) of the gains tax regulations provides that the creation of a lease or sublease is a transfer of an interest in real property, but only where:

(1) the sum of the term of the lease or sublease and any options for renewal exceeds 49 years;

(2) substantial capital improvements are or may be made by or for the benefit of the lessee or sublessee; and

(3) the lease or sublease is for substantially all of the premises constituting the real property. *Substantially all* is defined to mean 90 percent or more of the total rentable space of the premises, exclusive of common areas ....

Section 590.5(b) of the gains tax regulations sets forth that when the creation of a leasehold is coupled with the granting of an option to purchase the property, the transfer is taxable regardless of the term of the lease.

Section 590.68(a) of the gains tax regulations provides that when the company (the beneficiary of an industrial revenue bond financing) transfers fee title to the real property to the IDA solely for the purpose of receiving tax-exempt financing, and simultaneously leases such property back, upon which the company will construct an improvement, the company will be considered the owner of the project and there will not be a taxable event for gains tax purposes until the company



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transfers an interest in the land or building to a party other than the IDA. This is also true for ground leases/subleases or other similar transactions which are designed to facilitate industrial revenue bond financings.

However, in a situation where the IDA obtains the real property directly from a third party at the direction of the company and leases the property to the company, the transfer to the IDA will be subject to the gains tax if the consideration for the transfer is \$1 million or more.

The Chase Manhattan Bank. N.A., Adv Op Comm T&F, February 8, 1993, TSB-A-93(1.1)-R, and Resnick Water St. Development Co., Adv Op Comm T&F, January 12, 1993, TSB-A-93(2)-R, advised that while the petitioner was not the beneficiary of the IDA financing, the transfer of certain condominium units to the New York City Industrial Development Agency (the "IDA Units") would not result in a change in beneficial ownership since the petitioner retains all the benefits and burdens of ownership of the IDA Units, and therefore, the transfer of title to such IDA Units to the IDA would not be subject to the gains tax and the transfer tax. In addition, the opinions advised that the reversion of fee title to the IDA Units to the petitioner would not result in a change in beneficial interest and, therefore, would not be subject to the gains tax and the transfer tax. These opinions further advised that the creation of certain leases and leasebacks between the IDA and the petitioner and the petitioner and the bond financing recipient were not subject to the gains tax and the transfer tax. Also, see Stanley Stahl, Adv Op Comm T&F, June 26, 1995, TSB-A-95(5)-R.

Regarding issue "1", in accordance with Section 575.11 of the transfer tax regulations and Section 590.68(a) of the gains tax regulations, the conveyance and transfer of title to real property to an IDA for the purpose of obtaining IDA financing, when the grantor/transferor remains the beneficial owner of the property, are not subject to the transfer tax and the gains tax. Also, as set forth in The Chase Manhattan Bank. N.A., supra, Resnick Water St. Development Co., supra, and Stanley Stahl, supra, the conveyances and transfers of certain condominium units to the New York City Industrial Development Agency were deemed not to result in a change in beneficial ownership since the petitioner retained all the benefits and burdens of ownership of the IDA Units. In this case, while Petitioner is not the beneficiary of the IDA financing, the conveyance and transfer of the condominium unit(s) to the IDA does not result in a change in beneficial ownership since the Petitioner retains all the benefits and burdens of ownership of the IDA Unit(s). Accordingly, the conveyance and transfer of title to the condominium unit(s) to the IDA are not subject to the transfer tax and the gains tax.

With respect to issue "2", based on the provisions of Section 575.11 of the transfer tax regulations, The Chase Manhattan Bank. N.A., supra, St. Development Co., supra, and Stanley Stahl, supra, the reversion or reconveyance of an IDA unit(s) to Petitioner does not result in a change in beneficial interest, since Petitioner remains the beneficial owner of the condominium unit(s) after

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the conveyance of fee title to the IDA. Therefore, the reversion or reconveyance of IDA unit(s) to Petitioner will not be subject to transfer tax. Also, as the gains tax has been repealed for transfers of real property that occur on or after June 15, 1996, the gains tax will not be an issue with respect to such reversion or reconveyance.

Regarding issue "3", in accordance with Section 575.11 of the transfer tax regulations and Section 590.68(a) of the gains tax regulations, the leaseback of real property by an IDA to the beneficiary of the IDA financing is not subject to transfer tax and gains tax, since the beneficiary of the IDA financing remains the beneficial owner of the real property. In this case, while Petitioner is not the beneficiary of the IDA financing, Petitioner is the beneficial owner of the real property. Therefore, the creation of the Overlease, whether in connection with the addition or deletion of additional Units in the IDA Unit, is not subject to transfer tax and gains tax. The termination of the Overlease is not subject to the transfer tax pursuant to Section 575.11 of the transfer tax regulations. Since the gains tax has been repealed for transfers of real property that occur on or after June 15, 1996, the gains tax is not an issue with respect to the termination of the Overlease.

Also, based on the provisions of Section 575.7 of the transfer tax regulations and Section 590.5 of the gains tax regulations, the creation of the Prime Lease, in connection with the addition or deletion of additional Units in the IDA Units for a term of less than 49 years, including renewal periods, is not subject to transfer tax and gains tax.

DATED: September 18, 1996

/s/  
John W. Bartlett  
Deputy Director  
Technical Services Bureau

NOTE: The opinions expressed in Advisory Opinions  
are limited to the facts set forth therein.