

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

TSB-A-92(10)-R
Real Property
Transfer Gains Tax
December 28, 1992

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. M921021B

On October 21, 1992, a Petition for Advisory Opinion was received from Andrew Feiner, Esq. and William Korman, CPA, c/o Zellermayer, Gratch and Jacobs, P.C., 950 Third Avenue, New York, New York 10022.

The issue raised by Petitioner, Andrew Feiner, Esq. and William Korman, CPA, is what is the amount of consideration that should be allocated to real property upon the transfer of a controlling interest in Petitioner's client to Bank D for purposes of the Real Property Transfer Gains Tax (hereinafter the "gains tax").

Petitioner's client, a partnership, owns a leasehold interest in one commercial real estate site and a fee interest in another. The leasehold and fee interest presently have a combined appraised fair market value of \$10 million. In addition, Petitioner's client has a cash bank account that contains \$50,000. Several years ago, Bank D loaned \$15 million to Petitioner's client secured by a mortgage on the leasehold and fee interests in real property. Approximately two years ago, as part of a workout, Bank D received a further security interest in the cash account (by reason of lock-box security interest in the rent derived from the real property). In addition, A, B and C, the partners of Petitioner's client, personally guaranteed the interest and a portion of the principal of the bank debt owed to Bank D. In exchange for cancellation of the debt to Bank D and for release of the partners' guaranty of that debt, the partners will transfer all of their partnership interests in Petitioner's client to Bank D.

Section 1440.1 of the Tax Law defines the term "consideration" for purposes of gains tax to mean as follows:

1. (a) "Consideration" means the price paid or required to be paid for real property or any interest therein, less any customary brokerage fees related to the transfer if paid by the transferor, including payment for an option or contract to purchase or use real property. Consideration includes any price paid or required to be paid, whether expressed in a deed and whether paid or required to be paid by money, property, or any other thing of value and including the amount of any mortgage, purchase money mortgage, lien or other encumbrance, whether the underlying indebtedness is assumed or taken subject to. Consideration includes the cancellation or discharge of an indebtedness or obligation.

(b) In the case of (i) the granting of an option with use and occupancy of real property or (ii) the creation of a leasehold or sublease that is a transfer of real property, as defined in subdivision seven of this section, consideration shall also include the value of the rental and other payments attributable to the use and occupancy of the real property or interest therein and the value of any option to purchase or renew included in such transfer.

(c) In the case of a transfer which includes other assets which are in addition to real property or an interest therein and for which there is no reasonable apportionment of the consideration for such real property or interest, consideration means that portion of the total consideration which represents the fair market value of such real property or interest. In the case of a transfer of a controlling interest in an entity with an interest in real property, there shall be an apportionment of the fair market value of the interest in real property to the controlling interest for the purpose of ascertaining the consideration for the transfer of such controlling interest. (emphasis added)

Section 590.47 of the Gains Tax Regulations provides as follows:

590.47 Consideration [Tax Law, §1440(1)]

(a) Question: Is the price paid for the ownership interest in an entity the consideration for a controlling interest used to calculate gain?

Answer: Generally, no. Section 1440(1) of the Tax Law states that:

" ... there shall be an apportionment of the fair market value of the interest in real property to the controlling interest to ascertain the consideration for the controlling interest."

Example: A corporation's only asset is a \$4 million fair market value piece of property. If 100 percent of the stock is purchased, the consideration is \$4 million (\$4,000,000 x 100 percent). If a 50-percent interest were acquired, only \$2 million consideration is used to calculate gain.

(b) Questions: How is fair market value determined?

Answer: Generally, by appraisal. It is the amount a willing buyer would pay a willing seller for the real property. It is not net fair market value, which deducts mortgages on the property from fair market value.

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Thus, in the example in subdivision (a) of this section, if the property is encumbered by a \$3 million mortgage, and \$1 million is paid for 100 percent of the stock, the amount of consideration for the acquisition is \$4 million, not \$1 million.

Accordingly, pursuant to Section 1440.1 of the Tax Law and Section 590.47 of the Gains Tax Regulations the consideration for the transfer of a controlling interest in Petitioner's client to Bank D is an apportionment of the fair market value of the interest in real property to the controlling interest being transferred which in the instant case would be \$10 million dollars.

DATED: December 28, 1992

/s/
PAUL B. COBURN
Deputy Director
Taxpayer Services Division

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