

**NEW YORK CITY TAX APPEALS TRIBUNAL
ADMINISTRATIVE LAW JUDGE DIVISION**

In the Matter of the Petition	:	
	:	
of	:	<u>DETERMINATION</u>
	:	TAT(H) 05-10(RP)
LOUIS M. HUBRECHT	:	
	:	

Hauben, D.C.A.L.J.:

Petitioner, Louis M. Hubrecht, filed a Petition with the New York City ("City") Tax Appeals Tribunal ("Tribunal") requesting redetermination of a deficiency of City Real Property Transfer Tax ("RPTT") under Chapter 21 of Title 11 of the City Administrative Code (the "Code") in connection with the grant, on September 7, 2001, of a leasehold interest in two buildings in Manhattan located at 698-700 Madison Avenue.

The parties consented to have the controversy determined on submission without a hearing pursuant to 20 RCNY §1-09(f) of the Tribunal's Rules of Practice and Procedure. The parties submitted a Joint Stipulation of Facts, with accompanying exhibits. Petitioner was represented by Kenneth Rubinstein, Esq., of Rubinstein & Rubinstein LLP. The Commissioner of Finance was represented by George P. Lynch, Esq., Assistant Corporation Counsel. Frances J. Henn, Esq., Assistant Corporation Counsel participated on the briefs. Each party submitted a brief and a reply brief. The final brief was received on August 24, 2007.

ISSUE

Whether the advance payment of all the rent payable to Petitioner under a long-term triple-net lease is consideration subject to the RPTT.

FINDINGS OF FACT

1. Petitioner, Louis M. Hubrecht, is the owner of two adjacent buildings located at 698 and 700 Madison Avenue¹ in Manhattan (the "Premises"). The Premises are attached brownstones that have been in Petitioner's family since the 1930's. During 2001, the Premises were used for both residential and commercial purposes. Petitioner managed the Premises.

2. During the 1990's, Petitioner's health deteriorated. For several years prior to 2001, it became increasingly more difficult for Petitioner to manage the Premises.

3. In September 2000, Petitioner, then in his late sixties, was arrested for fatally shooting one of the residential tenants of the Premises. Petitioner's bail agreement prohibited the sale of the Premises. According to Petitioner, he realized that he needed to provide for his family during his likely incarceration; yet he wished to keep the Premises in the family after he died regardless of the outcome of his trial. Petitioner sought advice from the law firm of Rubinstein & Rubinstein, LLP regarding the management of the Premises and financial planning for him and his family. Petitioner decided that net leasing the Premises for a single,

¹ Block 1377, Lots 17 and 56.

lump-sum payment best suited his needs. Petitioner then retained Daniel J. Altman, Esq., of Belkin, Burden, Wenig & Goldman, LLP, to solicit offers to lease the Premises.

4. During the summer and fall of 2001, Petitioner received several offers to lease the Premises on a long-term, net-lease basis for one lump-sum, up-front payment. Petitioner also received several unsolicited offers to purchase the Premises, all of which were rejected.

5. Petitioner accepted an offer from 700 Madison Partners (the "Lessee") to lease the Premises for a period of 49 years less one day commencing September 7, 2001, after which the Lessee's rights to the Premises would terminate and the Premises would revert back to Petitioner or his heirs (the "Lease"). The entire rent payable to Petitioner under the Lease, \$7,250,000, was paid in a lump sum at the commencement of the Lease (the "Payment"). Various lease provisions required Lessee to maintain the Premises at its own expense and pay all property taxes and other charges associated with the operation of the Premises during the term of the Lease. Lessee leased the premises subject to existing residential and commercial leases. Lessee had the right to improve the property at its own expense. Lessee agreed to take no action that would diminish the value of Petitioner's fee interest.

6. Lessee had the right to mortgage its leasehold interest in the Premises as well as to sublease the Premises. Lessee also was required to maintain insurance on the Premises.

7. The Lease neither provided for an extension of the lease term nor granted Lessee an option to purchase the Premises. Lessee had the right of first refusal in the event that, during the term

of the lease, a third party offered to purchase the Premises on terms that were acceptable to Petitioner. If such right of first refusal was exercised, Lessee would receive a credit of \$8,000,000 towards the purchase price. Lessee was given a security interest in and lien on Petitioner's fee estate and improvements.

8. In 2004, Lessee offered to purchase fee title to the Premises from Petitioner for \$500,000, which offer was refused.

9. On June 23, 2004, Respondent issued a Notice of Determination against Petitioner with respect to the Lease that asserted a real property transfer tax deficiency in the amount of \$190,312.50, with interest of \$36,582.60² and penalties of \$3,806.25, for a total deficiency of \$230,701.35. The Notice of Determination explained that the "transfer of Real Property o[r] interest in Real Property in exchange for consideration is subject to the Real Property Transfer Tax." The asserted deficiency was predicated on Respondent's determination that the \$7,250,000 pre-payment of rent was consideration subject to RPTT.

10. On or about December 2006, Howard C. Gelbtuch, MAI, CRE, FRICS, a principal of Greenwich Realty Advisors, Inc., performed an appraisal of the Premises' fair market sale value and fair market rental value for a net lease as of the starting date of the Lease. Mr. Gelbtuch concluded that the fair market sale value of the Premises in September 2001 was \$10,600,000 and that the fair market rental value for a 49-year net lease of the Premises in September 2001 was \$7,300,000.³

² Computed to July 23, 2004.

³ Petitioner also submitted an appraisal of the value of the Premises as of September 2000, one year before the Lease was entered into.

11. For federal income tax purposes, Petitioner reported the \$7,250,000 lump-sum payment as rent amortizable over the lease term pursuant to Section 467 of the Internal Revenue Code.⁴

STATEMENT OF POSITIONS

Petitioner contends that his grant of a leasehold interest is not subject to the RPTT since the amount prepaid under the Lease is rent for the use and occupancy of the Premises which is not consideration subject to the RPTT.

Respondent contends that the grant of a leasehold interest is subject to the RPTT with the amount subject to the RPTT being the amount paid that is not subject to the City Commercial Rent or Occupancy Tax (the "CRT"). Respondent argues that the entire prepayment under the Lease is consideration to obtain the leasehold and is not a payment for the use or occupancy of the Premises.

CONCLUSIONS OF LAW

Petitioner entered into a Lease Agreement with Lessee for a term of 49 years less one day for rent of \$7,250,000, all of which was paid in advance. Lessee also was obligated during the term of the Lease to pay the real property tax and other expenses of the Premises that would come due so that the amount paid to Petitioner was net of all expenses of the Premises. Lessee was responsible for maintaining the Premises during the lease term. Lessee had the right to improve the Premises at its own expense and the right to

⁴ It is noted that on March 13, 2003, the New York State Department of Taxation and Finance notified Petitioner that it had determined that "the leasehold grant is not subject to the Real Estate Transfer Tax, as it does not meet the criteria described within Section 1401(e)(i) of Article 31 of the Tax Law." Under that section, leaseholds for forty nine years or more are subject to the transfer tax. The Lease is for one day less than forty nine years.

mortgage its leasehold interest in the Premises. At the end of the lease term, the Premises, including any improvements made by Lessee, would revert to Petitioner.

The RPTT is imposed on the transfer of real property by deed when the consideration for the transfer exceeds \$25,000. Code §11-2102.a. A "deed" includes a "document or writing whereby a leasehold interest in real property is granted" Code §11-2101.2. The parties agree that Petitioner granted a leasehold interest to Lessee.⁵ Where there is a grant of a leasehold interest, the Code subjects to RPTT that amount which "is not considered rent for purposes of the [CRT]." Code §11-2102.a(10)(iii). Under the CRT, rent is "the consideration paid or required to be paid by a tenant for the use or occupancy of premises." Code §11-701.6. The only issue in this matter is whether any part of the Payment is consideration subject to the RPTT. To the extent that the Payment is found to be consideration for the use or occupancy of the Premises it is rent under the CRT and no RPTT is due on that amount.

Normally, payments to a landlord pursuant to a lease are for the use or occupancy of the premises. In this matter, Lessee paid Petitioner \$7,250,000 to obtain the use and occupancy of the Premises for the term of the Lease. Petitioner's unchallenged appraisal of the fair market rental value of the Premises on a triple net basis confirms that the Payment was entirely to rent the property; *i.e.*, that it was for the use and occupancy of the Premises. That the entire amount of rent is paid at the start of

⁵ In its brief, Respondent noted that "this is a transaction to which the RPTT applies, as a grant of a leasehold interest." Respondent's Brief, p. 2. Respondent further stated that she "does not argue that [the transaction] was a [sic] outright sale, a disguised sale, or in any sense whatsoever a conveyance of the fee estate or any part thereof." Respondent's Brief, p. 20.

the lease term does not change its character from rent into something else. See, *Matter of the Petition of Automatic Data Processing, Inc.*, 1991 N.Y. City Tax Lexis 127 (N.Y.C.D.O.F. 1991). Nor does the Lease's term of 49 years less one day alter that conclusion.⁶ Respondent's assertion that no part of the rent payable to Petitioner under the Lease was for the use or occupancy of the Premises is not supported by the record. The Payment was entirely rent "for the use or occupancy of premises" within the meaning of Code §§11-701.6 and 11-2102.a(10)(iii) and thus is not consideration subject to the RPTT.

To support its position, Respondent relies primarily on bankruptcy cases where the issue was whether, for bankruptcy purposes, a "lease" should be treated as a sale, financing arrangement or something else other than a lease. See, *International Trade Admin. v. Rensselaer Polytechnic Inst.*, 936 F.2d 744, (2d Cir. 1991); *In Re PCH Associates*, 804 F.2d 193 (2nd Cir. 1986); *In Re Morregia & Sons*, 852 F.2d 1179 (9th Cir. 1988); *Matter of Tak Broadcasting Corporation v. C.T. Robertson*, 137 B.R. 728 (U.S.D.C., Wisc. 1992). Taking into account various factors, including prepaid rent, long lease terms and the shifting of obligations between landlord and tenant in net leases, these cases concluded that certain leases should be categorized as something other than a lease for bankruptcy purposes; *i.e.*, as sales or financing arrangements. Respondent, however, concedes that the transaction at issue is the grant of a leasehold interest. Respondent further concedes that there was no sale. Finally, there is no claim that this was a financing arrangement, which in any event would not appear to be subject to the RPTT. Thus, the cases

⁶ The traditional obligations and duties of lessors and lessees often are shifted in triple net leases, many of which are long-term leases.

cited by Respondent, having no bearing on the issue of whether the Payment was for the use or occupancy of the Premises, are irrelevant.

All other arguments raised have been considered and are found to be without merit.

ACCORDINGLY, IT IS CONCLUDED THAT the Payment was consideration solely for the use or occupancy of the Premises and is not consideration subject to the RPTT. The Petition of Louis M. Hubrecht is granted and the Notice of Determination dated June 23, 2004 is cancelled.

DATED: February 21, 2008
New York, New York

WARREN P. HAUBEN
Deputy Chief Administrative Law Judge