

RPTT-2008-03  
04/10/08

## STATEMENT OF AUDIT PROCEDURE

### AUDITS OF PURPORTED “DUMMY/STRAWMAN” TRANSFERS IN CONNECTION WITH REAL ESTATE SYNDICATIONS

#### **I. BACKGROUND**

Investors use a variety of vehicles to acquire and finance the acquisition of real property in New York City. Frequently, one or more promoters will form a partnership or limited liability company to acquire a property. The promoters make an initial capital contribution to that entity (hereafter referred to as the “owner/principal”). Generally, the promoters then raise the money to acquire the property by selling interests in the owner/principal to investors using a public offering or private placement syndication. Additional funds may be obtained from lenders, usually on a short term unsecured basis to be repaid out of the proceeds of the syndication or replaced with permanent financing.

Generally the investors acquire a majority interest in the owner/principal through the syndication. If the syndication is completed or substantially completed before the owner/principal acquires the real property, the New York City Real Property Transfer Tax (“RPTT”) applies only to the purchase of the property by the owner/principal.

If the owner/principal purchases the property prior to the syndication, the RPTT would apply twice, first to purchase of the real property by the owner/principal and again to the transfer of a controlling economic interest in the owner/principal if the investors acquire a 50 percent<sup>1</sup> or greater ownership interest pursuant to the syndication.

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<sup>1</sup>The 50 percent ownership interest is measured by the fair market value or the combined voting power of the stock in a corporation or by the capital, profits or beneficial ownership in a partnership, trust or other entity. A transfer of a controlling interest can include the issuance of shares or interests in the entity. A series of transfers of ownership interests in an entity can constitute a controlling interest transfer if the transfers are pursuant to a plan. Transfers within three years are presumed to be pursuant to such a plan. Transfers pursuant to a syndication also are considered to be made pursuant to a plan. See Title 19 Rules of the City of New York §23-02, “Controlling interest”, par. (2), illustration (xiv).

Although syndication promoters try to time the transactions so as to avoid a double tax, occasionally they may not be able to do so. In those cases, the promoters will use another entity (hereafter referred to as the “nominee”) to acquire title to the property on behalf of the owner/principal. The nominee will hold title to the property only until the syndication can be completed or substantially completed, and will then transfer title to the property to the owner/principal. If properly structured and documented, the transfer of the property by the nominee to the owner/principal should qualify as a transfer from “a mere agent, dummy, straw man or conduit”<sup>2</sup> to its principal.

## **II. SCOPE**

This Statement of Audit Procedure provides guidance to auditors examining a transaction for which the taxpayer has claimed the “dummy/strawman” exemption for a transfer from a nominee to an owner/principal as part of a real estate syndication as described above.

This Statement of Audit Procedure is not applicable in auditing a return relating to the acquisition of the property by the nominee.

This Statement of Audit Procedure shall apply to all open cases.

## **III. PROCEDURES**

The auditor may accept as filed a return claiming the “dummy/strawman” exemption if **all of the following conditions are met:**

1. **Return.** The taxpayer must check condition (h) on the Form NYC-RPT and complete Schedule E claiming an exemption from the RPTT under the “dummy/strawman” exception.
2. **Documentation.** The auditor should request the following documents if not attached to the Form NYC-RPT:
  - nominee or agency agreement
  - formation documents for the nominee (the certificate of limited partnership, certificate of incorporation or articles of organization for a limited liability company)
  - syndication materials (the private placement or public offering materials sent to prospective investors)
  - loan agreements and other financing documents for financing the acquisition of the property by the nominee or the owner/principal
  - any other related documents

When reviewing the documents submitted, the auditor should look for the following:

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<sup>2</sup> The RPTT does not apply to:

a deed, instrument or transaction conveying or transferring real property or an economic interest therein from a mere agent, dummy, straw man or conduit to his principal or a deed, instrument or transaction conveying or transferring real property or an economic interest therein from the principal to his agent, dummy, straw man or conduit.

Ad. Code §11-2108(b)(7).

**A. Nominee or agency agreement.**

- The agreement must have been entered into prior to the transfer of the property to the nominee
- The agreement should identify the property and provide that the purpose of the agreement is to facilitate the acquisition of that property by the owner/principal.
- The agreement should provide that the nominee is acting for and on behalf of the owner/principal
- The agreement should provide that the nominee must acquire, hold, dispose of and otherwise deal with the property solely as directed by the owner/principal.
- The nominee should have no discretionary authority or responsibility for the property
- The owner/principal should indemnify the nominee for any losses, expenses or damages resulting from the nominee's actions under the agreement
- The agreement should terminate within one year after the acquisition of the property by the nominee and should provide that the property will be transferred to the owner/principal on termination of the agreement.

**B. Formation documents for nominee.** The organizational documents for the nominee must expressly provide that the nominee is being formed for the purpose of acquiring title to the property as a nominee for the owner/principal.

**C. Financing documents.** Documents relating to any financing provided by lenders in connection with the acquisition of the property by the nominee should acknowledge the beneficial ownership by the owner/principal. Any financing documents should provide that such financing is for the limited period of the syndication and that it will be repaid out of the proceeds of the syndication and/or any permanent financing following the transfer of the property from the nominee to the owner/principal.

**D. Syndication documents.** The syndication documents should describe the transaction, particularly the nominee arrangement, consistent with the provisions of the nominee or agency agreement and the characterization of the transaction as a "dummy/strawman" transaction.

**E. Other documents.** Any other documents executed in connection with the acquisition of the property and the syndication, such as the deed, the contract of sale or any assignment of the contract, should be consistent with the provisions in the nominee/agency agreement and the characterization of the transaction as a "dummy/strawman" transaction.

**3. Duration.** The nominee arrangement should be for a limited period of time. The transfer of the property from the nominee to the owner/principal should take place within one year after the acquisition by the nominee.

4. **Payment.** There should be no fee or other payment, other than a nominal amount not in excess of ten dollars, paid to the nominee for the conveyance of the property from the nominee to the owner/principal. The property should not be conveyed subject to any indebtedness.

If a taxpayer claims the “dummy/strawman” exemption for a transfer from a nominee to an owner/principal as part of a real estate syndication but the transfer **does not meet all of the above conditions**, for example, if some of the listed documents are not submitted or seem inconsistent with a nominee or agency arrangement, an auditor may not on his or her own accept the return as filed. Instead, the auditor will consult a supervisor who will review all of the facts and circumstances of the syndication and determine if the “dummy/strawman” exemption applies.