

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

TSB-A-93 (1)R
Real Property
Transfer Gains Tax
Real Estate Transfer Tax
January 7, 1993

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. M921207B

On December 7, 1992, a Petition for Advisory Opinion was received from The Chase Manhattan Bank, N.A., Real Estate Resources, 4 Chase MetroTech Center, Brooklyn, New York 11245.

The issues raised by Petitioner, The Chase Manhattan Bank, N.A., are:

1. Whether the conveyance of title to a condominium unit or units by Petitioner to the New York City Industrial Development Agency in connection with the Original Conveyance, in connection with a new conveyance following a Pre-Date Termination, in connection with Prudential Securities Incorporated and affiliate (hereinafter "Prudential") lease of additional space or any similar conveyance, will be subject to New York State Real Property Transfer Gains Tax (hereinafter the "gains tax") or New York State Real Estate Transfer Tax (hereinafter the "transfer tax").

2. Whether an IDA Title Termination (including reversion of fee title to the IDA units to Petitioner) with respect to any or all of the IDA condominium units, will be subject to gains tax or transfer tax.

3. Whether the creation of the IDA-Petitioner lease or portion thereof whether in connection with its original creation, in connection with a new conveyance following a Pre-Date Termination, in connection with Prudential's lease of additional space or the termination of the IDA-Petitioner lease or portion thereof upon the expiration of its term or upon an IDA Title Termination with respect to any or all of the IDA Units, or any similar creation or termination, will be subject to gains tax or transfer tax.

4. Whether the creation of the Petitioner-Prudential Lease or portion thereof in connection with the original conveyance, in connection with a new conveyance following a Pre-Date Termination or in connection with Prudential's lease of additional space will be subject to gains tax or transfer tax.

5. Whether any of the transactions described herein between Petitioner and the IDA will result in the imposition of any New York State or New York City mortgage recording tax.

Petitioner currently owns the fee interest in the parcel located in the Borough of Manhattan, City, County and State of New York, identified on the tax maps as Block 4, Lot 1 (the "Land") upon which is located the building having the street address One New York Plaza, New York, New York (the "Building"). (The Land and the Building together are hereafter referred to as the "Property"). The Building, which is owned by Petitioner, was completed in approximately 1970 and is comprised of approximately 2,400,000 feet of commercial space located on approximately 50 floors.

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The basic economic transaction is a lease by Petitioner to Prudential for the use of approximately 1,000,000 square feet in the Building. This space will generally consist of the rentable areas on the second through sixteenth floors of the Building plus miscellaneous areas located elsewhere in the Building, including without limitation areas on the ground floor and on the first Concourse level.

In connection with this lease, Petitioner has been informed that it will be necessary for Petitioner to transfer to the New York City Industrial Development Agency (the "IDA") title to the portion of the property occupied by Prudential. As part of the arrangement to induce Prudential to retain its offices in New York City, it is anticipated the New York City (the "City") will extend substantial tax and other benefits (the "Benefits") to reduce Prudential's costs of operating and maintaining its offices in the City. In this connection, it is expected that Prudential will obtain IDA financing from the IDA and other Benefits by entering into a sub-sublease with the IDA, which will sub-sub-sublease the space back to Prudential. It is anticipated that an additional Benefit, however, will be the arrangement for a real estate tax abatement on the space to be occupied by Prudential, with the agreement that certain payments in lieu of real estate taxes ("PILOT Payments") will be made. Petitioner has been informed that as a technical matter, the only way for such real estate tax Benefits (and perhaps some of the other Benefits) to be extended is for the IDA to take title to the real property to be occupied by Prudential. This will necessitate that Petitioner transfer to the IDA title to the portion of the Property to be occupied by Prudential, which portion the IDA will lease back to Petitioner.

The IDA will not take title to the entire Property. Instead, a condominium will be created at the Property pursuant to which, in general, each floor will become a separate condominium unit. The units to be occupied by Prudential will be conveyed by Petitioner to the IDA. The Units which are from time to time owned by the IDA are herein referred to as the "IDA Units" The remaining Units in the Building which from time to time are not IDA Units are herein referred to as the "Petitioner's Units".

The proposed structure will be implemented as follows:

1. Separate condominium units will be created pursuant to a Declaration of Condominium.
2. Petitioner will convey title to the IDA of the initial units comprising the IDA Units for no consideration (the "Original Conveyance").
3. The following leases and subleases will be created concurrently:
 - (a) IDA will net lease all of the aforesaid IDA Units to Petitioner for a nominal (or no) net rent (the "IDA-Petitioner Lease").

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- (b) Petitioner will, in turn, sublet all of the aforesaid IDA Units to Prudential (the "Petitioner-Prudential Lease") for a rent negotiated between Petitioner and Prudential.
4. Prudential and the IDA will enter into certain transactions as to which Petitioner is not a party and has no first hand knowledge as to their nature. Petitioner has been told that pursuant to those transactions, Prudential will receive Benefits.

It is currently contemplated that Petitioner will convey to the IDA title to the IDA Units. The IDA's title will end automatically and without further act on a certain date (the "Date"), or earlier upon the occurrence of certain events. (Such ending of the IDA's title with respect to any or all units or the ending of the IDA's title with respect to any or all units, through the delivery of a deed are referred to herein as an "IDA Title Termination" with respect to such unit or units. An IDA Title Termination that occurs on the Date is referred to herein as an "On-Date Termination." An IDA Title Termination that occurs prior to the Date is referred to herein as a "Pre-Date Termination.") It is anticipated that Petitioner will except and reserve to itself all right, title and interest in units not conveyed to the IDA.

The precise list of events that would cause Pre-Date Termination is still being negotiated among the parties. Among the events being considered by the parties are (i) the termination of the Petitioner-Prudential Lease, (ii) the election by the IDA to end the IDA title, (iii) the IDA Units becoming subject to real estate taxes, and (iv) the election by Petitioner to end the IDA title, which election may only be made under certain circumstances, such as upon Petitioner making PILOT Payments due to Prudential's failure to do so. In addition, it is possible that in the case of some or all of these events the ending of the IDA's title will be accomplished by the IDA executing and delivering to Petitioner a deed. A Pre-Date Termination may occur with respect to some or all of the IDA Units.

Upon an IDA Title Termination with respect to any unit, whether an On-Date Termination or a Pre-Date Termination, Petitioner will have full fee simple title to such unit. In addition, the IDA-Petitioner Lease will no longer apply to such unit or, upon an IDA Title Termination with respect to all the units, the IDA-Petitioner Lease will terminate.

Upon or after a Pre-Date Termination with respect to less than all of the units, Petitioner may once again convey to the IDA title to some or all of such units. In addition, such units would again become subject to the IDA-Petitioner Lease (and the Petitioner-Prudential Lease to the extent such units were not otherwise subject to such lease) or a new such lease or leases would be entered into with respect to such units.

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The IDA Units, when reconveyed to Petitioner following an IDA Title Termination, Pre-Date Termination or any other similar termination, will not be reconveyed subject to nor will Petitioner assume any mortgages placed on such units by the IDA for the benefit of Prudential.

If Prudential exercises certain options to lease additional space or otherwise leases additional space, then the condominium units representing such additional space may, to the extent that they are eligible for some or all of the Benefits, become IDA Units. In such case, such IDA Units will be conveyed by Petitioner to the IDA and the above leases with terms similar to those described above will be executed for such additional IDA Units, for the remainder of the term of the above leases.

At the time of any conveyance by Petitioner to the IDA or at the time of any IDA Title Termination, it is possible that some or all of the IDA Units (or Petitioner's interest in such units) will be subject to a mortgage placed on such units (or Petitioner's interest) by Petitioner. Similarly, Petitioner may obtain financing secured by a mortgage (or may otherwise permit the placing of a mortgage) which will be a lien on any or all of the following: (i) all or a portion of Petitioner's leasehold position under the IDA-Petitioner Lease, (ii) all or a portion of Petitioner's interest in the IDA Units and (iii) all or a portion of the IDA's title in the IDA Units (The IDA has agreed to subject its title to any mortgage at Petitioner's request, subject to certain restrictions, such as limitations on the mortgagee's ability to foreclose against the IDA's title.) Under all circumstances, as against the IDA, Petitioner will be the beneficiary of any proceeds received under any debt secured by the lien of such mortgage and as against the IDA will be the party with ultimate economic liability to repay any such debt.

The term of the Petitioner-Prudential Lease, including any renewal periods, will be less than 49 years. In addition, Petitioner is not expected to grant Prudential any option to purchase the Property or any portion thereof.

The gains tax is a ten percent tax on the gain derived from the transfer of real property, which includes the transfer or acquisition of a controlling interest in an entity with an interest in real property, where the real property is located in New York State and where the consideration for the transfer is \$1 million or more.

Section 590.5 of the Gains Tax Regulations provides as follows:

590.5 Lease/sublease as a transfer of real property. [Tax Law, §1440(7)]

(a) Question: Is the creation of a leasehold or sublease a transfer of real property?

Answer: Yes. The creation of a leasehold 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 of the total rentable space, of the premises exclusive of common areas. (See section 590.56 of this Part, relating to an assignment of a lease.)

For the purpose of determining whether a lease or sublease is for substantially all of the premises constituting the real property, premises shall include, but not be limited to the following:

(1) an individual building, except for space which constitutes an individual condominium or cooperative unit;

(2) an individual condominium or cooperative unit; or

(3) where a lease or sublease is of vacant land only, any portion of such vacant land.

(b) Question: Is the creation of a leasehold for a term of less than 49 years ever taxable?

Answer: Yes. If 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 590.67(a) of the Gains Tax Regulations provides, in part, as follows:

590.67 Transfers pursuant to industrial development agency projects.
[Tax Law, §1440]

(a) Question: How are transfers of interests in real property to and from an industrial development agency (IDA) treated for purposes of the gains tax?

Answer: 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 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.

Section 575.7 of the Transfer Tax Regulations states as follows:

575.7 Leases and subleases (Tax Law, §1401(d)(e), (f)) (a) Creation of a taxable lease or sublease not coupled with an option to purchase. The creation of a lease or sublease is a conveyance subject to tax 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 lessee 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. "Premises" means each unit of real property which, at the time that the lease or sublease is created, is capable of being sold separately.

For the purpose of determining whether a lease or sublease is for substantially all of the premises constituting the real property, premises shall include, but not be limited to the following:

(1) an individual building, except for space which constitutes an individual condominium or cooperative unit;

(2) an individual condominium or cooperative unit; or

(3) where a lease or sublease is of vacant land only, any portion of such vacant land.

Moreover, Section 575.11(a) of the Transfer Tax Regulations provides, in part, as follows:

(a) The following are examples of conveyances which are subject to the 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 paragraph (1) of subdivision (c) of section 575.9 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 or the conveyance.

Section 575.11(b) of the Transfer Tax Regulations provides as follows:

"(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 250 of the Tax Law defines the term "mortgage" to include "every mortgage or deed of trust which imposes a lien on or affects the title to real property, notwithstanding that such property may form a part of the security for the debt or debts secured thereby."

In the matter of Macy & Co. v. Bates, 280 App. Div. 292 the Court held, in part, as follows:

A mortgage, whether in form or equitable, imports a debt or obligation to be secured, due from the mortgagor to the mortgagee, a right to foreclose, and the reciprocal right to redeem. Without those elements there can be no mortgage, and they are absent here.

With respect to issue "1", the focus of Section 590.67 of the Gains Tax Regulations and Section 575.11 of the Transfer Tax Regulations is to exclude from gains tax and transfer tax respectively the transfer of title to real property to an IDA for the purpose of obtaining IDA financing, where the grantor remains the beneficial owner of the property. In the instant case, while Petitioner is not the beneficiary of the IDA financing, the transfer of the condominium units will not result in a change in beneficial ownership since Petitioner retains all the benefits and burdens of ownership of the IDA Units. Accordingly, in keeping with the intent of Section 590.67 of the Gains

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Tax Regulations and Section 575.11 of the Transfer Tax Regulations, the conveyance of title to the condominium units in connection with the Original Conveyance, in connection with a new conveyance following a Pre-Date Termination and in connection with Prudential's lease of additional space or any similar conveyance will not be subject to gains tax or transfer tax.

Concerning issue "2", pursuant to Section 590.67 of the Gains Tax Regulations and Section 575.11 of the Transfer Tax Regulations since Petitioner remains the beneficial owner of the condominium units, a Pre-Date Termination of the IDA's title to any of the units will not result in a change in beneficial interest. Therefore, a Pre-Date Termination of the IDA's title to any of the units will not be subject to gains tax or transfer tax.

As for issue "3", pursuant to Section 590.67 of the Gains Tax Regulations and Section 575.11 of the Transfer Tax Regulations the lease back of property by an IDA to the beneficiary of the IDA financing, is not subject to gains tax and transfer tax, respectively, since the beneficiary of the IDA financing remains the beneficial owner of the property. In the instant case, while Petitioner is not the beneficiary of the IDA financing, Petitioner is the beneficial owner of the property. Therefore, in keeping with the intent of Section 590.67 of the Gains Tax Regulations and Section 575.11 of the Transfer Tax Regulations, the creation of the IDA-Petitioner lease or portion thereof whether in connection with its original creation, in connection with a new conveyance following a PreDate Termination, in connection with Prudential's lease of additional space or the termination of the IDA-Petitioner lease or portion thereof upon the expiration of its term or upon an IDA Title Termination with respect to any or all of the IDA Units will not be subject to gains tax or transfer tax.

With respect to issue "4", pursuant to Section 590.5 of the Gains Tax Regulations and Section 575.7 of the Transfer Tax Regulations the creation of a lease for a term of less than 49 years, including renewal periods and not coupled with an option to purchase is not subject to gains tax and transfer tax respectively. Accordingly, since the creation of the Petitioner-Prudential Lease or portion thereof in connection with the original conveyance, in connection with a new conveyance following a Pre-Date Termination or in connection with Prudential's lease of additional space will be for a term of less than 49 years, including renewal periods and contains no options to purchase such leases will not be subject to gains tax or transfer tax.

Concerning issue "5", pursuant to Section 250 of the Tax Law and Macy & Co. v. Bates, supra, while the transactions described in issues "1", "2", "3" and "4" affect title to the real property such conveyances are not given as security for the payment of a debt or for the performance of an obligation. Accordingly, for purposes of Article 11 of the Tax Law no mortgage exists and such transactions will not be subject to New York State and New York City mortgage recording tax.

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It is noted that this opinion does not address the application of Article 11 of the Tax Law, the Tax on Mortgages, to Petitioner's mortgaging of its interest in the IDA-Petitioner lease or all or a portion of Petitioner's reversionary interest in the fee interest in the IDA Units.

DATED: January 7, 1993

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