



November 21, 2007

Re: Request for a Ruling

New York City Property Tax
New York City Real Property Transfer Tax
FLR No: 074873-021

Dear :

This is in response to your ruling request dated May 17, 2007, on behalf of _____ for a ruling regarding the application of the Real Property Tax ("RPT"), and the Real Property Transfer Tax ("RPTT"), as these statutes would apply to a conveyance of real property from _____ to a single-member limited liability company ("LLC") in which _____ is the sole member. This office received additional information concerning this request on September 7, 2007.

FACTS:

_____ is a New York not-for-profit corporation. In 1991, _____ was recognized by the Internal Revenue Service ("IRS") as qualifying for federal tax-exemption status under Section 501(c)(3) of the Internal Revenue Code of 1986, as amended (the "Code"). _____ has been similarly recognized as tax exempt, by New York State and New York City for state and local corporate income tax purposes (including the New York City General Corporation Tax ("GCT"), as well as from sale and use taxes).

_____ is a unique, public service organization. It is the leading third-party (i.e., non-university or college) provider of affordable student housing in New York City and the surrounding metropolitan area. As such it currently provides more than 6000 dormitory beds for college and graduate students. Historically, _____ has leased on a long-term basis "single room occupancy" hotel and other buildings, converted those facilities into dormitory rooms and subleased such dormitory housing to students attending New York City area schools.

This model has been undergoing some change in recent years as _____, instead of leasing dormitory properties, is now seeking to acquire and /or develop dormitory properties in New York City. In some instances, _____ will seek to finance these activities using tax-exempt bond financing in the form of Dormitory Authority of the State of New York (“DASNY”) bonds. In fact, it should be noted that _____ is the only non-university or college that is expressly authorized by New York State legislation to utilize the funding provided through the issuance of DASNY bonds for student and faculty housing.

For a variety of reasons, including the desire to limit _____ exposure to the liabilities associated with owning and/or developing real property and to more readily secure DASNY and /or other financing to acquire and/or develop real property in New York City, it is imperative (and often required) that _____ conduct such activities through a separate legal entity. In this regard, _____ options are limited to organizing one of the two following types of entities to acquire, own and/or develop real property for dormitory housing in New York City: (1) a subsidiary not-for-profit corporation that would seek IRS and New York State recognition as a 501(c)(3) charitable and educational tax-exempt organization; or (2) a single member LLC with _____ as the sole member.

_____ has chosen the single member LLC option with _____ as the sole member. _____ represents that: (1) the LLC will be a not-for-profit entity, organized or conducted for section 420-a purposes; (2) the articles of organization and/or operating agreement of the LLC will provide that the LLC will operate for the same charitable and educational not-for-profit, tax exempt purpose as _____; (3) the LLC will have substantially the same, if not identical management as _____; (4) the LLC will be managed and maintained with _____ as its sole member; (5) upon termination of the LLC, the LLC’s property will revert to _____ or a comparable not-for-profit entity. Finally, since _____ recognizes that the transfer of any interest in the single-member LLC would result in the loss of the tax exemption to the LLC, _____ and the LLC will provide the Department of Finance (“DOF”) with an annual affidavit stating that there had been no change in the beneficial ownership of the LLC.

_____ intends to purchase real property in New York City from unrelated, non-tax exempt third parties, and then in a timely manner thereafter contribute such real property to a single member LLC with _____ as the sole member.

ISSUE:

You have requested rulings as to whether:

1. _____ is exempt from real property tax pursuant to section 420-a of the Real Property Tax Law (“RPTL”).
2. Property owned by a single-member LLC, where the single-member, _____, is a not-for-profit educational organization, will qualify for a RPTL section 420-a exemption.
3. The RPTT will be imposed upon the transfer of real property from an unrelated non-tax exempt third party to _____ by reason of section 11-2106(b)(2) of the New York Administrative Code (the “Code”).
4. The RPTT will be imposed upon the transfer of real property from _____ to a single-member limited liability company in which _____ is the sole member.

CONCLUSION:

1. _____ is exempt from the RPT since _____ is organized or conducted for educational purposes under RPTL section 420-a.
2. Based on the facts provided, real property owned by _____ will continue to be exempt from the RPT while held by a single-member limited liability company, where the single member is _____ and the property continues to be used exclusively for educational purposes. Provided that the limited liability company meets the criteria established below and the property, based on ownership and use would otherwise qualify for a section 420-a exemption, the organizational form would not preclude exemption.
3. Based upon the facts presented we have determined that Code section 11-2106(b)(2) applies to the transaction. Thus, the transfer of the real property by an unrelated non-tax exempt third party to _____ will be exempt from the RPTT.
4. The RPTT does not apply to the conveyance of the real property from _____ to a single-member limited liability company, where the sole member is _____.

DISCUSSION:

REAL PROPERTY TAX

I. Exempt status of _____

RPTL section 420-a provides tax exemptions for mandatory classes of not-for profits as follows:

[r]eal property owned by a corporation or association organized or conducted exclusively for religious, charitable, hospital, educational, or moral or mental improvement of men, women or children purposes or for two or more such purposes, and used exclusively for carrying out thereupon one of more of such purposes ...shall be exempt from taxation as provided in this section.

There are essentially three tests for a section 420-a tax exemption: nonprofit status, organization for exempt purposes, and use of property for exempt purposes. _____ is a New York not-for-profit corporation recognized by the IRS as qualifying for federal tax-exemption status under Section 501(c)(3) of the Code. _____ is a unique, public service organization. It is the leading third-party (i.e., non-university or college) provider of affordable student housing in New York City and the surrounding metropolitan area. As such it currently provides more than 6000 dormitory beds for college and graduate students. Moreover, it should be noted that _____ is the only non-university or college that is expressly authorized by New York State legislation to utilize the funding provided through the issuance of DASNY bonds for student and faculty housing.

Case law tends to support the granting of section 420-a tax-exempt benefits for real property used for the creation of dormitories. "Dormitories ... are essential parts of universities and colleges and have been held to be tax exempt based upon the theory that education contemplates not only the mental and moral but the physical training and welfare and the proper maintenance of those in attendance at the institution."

University of Rochester v. Wagner, 408 N.Y.S 2d 157, (4th Dept 1978). Moreover, the courts have also held that dormitory functions are necessary to the college community and so further the goal of education. Matter of Faculty-Student Association of State University College at Oswego v. Sharkey, 35A.D.2d 161, aff'd 29 N.Y. 2d 621(1971).

While virtually all reported cases concerning section 420-a educational exemptions for dormitory houses are for organizations affiliated with a particular college or university, the lack of such affiliation does not necessarily preclude an organization such as _____ from qualifying for a section 420-a exemption. _____ is unique in that it has been authorized by an act of the Legislature to gain access to and utilize DASNY for financing student housing in New York City. The Justification in the memorandum in support of legislation indicated that there were 700,00 students attending institutions of higher learning in the greater NYC metropolitan area and at least 10,00 students in need of housing. In addition the certificate of incorporation of _____ indicates that its purposes include acquiring residential facilities for students and teachers of educational institutions at the lowest possible cost and conducting programs of education to increase the awareness of the public to the existence of the housing problem affecting students and teachers, as well as the necessity for finding solutions to the aforesaid housing problem. In view of the above, it is the opinion of this office that _____ is organized or conducted for educational purposes under section 420-a.

II. Exempt status of a single-member limited liability company.

_____ intends to purchase real property in New York City from unrelated, non-tax exempt third parties, and then in a timely manner thereafter contribute such real property to a single member LLC with _____ as the sole member. As the statute specifically requires ownership, the first issue that has to be addressed is whether a LLC is a “corporation or association organized or conducted exclusively for” an exempt purpose pursuant to RPTL section 420-a.

A LLC is defined by section 102(m) of the NYS Limited Liability Company Law (“LLCL”) as “an unincorporated organization organized of one of more persons having limited liability for the contractual obligations and other liabilities of the business (...), other than a partnership or trust, formed and existing under this chapter and the laws of this state.” In Mononk Trust v. Board of Assessors of Town of Gardiner, 47 N.Y.2d 476, the court of appeals held that a trust was an association within the meaning of section 421 (predecessor to section 420-a). The court then said that “[w]hatever the meaning of the term ‘corporation or association’ in another context, the phrase has long been understood in tax exemption statutes of this sort ... simply to indicate that the particular organization granted the exemption need not be incorporated. Although the word ‘corporation’ is strictly defined in the law, the word ‘association’ is a broad term which may be used to include a wide assortment of differing organizational structures including trusts, depending on the context.” 47 N.Y.2d at 482-83. Therefore, the term ‘association’ appears broad enough to include a limited liability company.

IRS regulations permit a single-member LLC to be disregarded from its owner for federal income tax purposes, in which case the entity would be treated as a branch or division of the owner. Therefore, an owner that is exempt from taxation under section 501 (a) of the IRC must include, as its own, information pertaining to the finances and operations of a disregarded entity in its annual information return (Form 990). IRS Announcement 99-102 (October 13, 1999).

Under federal “check-the-box” regulations, a single member LLC is disregarded as a separate entity from its owner unless the owner affirmatively elects corporate tax treatment. Treas. Reg. Section 301.7701-3(b)(1)(ii) 2001. Neither _____ nor the LLC will make this election and for federal tax purposes, the transferred real property will be treated as though _____ owned it directly. Thus for federal tax purposes, the

single-member LLC will have no tax status of its own and will be treated as a branch of an exempt educational institution.

Where a separate not-for-profit “operates solely to carry out a purpose of the exempt corporation” and the property is used exclusively to benefit a separate exempt organization, the Court of Appeals has held that property may be exempt under section 420-a, even though title is held by a related not-for-profit organization. St. Joseph’s Properties v. Srogi, 51 N.Y. 2d 127,129 (1980). Although here the related organization is a single-member LLC and not a not-for-profit corporation, the reasoning remains applicable. “While exemption statutes should be construed strictly against the taxpayer seeking the benefit of the exemption, an exemption so literal and narrow that it defeats the exemption’s settled purpose is to be avoided.” Symphony Space v. Tishelman, 60 N.Y. 2d 33 (1983).

It must be considered, however, that the LLC is not statutorily a not-for-profit entity. LLCL section 201 states that “[a] limited liability company may be formed under this chapter for any lawful business purpose or purposes....” The term “business” is defined as “every trade, occupation, profession or commercial activity.” See, LLCL section 102 (e). The Practice Commentary to the LLCL notes that “although the LLCL does not expressly prohibit the formation of not-for-profit LLCs, the definition of ‘Business’ in section 102(e)...suggests that the drafters intended that a LLC was to be formed for pecuniary profit.” LLCL Practice Commentary at 7 (McKinney 2001-02); see also Karon S. Walker, New York Limited Liability companies and partnerships section 15.8, at 358 (1995). Accordingly, to retain the exemption, the LLC’s articles of organization and/or operating agreement, as appropriate, should provide an organizational purpose consistent with section 420-a and specify that the LLC could not receive pecuniary profit or otherwise operate in any manner inconsistent with a not-for-profit organization.

Therefore, property owned by a single-member LLC, where the single-member is a not-for-profit educational organization, may qualify for a RPTL section 420-a exemption where the applicant establishes that:

1. The LLC’s sole member qualifies for a section 420-a tax exemption. The LLC must also show that it is effectively a not-for-profit entity, organized or conducted for section 420-a purposes.
2. The articles of organization and/or operating agreement of the LLC, as appropriate, must state there will be no pecuniary profit and the LLC will operate for not-for-profit purposes consistent with section 420-a;
3. There must be commonality between the management of the LLC and its single-member;
4. The property must be managed and maintained by the single-member;
5. Rent may not exceed carrying, maintenance and depreciation charges as specified in section 420-a;
6. Upon termination of the LLC, the property must revert to _____ or another exempt entity. Also, transferring any interest in the LLC to a non-qualifying entity will result in loss of the exemption; and
7. Both, the LLC and _____ must annually file an affidavit stating that there has been no change in the LLC’s beneficial ownership. This affidavit will be in addition to the certifications of continuing use otherwise required by DOF.

Upon transfer of the real property to the LLC, a new section 420-a application must be filed with the Exemption Unit. Based on the facts provided and assuming the criteria established above are satisfied, the property would qualify for exemption under the educational category of RPTL section 420-a. The foregoing conclusions are based solely on the facts set forth above as provided to the Office of Legal Affairs. DOF reserves the right to review the information submitted.

REAL PROPERTY TRANSFER TAX

The RPTL applies to each deed conveying an interest in New York City real property when the consideration for the real property exceeds \$25,000.00. Code section 11-2102(a). Code section 11-2101.9 defines "consideration" as the price paid or required to be paid for the property and includes the amount of any indebtedness on the property, whether or not that indebtedness is assumed.

III. Transfer of real property to an exempt entity

Code section 11-2106(b) exempts certain deeds, instruments and transactions from the RPTT. When that section applies both the grantor and the grantee are exempt. Code section 11-2106(b)(2) exempts conveyances of real property by or to any corporation:

...organized and operated exclusively for religious, charitable, or educational purposes,...and no part of the net earnings of which inures to the benefit of any private shareholder or individual and no substantial part of the activities for which is carrying on propaganda, or otherwise attempting to influence legislation; provided , however, that nothing in this paragraph shall include an organization operated for the primary purpose of carrying on a trade or business for profit, whether or not all of its profits are payable to one or more organizations described in this paragraph.

Code section 11-2106(b)(2) closely resembles IRC section 501(c)(3), which exempts certain religious, charitable, and educational organizations from federal income tax. Code section 11-2106(b)(2) does not expressly require an organization to have received a federal exemption under IRC section 501(c)(3) to be exempt from the RPTT. It is equally true that the mere granting of a section 501(c)(3) exemption by the IRS is not sufficient to establish an exemption under Code section 11-2106(b)(2). In this case however, based upon all of the facts listed above, we have concluded that this transaction will be considered exempt under Code section 11-2106(b)(2).

Based upon the fact that the IRS granted an exemption under IRC section 501(c)(3) in 1991, and our independent review of the facts in this matter, it is the opinion of this office that satisfies the requirements for exemption under Code section 11-2106(b)(2). Thus, the RPTT will not be imposed upon the transfer of the property by a Grantor to as Grantee. However, notwithstanding the exemption hereby granted pursuant to this ruling, the Grantor must report the transfer on form NYC RPT and should attach a copy of this ruling to that return.

DOF reserves the right to verify the information submitted.

IV. Transfer of real property to single-member limited liability company.

After purchases real property in New York City from unrelated, non-tax exempt third parties, it is intention to contribute such real property to a single member LLC with as the sole member. Since

Code section 11-2106(b)(2) exempts conveyances of real property by a qualifying corporation as well as to a qualifying corporation, the conveyance by _____ to the single member LLC will also be exempt under Code section 11-2106(b)(2).¹

Once again DOF reserves the right to verify the information submitted.

Very truly yours,

Dara Jaffe
Assistant Commissioner
Office of Legal Affairs

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¹ The conveyance would also be exempt as a mere change of form. Under Code section 11-2106(b)(8), a deed conveying an interest in real property that effects a mere change of identity or form of ownership is exempt from the RPTT to the extent that the beneficial ownership of the property remains the same. In this case, before the proposed conveyance would own 100% of the property. Following the conveyance, the LLC which is 100% owned by _____ would own the property. Thus, there would be no change in the property's beneficial ownership as a result of the proposed conveyance, and that conveyance would be exempt from the RPTT under Code section 11-2106(b)(8).