NEW YORK CITY TAX APPEALS TRIBUNAL
ADMINISTRATIVE LAW JUDGE DIVISION

In the Matter of the Petition of VESTRY ACQUISITION LLC	:	DETERMINATION TAT(H) 15-14(RP)

Chu-Fong, A.L.J:

On March 13, 2014, Vestry Acquisition LLC (Petitioner) filed a Petition for a Hearing (Petition) with the New York City (City) Tax Appeals Tribunal (Tribunal) to review a Notice of Determination (Notice) issued by the City Department of Finance (Respondent), dated December 15, 2014, which asserts a liability for Real Property Transfer Tax (RPTT), under Chapter 21 of Title 11 of the Administrative Code of the City of New York (Administrative Code), for a transfer that occurred on March 27, 2012.

Petitioner was represented by Robert G. Goldberg, Esq., of Meister Seelig & Fein, LLP. The Commissioner of Finance of the City of New York was represented by Amy H. Basset, Esq., Assistant Corporation Counsel.

On December 18 and 21, 2015, pursuant to Section 1-09 (f) of the Tribunal Rules of Practice and Procedure, the parties agreed to have this matter determined on submission without the need for appearance at a hearing. On the same dates, the parties filed Stipulated Facts and Exhibits. A briefing schedule was set with

the final brief filed on August 24, 2016, which date began the six-month period for the issuance of this determination.

ISSUES

I. Whether Petitioner established that its March 27, 2012 real property transfer is exempt from RPTT based on a 50% change in beneficial ownership, as opposed to a 75% change.

II. Whether penalties should be abated.

FINDINGS OF FACT

1. On November 21, 2002, Harlan Waskal, Charles Dunne, and Andreas Kaubisch formed Petitioner as a limited liability company (LLC) under the laws of the State of Delaware. On the same date, Petitioner became authorized to conduct business in the State of New York. Petitioner sponsored a condominium development at 31-33 Vestry Street in New York City, New York 10013.

2. Petitioner's operations were controlled by the LLC Agreement of Vestry Acquisition LLC (Agreement), which Messrs. Waskal, Dunne, and Kaubisch entered into on November 20, 2002.

3. As relevant to this matter, in Section VI (Section 6), the Agreement outlines the procedures regarding the "TRANSFER OF INTEREST AND WITHDRAWALS OF MEMBERS."

4. Section 6.1.1 provides seven conditions that must be met in order to affect a transfer of rights or interests (Agreement, p. 21). Among the requirements are approval from all the other

Members (Agreement, § 6.1.1.67 [sic], p. 21), and compliance with "Right of First Offer" provision (Agreement, § 6.1.6, pp. 21-22).

5. The Agreement's "Right of First Offer" section provides the following:

> "If an Interest Holder (a 'Transferor') desires to Transfer all or any portion of, any interest or rights in, the Transferor's Interest (the 'Transferor Interest'), the Transferor shall notify the other Members of that desire (the 'Transfer Notice'). The Transfer Notice shall describe the Transferor Interest. The other Members shall each have the option (the 'Purchase Option') to purchase all of the Transferor Interest for a price (the 'Purchase Price') equal to the Appraised Value (as determined pursuant to Section 6.4)" (Agreement, § 6.1.4.1, pp. 21-22).

6. Additionally, Section 6 provides the following regarding transfers that fail to comply with its provisions:

> "Each Member hereby acknowledges the reasonableness of the prohibition contained in this Section 6.1 in view of the purposes of the Company and the relationship of the Members. The Transfer of any Membership Rights or Interest in violation of the prohibition contained in this Section 6.1 shall be deemed invalid, null and void, and of no force or effect. Any Person to whom Membership Rights are attempted to be transferred in violation of this Section shall not be entitled to vote on matters coming before the Members, participate in the management of the Company, receive distributions from the Company, or have any other rights in or with respect to the Membership Rights" (Agreement, § 6.1.3, p. 21).

To summarize the foregoing, the Agreement invalidates any transfer of rights or interests that fails to comport with its terms.

7. The Agreement provided at Section 4.1.2, among other interests and rights, the ability for each Member to receive a distribution of one or more condominium units:

> "Notwithstanding any other provision hereof, each Interest Holder shall have an option to receive a distribution of one or more condominium units for personal or investment use, if any are created by the Company, provided all other Interest Holders receive equivalent pro rata distributions of cash or property in proportion to their Percentages. The designation of condominium units pursuant to this option shall be made prior to the commencement of any sales or marketing activities by the Company with respect to any condominium units" (Agreement, § 4.1.2, p. 11).

8. As relevant to the forgoing, Section 1 of the Agreement defines the term "Percentages" to mean, "...as to a Member, the percentage set forth after the Member's name on Exhibit A, as amended from time to time" (Agreement, p. 6).[1] The referenced Exhibit A provides, in relevant part, the following information:

Harlan Waskal	$275,000.00	50%
Charles Dunne	$137,500.00	25%
Andreas Kaubisch	$137,500.00	25%

9. Section 9.5 of the Agreement provides the following:

> "This Agreement constitutes the complete and exclusive statement of the agreement among the Members. It supercedes all prior written and oral statements, including any prior representation, statement, condition, or warranty. Except as expressly provided otherwise herein, this Agreement may not be amended

[1] This section does not reference any other figure other than the number listed within the Exhibit A chart. There is no accounting for distributive share of Petitioner's profits or ownership. Rather, it only references the percentage set forth after the names on the chart.

without the written consent of all of the Members" (Agreement, p. 28).

The record contains no amendments or changes to Exhibit A that comport with either Section 6 or Section 9.5 of the Agreement.

9. The condominium development at 31-33 Vestry Street, which Petitioner sponsored, contained seven condominium units. By 2012, five of the seven units had sold, leaving only two remaining units.

10. A September 5, 2006 letter from Mr. Kaubisch to Mr. Dunne (2006 Letter) indicates that the two reached an agreement regarding the exercise of their rights to acquire a condominium unit in the 31-33 Vestry building. This letter provides the following:

> "Reference is hereby made to that certain LLC Agreement of Vestry Acquisition LLC (the 'Vestry Agreement') dated as of the 20th day of November, 2002. All terms not otherwise defined herein shall have the meanings assigned to them in the Vestry Agreement.
>
> "As previously agreed, in connection with the potential development of a building (the 'Vestry Building') to be located at 31-33 Vestry Street, New York, New York, you and I may collectively have the right to retain one residential unit at the Vestry Building (the 'Retained Vestry Unit').
>
> "This letter shall confirm that in consideration for one dollar and other good and valuable consideration, the receipt of which is hereby acknowledged, I hereby relinquish any right I might have to the Retained Vestry Unit to you. As a consequence of such relinquishment, my proportionate share of any additional Capital Contribution required in accordance with Section 3.2.1 of the Vestry Agreement shall be reduced by a fraction, the numerator

> of which shall be fifty percent of the square footage of the Retained Vestry Unit, and the denominator of which shall be the square footage of the Vestry Building, all as finally determined. Consequently, your proportionate share of any Capital Contribution required in accordance with Section 3.2.1 of the Vestry Agreement shall be increased by like amount."

While the document presents neither a notarization nor a postmark, the signature of Mr. Kaubisch appears beneath the letter, and Mr. Dunne signed beneath a line stating "Agreed and Accepted." The record does not indicate that Messrs. Kaubisch and Dunne provided notice to Mr. Waskal, or complied with the other terms provided under Section 6 of the Agreement.

11. In 2012, Mr. Dunne exercised his rights under the Agreement's Section 4.1.2. On March 27, 2012, Petitioner distributed a condominium unit to Mr. Dunne for total consideration of $10,000,000.00. On April 4, 2012, a RPTT return was filed for the transfer, showing tax due of $71,250.00 on the consideration of $5,000,000.00, which represented a 50% change in beneficial ownership times the total consideration (i.e., $10,000,000.00). At the same time as the filing, Petitioner paid the reported $71,250.00 shown due.

12. Respondent conducted a review of the subject RPTT, in which it requested various documents from Petitioner, including the Agreement. Based upon its examination, it concluded that, prior to the transfer, Mr. Dunne possessed 25% beneficial ownership in the condominium unit, not 50% as provided on the RPTT return. On December 15, 2014, Respondent issued the Notice to Petitioner, which assesses additional RPTT due in the amount

of $35,625.00 with interest. Respondent also asserted penalty on that amount.

SUMMARY OF THE PARTIES' POSITIONS

Petitioner contends that the RPTT return properly reported a 50% change in beneficial ownership. It claims that the 2006 Letter modified the Agreement, such that Mr. Dunne obtained Mr. Kaubisch's right to obtain 25% of a condominium unit. As such, Petitioner claims that Mr. Dunne possessed 50% beneficial ownership prior to the transfer, and that the RPTT return properly reported only a 50% change. In the alternative, it submits that the 50% change is correct because, upon dissolution, Mr. Dunne possessed a greater than 50% interest in the profits, losses, distribution, and rights in Petitioner. Given the foregoing, Petitioner requests that Respondent's determination be found erroneous, and the Notice be cancelled.

Respondent contends that Petitioner failed to carry its burden of proving that there was a 50% change in beneficial ownership. Citing to the Agreement, it notes that Mr. Dunne possessed 25% of the condominium unit prior to the sale, thus, the change was 75%. Respondent argues that the 2006 Letter was ineffective, and that, contrary to Petitioner's alternative argument, Mr. Dunne only held 25% interest in Petitioner. As such, Respondent requests that the Petition be denied and the Notice sustained.

CONCLUSIONS OF LAW

The Administrative Code imposes a tax upon all transfers of real property in excess of $25,000.00 (Administrative Code § 11-2102); however, it also exempts certain transfers from taxation, including those in which the beneficial ownership of such real property or economic interest remains the same (Administrative Code § 11-2106 [b] [8]; 19 RCNY § 23-05 [b] [8]).[2]

Petitioner and Respondent disagree over whether the March 27, 2012 transfer represents a 50% or 75% change in beneficial ownership. It must be observed, tax exemptions exist as matters of legislative grace (*Matter of Grace v New York State Tax Commn.*, 37 NY2d 193, 196 [1975]), and the taxpayer bears the burden of proof (Administrative Code § 11-2103). Herein, in order for Petitioner to prevail, the evidence must establish that Respondent erroneously determined that there was a 75% change in beneficial ownership where there was, in fact, a 50% change. In order to determine Mr. Dunne's percentage ownership prior to the transfer, the Agreement must be analyzed.

The Agreement contains clear and unambiguous terms and language, including its members' right to receive a condominium unit under Section 4.1.2 (Agreement, p. 11). This clause requires the distributions to be in accordance with each Members' Percentages, which Section 1 defines as, "the percentage set forth after the Member's name on Exhibit A, as amended from time

[2] As a concept, beneficial ownership remains amorphous, broadly defined as the difference between the economic interest prior and subsequent to the transfer (Administrative Code § 11-2106 [b] [8]; 19 RCNY § 23-05 [b] [8]). In this matter, the parties have not presented conflicting definitions of this term. Both agree that Mr. Dunne, as a member in Petitioner, possessed beneficial ownership of the condominium unit prior to the transfer; the parties only disagree as to the percentage of such beneficial ownership.

to time" (Agreement, § 1, p. 6). Exhibit A lists 25% after Mr. Dunne's name. Reading the foregoing provisions of the Agreement together, Mr. Dunne owned 25% of the distributed condominium unit prior to the transfer. Subsequent to Petitioner's distribution, Mr. Dunne owned 100%. As a result, the transfer resulted in a 75% change in beneficial ownership of the condominium unit.

Petitioner claims that under the 2006 Letter and the Agreement, Mr. Dunne acquired Mr. Kaubisch's interest or right to a distribution of a condominium unit from Petitioner. It further notes that Mr. Dunne possessed a greater than 50% interest in Petitioner's profits and losses. For these reasons, Petitioner claims that Mr. Dunne possessed a 50% interest in the condominium unit prior to the March 27, 2012 transfer.

Section 4 of the Agreement does not reference profits or ownership of Petitioner. Rather, the Agreement clearly ties a member's interest in a distributed condominium unit to his "Percentage," which, as defined in Section 1, was listed in Exhibit A to the Agreement. The record contains no document that both changes Mr. Dunne's percentage in Exhibit A to 50%, and that contains the "express written consent" of all Members, as required by Section 9.5 (Agreement, p. 28). As such, it must be concluded that prior to the March 27, 2012 transfer, the members did not amend the percentages in Exhibit A.

Further, in considering whether the 2006 Letter transferred rights from Mr. Kaubisch to Mr. Dunne,[3] the parties failed to

[3] The 2006 Letter refers to the "right" to a distribution of condominium unit under Section 4.1.2. The requirements under Section 6 apply to the transfer of all or any portion of a member's interest or "rights" in Petitioner. Any transfer between Messrs. Kaubisch and Dunne must comply with the Agreement's terms.

comply with the Agreement's terms. Specifically, the record contains no evidence of either approval from all the members (Agreement, §§ 6.1.1.67 [sic], p. 21; 9.5, p. 28), or a Transfer Notice to Mr. Waskal, as required by Section 6.1.4.1 (Agreement, pp. 21-22). Under the terms of the Agreement itself, an attempted transfer, which fails to comply with its provisions, must be rendered null and void (Agreement, § 6.1.3, p. 21). Therefore, inasmuch as the 2006 Letter purports to transfer rights between Messrs Kaubisch and Dunne, it must be held null and void under the Agreement.

Indeed, reaching the conclusion favored by Petitioner requires ignoring entire provisions of the Agreement. The clear and unambiguous terms of the Agreement prevent any modifications (*see e.g. Fineman Family LLC v Third Ave. N. LLC*, 90 AD3d 549, 551 [1st Dept 2011]; *Arfa v Zamir*, 63 AD3d 484, 485 [1st Dept 2009]). With regard to transferring rights or interests in an LLC, the Courts have held that the parties must strictly adhere to the terms of the company's operating agreement(*see e.g. Gartner v Cardio Ventures, LLC*, 121 AD3d 609 [1st Dept 2014]), which further militates against finding the 2006 Letter to be an effective transfer. Petitioner has failed to clearly establish that the subject transfer constituted a 50% change in beneficial ownership.

The next issue to be determined is whether Respondent properly imposed penalties under Administrative Code § 11-2114 (b) (3). This section provides that a penalty may be imposed on a real property transfer, stating:

"Failure to pay tax required to be shown on return. In case of failure to pay any amount in respect of any tax required to be shown on a return required to be filed under this chapter which is not so shown (including a determination made pursuant to section 11-2107 of this chapter) within ten days of the date of a notice and demand therefor, unless it is shown that such failure is due to reasonable cause and not due to willful neglect, there shall be added to the amount of tax stated in such notice and demand one-half of one percent of such tax if the failure is not for more than one month, with an additional one-half of one percent for each additional month or fraction thereof during which such failure continues, not exceeding twenty-five percent in the aggregate.
For the purpose of computing the addition for any month, the amount of tax stated in the notice and demand shall be reduced by the amount of any part of the tax which is paid before the beginning of such month" (Administrative Code § 11-2114 [b] [3]).

In this case, Petitioner remitted the tax shown to be due on the RPTT return with the filed RPTT return, and its calculation of the tax due was not baseless. As a whole, the record shows a lack of willful neglect. Further, while it has been concluded that the members' failure to strictly adhere to the Agreement was dispositive of Issue I, it also presents reasonable cause for the underpayment. As a result, penalties are abated.

Accordingly, it is determined that:

1. The petition of Vestry Acquisition LLC is granted to the extent that the penalty imposed under Section 11-2114 (b) (3) of the Administrative Code is cancelled, but in all other respects, is denied.

2. The Notice of Determination, dated December 15, 2014, is modified to the extent provided in Paragraph "1" above, but is otherwise sustained.

IT IS SO ORDERED.

DATED: February 7, 2017
New York, New York

/s/
Alexander F. Chu-Fong
Administrative Law Judge