

April 19, 2001

Re:

Request for Ruling
Real Property Transfer Tax
Commercial Rent or Occupancy Tax
FLR-004773-721

Dear _____ :

This is in response to your request for a ruling, dated December 7, 2000 regarding the application of the New York City Real Property Transfer Tax (RPTT) and the New York City Commercial Rent and Occupancy Tax (CRT) to the situation, described below, involving _____ and its affiliates (collectively referred to as “the Corporate Lessee”) regarding the _____ real estate project. Additional information was received on January 5 and February 16, 2001.

FACTS

The facts presented are as follows:

The Real Estate Project

The Corporate Lessee has entered into a synthetic lease (“Synthetic Lease”) arrangement concerning a condominium unit (the “Leasehold Unit”) in the multi-use, multi-unit real estate project which is to be developed by _____ (the “LLC”) on land located adjacent to _____ in New York City. A more detailed description of the LLC, the condominium and the construction project is set forth in FLR-004770-021 (issued herewith). Briefly, the LLC has six members: the “Leasehold member”, the “Hotel member”, the “Residential member”, the “Office member”, the “Retail member” and the “Garage member”. The condominium project will consists of a total of seven (7) Units, one of which will be owned by each of the LLC’s respective members, and one of which will be owned by a charity following the members’ donation of such Unit.

Because the Units will be housed in one integrated structure, the project will be submitted to a condominium regime. However, historically, it has not been possible to file a Declaration of Condominium and convey title to individual condominium units prior to the substantial completion of construction. For this and other reasons, the LLC has taken title to the land and will hold title to the structure during the project’s construction.

Upon completion of a member's Unit, the LLC will convey that Unit to the member. The Corporate Lessee is not a member of the LLC. Rather, as will be discussed below, the Leasehold member is a trust (the "Trust") that will take legal title to the Leasehold Unit upon completion of construction.

During construction, the land and building, including the Leasehold Unit, will be subject to a mortgage or mortgages securing the loans constituting the Project Financing which finances the construction of the project and most of the land acquisition costs. Upon the conveyance of the Leasehold Unit to the Trust, the Project Financing and the mortgage or mortgages securing the Project Financing will be severed into a separate loan and mortgage for the Leasehold Unit reflecting such Unit's allocable share of the Project Financing ("Allocable Share") with the Trust as mortgagor. The Leasehold Unit's Allocable Share will then be replaced with permanent mortgage financing in the form of the Synthetic Lease transaction discussed below, and the Trust will be released from any obligations under the Project Financing and the Leasehold Unit will not be subject to any other encumbrances.

The Synthetic Lease Arrangement

The Synthetic Lease arrangement is a financing structure in which the Corporate Lessee is intended to be treated as the owner of the Leasehold Unit for income tax purposes, but as a lessee under an "operating lease" (the "Lease") with the Trust (which holds legal title to the property) for financial statement purposes. You have represented that the Corporate Lessee's tax reporting and actions will be consistent with its characterization as the owner of the Leasehold Unit for tax purposes. For example, the Corporate Lessee will capitalize interest and construction costs as the owner of the Leasehold Unit. In addition, the Corporate Lessee, rather than the Trust, will claim the depreciation deductions for the Unit on income tax returns, and the Corporate Lessee will treat the payments due under the Lease as the repayment of a debt obligation, and not as a deductible rental payment.

The Trust was established with _____ as the Certificate Trustee, and the Certificate Holders as the beneficiaries of the Trust. The Certificate Holders will make or have made equity investments in the Trust which are evidenced by the Certificates. In addition, the Trust has obtained or will obtain loans from various "Lenders" which will be secured by a mortgage on the Leasehold Unit. The Lenders and the Certificate Holders will be collectively referred to herein as "Participants" and the amounts loaned to or invested with the Trust will be collectively referred to herein as "Advances". However, in terms of the priority of repayment of the Advances, the Certificate Holders' position as equity investors will be fully subordinated to that of the Lenders.

You have represented that neither the Trust nor any of the Participants is affiliated with the Corporate Lessee. The Trust, the Participants and the Corporate Lessee are, however, all parties to a Participation Agreement that governs the Advances from the Participants. Under the Participation Agreement, the Advances are tied to funding requests made by the Corporate Lessee, and the Participants are to make the Advances directly to the

financial entity designated to act as the Participants' administrative agent (the "Agent") which is not affiliated with the Corporate Lessee.

Prior to the LLC's conveyance of the Leasehold Unit to the Trust, the Advances will be used only to cover the Trust's share of the land acquisition costs and certain other costs. At the time of the conveyance, provided the completed Leasehold Unit meets certain minimum appraised valuation requirements, the Administrative Agent will purchase, on behalf of the Participants, the severed mortgage on the Leasehold Unit from the Project Financing lender using additional Advances. At that time, the Trust, as mortgagor, and the Administrative Agent, as mortgagee, will amend and restate the mortgage to reflect the terms of the Participation Agreement, the Lease and other documents relating to the Synthetic Lease arrangement. As amended and restated, this mortgage will be referred to herein as the Participants' Mortgage.

In the event that, prior to the conveyance of the Leasehold Unit to the Trust, there is a default or other failure to satisfy the conditions for the conveyance of the Leasehold Unit, the Certificate Holders are entitled to exercise a Put Election Option which would require the Trust to redeem their investments at the face amount of the Certificates. The Corporate Lessee has made or will make a Liquidity Loan to the Trust, which is required to hold the proceeds of this Liquidity Loan in a separate, special bank account. The Liquidity Loan funds would enable the Trust to make the payments required by the exercise of the Put Election Option. Upon the exercise of the Put Election Option, the Corporate Lessee also would be required to make rental payments to the Trust to enable the Trust to refund the portion of the Advances received from the Lenders.

Although the Trust holds legal title to the membership interest in the LLC, it has designated the Corporate Lessee as its exclusive agent for purposes of the construction, design and conveyance of the Leasehold Unit, pursuant to a Construction Agency Agreement. Under the Construction Agency Agreement, the Corporate Lessee will (1) control and supervise the design and construction of the Leasehold Unit; (2) exercise all rights and benefits under the LLC's operating agreement, including the voting of the Trust's membership interest in the LLC; and (3) perform all obligations and liabilities of the Trust under the LLC's Operating Agreement. The Corporate Lessee has also agreed to indemnify the Trust for any liability that may result from its failure to carry out its obligations under the Operating Agreement. Further, the Corporate Lessee's only restriction under the Construction Agency Agreement is that it may not enter into any agreement that would impose any personal liability on the Trust. In the event the Corporate Lessee defaults on its obligations under the Construction Agency Agreement, the Trust has the right to require the Corporate Lessee to pay the outstanding amount of the Advances.

The Lease between the Trust and Corporate Lessee becomes effective on the date of the conveyance of the Leasehold Unit to the Trust, and has a term of five (5) years. Under the Lease, the Corporate Lessee will accept delivery of the Leasehold Unit from the LLC on behalf of the Trust, and agrees that the conveyance of title to the Leasehold Unit by the LLC to the Trust will also constitute the Corporate Lessee's acceptance of the

Leasehold Unit for purposes of the Lease and other operative documents. The payments that the Corporate Lessee must make under the Lease are referred to as “rent” and are equivalent to the amount needed to pay the interest and yield on the Advances as well as any additional amounts owed under the Lease or other documents, including any required repayment of the Advances. The Corporate Lessee’s obligation to pay such rent is absolute and unconditional, without regard to the condition of the Leasehold Unit. Moreover, the Synthetic Lease arrangement will be treated as a mortgage for purposes of the New York City and New York State mortgage recording tax (MRT), and MRT will be paid on any new or additional indebtedness not previously secured by a tax-paid mortgage.

The Lease also provides that the Corporate Lessee is responsible for, and the Trust shall be held harmless from, all costs associated with possession and ownership of the Leasehold Unit, including property taxes, utility charges, repairs and insurance. Further, the Corporate Lessee may make any alterations, renovations, improvements or additions to the Leasehold Unit provided that such modifications do not impair the value or useful economic life of such Unit. In addition, the Corporate Lessee may sublease all or any part of the Leasehold Unit without the Trust’s consent. An assignment or similar transfer of the Corporate Lessee’s interest in the Lease does require the Trust’s consent, however.

The Participation Agreement specifically states the Lease is intended to grant a security interest in the Leasehold Unit for the benefit of the Participants to secure the Corporate Lessee’s performance. Further, the Participant’s Mortgage is also designed to secure the Corporate Lessee’s payment and the performance of its obligations under the Lease. Moreover, the Corporate Lessee’s rental payments under the Lease are required to be used to pay interest and yield on the Advances, and to repay the principal amount of the Advances when due. Hence, the Corporate Lessee’s rental payments will be directly applied to pay the obligations due under the Participation Agreement. In addition, you have represented that the Participation Agreement imposes conditions on the Corporate Lessee that are common in financing agreements. For example, it obligates the Corporate Lessee (rather than the Trust) to provide periodic financial information and notification of any “Material Event.” Further, any default under the Lease by the Corporate Lessee permits the Participants to demand the Corporate Lessee’s repayment of the Advances.

Under the Lease, the Corporate Lessee must maintain insurance covering any loss or liability to the Trust. Moreover, in the event of a casualty or condemnation following the conveyance of the Leasehold Unit to the Trust, the Corporate Lessee must restore the Unit to substantially the same condition and value as existed prior to the casualty or condemnation. In such circumstances, any insurance proceeds or condemnation awards will be payable to the Corporate Lessee, unless there is a default under the Lease. If a default has occurred, the insurance or award amounts may be applied to the repayment of the Advances (first to lenders, then to Certificate Holders), and any excess will be paid to the Corporate Lessee. In the event of a “Significant Casualty”, “Significant Condemnation”, or “Significant Event”, either the Corporate Lessee or the Trust may terminate the Lease. On termination, the Lease obligates the Corporate Lessee to pay the Purchase Amount – an amount equal to the then outstanding Advances plus any unpaid

accrued rent – and acquire the legal title to the Leasehold Unit from the Trust. The Trust has the right to impose this same obligation on the Corporate Lessee in the event of the Corporate Lessee’s default under the Lease.

The Lease also grants a “Purchase Option” to the Corporate Lessee, which permits the Corporate Lessee to purchase the Leasehold Unit for the Purchase Amount at any time during the term of the Lease or upon the expiration of the lease term, even if the Corporate Lessee is in default. You have represented that it is highly likely that the Corporate Lessee will exercise the Purchase Option. The payment of Purchase Amount is, hence, the functional equivalent of the repayment of principal and accrued interest.

As an alternative to exercising the Purchase Option, the Corporate Lessee can exercise a “Sale Option”. Under the Sale Option, the Corporate Lessee would be required to sell the Leasehold Unit to a third party purchaser upon the expiration of the Lease, and would guarantee that the Trust receive a minimum of the Sales Recourse Amount on the sale. The Sales Recourse Amount is the amount that, if paid on the date of the determination of the Sales Recourse Amount, would have a discounted value as of the commencement of the Lease term, along with fees, fixed expenses and basic rent, equal to 89.75 percent of the outstanding Advances as of the Sales Recourse Amount’s determination date. If the net proceeds of the sale are less than the Sales Recourse Amount, the Corporate Lessee must, in effect, make up the difference. If the net proceeds of the sale exceed the Sales Recourse Amount, the Trust would receive the excess of such proceeds up to the Purchase Amount. If the net proceeds are more than the Purchase Amount, the Corporate Lessee would be entitled to receive the amount in excess of the Purchase Amount.

ISSUES

You have requested rulings as to whether:

1. The LLC’s conveyance of the Leasehold Unit to the Trust is exempt from the RPTT;
2. The Corporate Lessee’s payments under the Synthetic Lease arrangement are exempt from the CRT.
3. The Synthetic Lease arrangement, including the Trust’s leasing of the Leasehold Unit to the Corporate Lessee, is exempt from the RPTT; and
4. The Trust’s anticipated conveyance of the Leasehold Unit to the Corporate Lessee (either during, or at the end of, the Lease’s term) pursuant to the Corporate Lessee’s Purchase Option is exempt from the RPPT.

CONCLUSION

Based on the facts presented and representations submitted, we have determined that the LLC’s conveyance of the Leasehold Unit to the Trust is exempt from the RPTT under section 11-2106(b)(7) of the Administrative Code of the City of New York (the “Code”).

We have also determined, based on the facts presented and representations submitted, that the Corporate Lessee's rental payments made pursuant to the Lease between the Trust and the Corporate Lessee are exempt from the CRT, because the substance of the transaction is a financing arrangement. We have similarly determined that the Synthetic Lease arrangement is exempt from the RPTT under section 2106(b)(6). Finally, we have determined that the anticipated conveyance of the Leasehold Unit from the Trust to the Corporate Lessee is exempt from the RPTT pursuant to section 11-2106(b)(6).

DISCUSSION

I. The LLC's Conveyance of the Leasehold Unit to the Trust

Code section 11-2102 imposes a tax on the transfer of real property or an economic interest therein when the consideration exceeds \$ 25,000. However, Code section 2106(b)(7) exempts transfers of real property interests "from a person acting as a mere agent, dummy, straw or conduit to his principal, or from the principal to such person...."

Here, pursuant to the LLC's Operating Agreement, the LLC will obtain and hold during construction the condominium Units on behalf of the LLC's respective members, which, in the case of the Leasehold Unit, is the Trust. Upon the completion of construction, the Leasehold Unit will be transferred to the Trust, and the other units will be transferred to the other respective members of the LLC.

Under the LLC's Operating Agreement, The Trust's interest is limited to the Leasehold Unit, and all benefits and obligations regarding the Leasehold Unit will be the responsibility of the Trust, and, ultimately the Corporate Lessee, by virtue of the Construction Agency Agreement, the Participation Agreement and the Lease. Neither the Trust nor the Corporate Lessee will derive any benefits from or be responsible for the obligations of any of the other Units. At the time of its conveyance to the Trust, the Leasehold Unit's Allocable Share of the Project Financing and the accompanying mortgage or mortgages will be severed into a separate loan and mortgage, which will be purchased by the Administrative Agent on behalf of the Participants. When all of the Units have been transferred to their respective members, the LLC will cease to exist. The LLC will never derive any benefit from the property, nor incur any detriment or obligation. It will be acting as a mere conduit for the Trust and the other members.

Based on the facts presented and representations submitted, we have determined that the LLC's conveyance of the Leasehold Unit to the Trust is exempt from RPTT under Code section 11-2106(b)(7). In light of this determination, it is not necessary to consider whether the conveyance is exempt as a mere change in form under Code section 11-2106(b)(8).

II. The Synthetic Lease Arrangement

The Synthetic Lease arrangement raises issues concerning the potential application of both the CRT and the RPTT. In addition, the Corporate Lessee's purchase option under that arrangement raises questions concerning the potential application of the RPTT.

A. The Synthetic Lease Arrangement and the CRT

The CRT is imposed on a tenant who occupies, uses, or intends to occupy or use premises in New York City¹ for "carrying on or exercising any trade, business, profession, vocation or commercial activity...." Code §§ 11-701(5), 11-701(7) and 11-702(a). A "tenant" is defined as a "person paying or required to pay rent for premises as a lessee, sublessee, licensee, or concessionaire." Code § 11-701(3). The owner of a building who occupies space in the building is not considered a "tenant" for purposes of the CRT. See Title 19, Rules of the City of New York (RCNY), § 7.01.

Given the form of the Lease, which is structured as a lease of the Leasehold Unit between the Trust and the Corporate Lessee, the Corporate Lessee would be subject to the CRT. However, the Corporate Lessee seeks to disavow the form of the transaction and contends that the Lease is, in reality, a financing program in which the Corporate Lessee will act as the owner of the Leasehold Unit.

In general, a taxpayer may not disavow the form of a transaction. See Commissioner v. National Alfalfa Dehydrating and Milling Co., 417 U.S. 134, 148-149 (1974); Sverdlow v. Bates, 283 App. Div. 487, 491 (3rd Dept. 1954). However, a taxpayer may assert a transaction's economic substance if (1) its tax reporting and actions are consistent with the substance of the transaction, Comdisco, Inc. v. United States, 756 F.2d 569, 578 (7th Cir. 1985); and (2) the taxpayer offers strong proof that the transaction is a financing arrangement, Illinois Power v. Commissioner, 87 T.C. 1417, 1434 (1986); Coleman v. Commissioner, 87 T.C. 178, 201-202 (1986), aff'd per curiam 833 F.2d 303 (3rd Cir. 1987).

The Corporate Lessee's tax reporting and actions will be consistent with its characterization as the owner of the Leasehold Unit for tax purposes. For example, the Corporate Lessee will capitalize interest and construction costs as the owner of the Leasehold Unit. In addition, the Corporate Lessee, rather than the Trust, will claim the depreciation deductions for the Unit on income tax returns, and the Corporate Lessee will treat the payments due under the Lease as the repayment of a debt obligation, and not as a deductible rental payment.

For federal income tax and New York State tax purposes, a leasing transaction, including a "Synthetic Lease" situation, will be treated as a financing arrangement if the lessee has the benefits and burdens of ownership despite not having title to the property. See Frank

¹ For periods beginning on or after September 1, 1995, the rent on any premises located in boroughs other than the Borough of Manhattan or located north of the center line of Ninety-sixth Street in the Borough of Manhattan is exempt from the CRT. Code § 11-704(h)(1)

Lyon Co. v. United States, 435 U.S. 561 (1978); Helvering v. F & R Lazarous & Co., 308 U.S. 252 (1939); Rev. Rul. 68-590, 1968-2 C. B. 66; FSA Memo 199920003 (May 21, 1999) (Synthetic Lease situation); Matter of Sherwood Diversified Services, Inc., 382 F. Supp. 1359 (interpreting New York State sales tax law); General Electric Co., Inc., TSB-A-96(5)R (June 25, 1996) (Synthetic Lease situation); Eastman Kodak Co., TSB-A-90(8)S (March 12, 1990). See also Matter of Erie County Industrial Development Agency v. Roberts, 63 N.Y.2d 810 (1984) aff'd for reasons stated at 94 A.D.2d 532 (4th Dept. 1983) (applying “benefits and burdens” analysis to lease transaction to determine if project financed by Industrial Development agency is a “public works” project for purposes of the Labor Law). In our opinion, it is appropriate to apply the above “benefits and burdens of ownership” analysis for purposes of the CRT.

The factors relevant to determining whether a lease transaction is a financing arrangement include: (1) which party exercises control over the property during the lease term, including the right to make improvements; (2) who bears the risk of loss from a casualty or condemnation, and the liability for repayment of a loan; and (3) which party has the potential to obtain profit or incur loss from the holding of the property. See Sun Oil Co. v. Commissioner, 562 F.2d 258, 268-269 (3rd Cir. 1977); Illinois Power, 87 T.C. 1417, 1437-1440; Pacific Gamble Robinson and Affiliated Companies v. Commissioner, T.C. Memo 1987-533; Eastman Kodak, TSB-A-90(8)S; FLR-93-110. See also Levy v. Commissioner, 91 T.C. 838, 860 (1988); Larsen v. Commissioner, 89 T.C. 1229, 1267 (1987), aff'd in part and reversed in part sub nom. Casebeer v. Commissioner, 909 F.2d 1360 (9th Cir. 1990); Torres v. Commissioner, 88 T.C. 702, 720-722 (1987); Coleman, 87 T.C. 178, 205; Grodt & McKay Realty Inc. v. Commissioner, 77 T.C. 1221 (1981).

Applying the above factors to the facts presented here, we conclude that the Corporate Lessee will have the benefits and burdens of ownership of the Leasehold Unit. Under the Lease, the Construction Agency Agreement, and other documents, the Corporate Lessee’s control over the Leasehold Unit is more like that of an owner rather than that of a lessee. See Illinois Power, 87 T.C. 1417, 1439-1440; Pacific Gamble Robinson, T.C. Memo 1987-533; Eastman Kodak, TSB-A-90(8)S. The Corporate Lessee will have complete control over the design and construction of the Leasehold Unit, as well as the right to possession and use of the Unit. In addition, the Corporate Lessee has the right to make additional improvements, renovations and alterations, provided they do not impair the value or useful life of the Unit. Also, the Corporate Lessee will have the right to sublease all or any part of the Unit.

Moreover, the Corporate Lessee will bear the risk of casualty and/or condemnation loss for the Leasehold Unit. See Sun Oil, 562 F.2d 258, 269; Illinois Power, 87 T.C. 1417, 1439-1440; Pacific Gamble Robinson, T.C. Memo 1987-533. See also Hilton v. Commissioner, 74 T.C. 305, 357-358 (1980). The Corporate Lessee is required to maintain insurance covering any loss or liability concerning the Unit. Moreover, in the event of a casualty or condemnation following the conveyance of the Leasehold Unit to the Trust, the Corporate Lessee must restore the Unit to substantially the same condition and value as existed prior to the casualty or condemnation, and its obligation to pay rent under the Lease will be unaffected. In such circumstances, any insurance proceeds or

condemnation awards will be payable to the Corporate Lessee, provided it is not in default under the Lease. If a default has occurred, the insurance or award amounts may be applied to the repayment of the Advances (first to lenders, then to Certificate Holders), and any excess will be paid to the Corporate Lessee. In the event of a “Significant Casualty”, “Significant Condemnation”, or “Significant Event”, either the Corporate Lessee or the Trust may terminate the Lease. On termination, the Lease obligates the Corporate Lessee to pay the Purchase Amount – an amount equal to the then outstanding Advances plus any unpaid accrued rent – and acquire the legal title to the Leasehold Unit from the Trust. The Trust has the right to impose this same obligation on the Corporate Lessee in the event of the Corporate Lessee’s default under the Lease.

The third factor is whether the Corporate Lessee or the Trust has the potential for profit or loss from holding the Leasehold Unit. See Frank Lyon, 435 U.S. 561, 579; Sun Oil, 562 F.2d 258, 268; Illinois Power, 87 T.C. 1417, 1437-1438; Hilton, 74 T.C. 305, 357-359; Pacific Gamble Robinson, T.C. Memo 1987-533; Rev Rul. 83-47, 1983-1 C.B. 63. Here, the Corporate Lessee will have the profit or loss potential. In the likely event that the Corporate Lessee exercises the Lease’s Purchase Option, the Corporate Lessee will be required to pay the Purchase Amount, which is the functional equivalent of repaying the amount of the outstanding loan plus accrued interest. Should the Corporate Lessee default, it will also be required to pay the Purchase Amount. In either case, if the Corporate Lessee is required to pay the Purchase Amount, it will be the beneficiary of any increase in the value of the Leasehold Unit, and it will bear the entire risk of any decrease in the value of the Unit. Similarly, if the Corporate Lessee pays the Purchase Amount, the Trust will not be able to benefit from any gain, and will be protected from any loss, in the Unit’s value.

Should the Corporate Lessee chose to exercise the Sale Option, it will be required to sell the Leasehold Unit to a third party, and will guarantee that the Trust receives a minimum of the Sales Recourse Amount on the sale. The Sales Recourse Amount is the amount that, if paid on the date of the determination of the Sales Recourse Amount, would have a discounted value as of the commencement of the Lease term, along with fees, fixed expenses and basic rent, equal to 89.75 percent of the outstanding Advances as of the Sales Recourse Amount’s determination date. If the net proceeds of the sale are less than the Sales Recourse Amount, the Corporate Lessee must, in effect, make up the difference. If the net proceeds of the sale exceed the Sales Recourse Amount, the Trust would receive the excess of such proceeds up to the Purchase Amount. If the net proceeds are more than Purchase Amount, the Corporate Lessee would be entitled to receive the amount in excess of the Purchase Amount. Hence, the Corporate Lessee will benefit from any increase in the value of the Leasehold Unit, to the extent that the net proceeds from the sale exceed the Purchase Amount.

The Trust’s potential risk of loss due to the depreciation in value of the Leasehold Unit is limited to the difference between the Purchase Amount and the Sales Recourse Amount, which is no more than 10.25 percent of the outstanding Advances. This potential depreciation risk is no different than the depreciation risk borne by any non-recourse lender. It does not spring from a genuine equity interest in the Leasehold Unit.

Moreover, the Trust's depreciation risk is minimal relative to the risk borne by the Corporate Lessee, inasmuch as the Corporate Lessee would be required to pay 89.75 percent of the outstanding Advances and lose all of its interest in the Leasehold Unit. Clearly, the Corporate Lessee bears the greatest risk of loss due to depreciation.

In the unlikely event of a default or a failure to satisfy conditions which precludes the LLC from conveying the Leasehold Unit to the Trust, the Trust and the Participants are protected from any potential loss. Under the Participation Agreement's Put Election Option and related provisions, the Certificate Holders are entitled to have their investments redeemed at face value by the Trust with funds that have been provided by the Corporate Lessee. In addition, the Corporate Lessee is required to pay sufficient rent to the Trust to allow the Trust to repay the Advances received from the Lenders.

In sum, the Corporate Lessee will have all of the potential to profit from an increase in the value of the Leasehold Unit and will clearly bear the greatest risk of depreciation in the value of the Unit. In addition, the Corporate Lessee will bear the risk of casualty and/or condemnation loss to the Unit, and will exercise a level of control over the Unit that is more like that of an owner than a lessee.

Accordingly, we conclude that the Corporate Lessee owns the Leasehold Unit for CRT purposes. Hence, the Corporate Lessee is not a tenant under Code section 11-701(3), and the CRT is inapplicable to the payments that the Corporate Lessee must make under the Synthetic Lease arrangement.

B. The Synthetic Lease Arrangement and the RPTT

Code section 11-2102(a) imposes a tax on the transfer of real property interests where the consideration for the real property and any improvement thereon exceeds \$25,000. The transfer of a real property interest includes the grant, assignment or surrender of a leasehold interest in real property. Code § 11-2102(a)(10).² However, the RPTT does not apply to 1) "[a] deed or instrument which was given solely as security for, or a transaction the sole purpose of which is to secure, a debt or obligation, or [(2)] a deed or instrument given, or a transaction entered into, solely for the purpose of returning such security." Code § 11-2106(b)(6).

Inasmuch as we have concluded that the Synthetic Lease arrangement is a financing program, the Lease between the Trust and the Corporate Lessee is merely part of that program and does not create a leasehold interest. See Part II(A), above. Similarly, any initial assignment or transfer on the part of the Corporate Lessee of an interest in the LLC to the Trust would also be part of that financing program. Accordingly, the RPTT will not apply to the creation or termination of the Lease.

² With regard to leaseholds, the RPTT is imposed only to the extent the consideration for the leasehold is not considered rent for purposes of the CRT. Code § 11-2102(a)(10)(iii).

C. The Corporate Lessee's Purchase Option

The granting of a purchase option to purchase real property will be subject to RPTT if the benefits and burdens of ownership are shifted to the holder of the option. See 19 RCNY § 23-03(j)(3). However, if the substance of the transaction is a financing arrangement, neither the grant of the option, nor the subsequent transfer of the real property pursuant to its exercise, will be subject to the RPTT. See Code § 11-2106(b)(6).

Here, we have already concluded that the Synthetic Lease arrangement is a financing program, and that the Corporate Lessee is the owner of the Leasehold Unit for purposes of the CRT. See Part II(A), above. The analysis is the same for the RPTT as it is for the CRT. Because the option merely represents the Corporate Lessee's right to redeem collateral, the RPTT will not apply to the granting of, or the transfer of title pursuant to, the Purchase Option.

The Department reserves the right to verify the information submitted.

Sincerely,

/s/ Devora B. Cohn
Associate Commissioner
For Legal Affairs