NEW YORK CITY TAX APPEALS TRIBUNAL
ADMINISTRATIVE LAW JUDGE DIVISION

In the Matter of the Petition	:	**DETERMINATION**
of	:	**TAT(H) 01-23(RP)**
RHM-88, LLC	:	

Murphy, A.L.J.:

Petitioner, RHM-88 LLC, filed a Petition for Hearing with the New York City ("City") Tax Appeals Tribunal ("Tribunal") requesting a redetermination of a deficiency of City Real Property Transfer Tax ("RPTT") assessed with regard to a transaction which occurred on July 23, 1997 ("Transfer Date").[1]

Petitioner was represented by Richard A. De Palma, Esq. and Brian T. Belowich, Esq., presently of Baker & McKenzie, LLP. The Commissioner of Finance ("Respondent") was represented by George P. Lynch, Esq., Assistant Corporation Counsel. Robert J. Firestone, Esq., Assistant Corporation Counsel, participated on the briefs.

A hearing was held on April 14, 15, and 16, 2004, at which time evidence was admitted, testimony was taken and a stipulation of facts and exhibits were submitted.

Petitioner submitted a Post-Trial Brief on November 12, 2004; Respondent submitted a Brief on February 4, 2005; Petitioner submitted a Post-Trial Reply Brief on March 4, 2005; and Respondent submitted a Sur-reply Brief on April 11, 2005.

[1] The Petition was filed on October 9, 2001. An Amended Petition, dated October 15, 2001, was filed to include an Affidavit of Service and add one page to Exhibit C.

ISSUES

I. Whether the July 27, 1997 payment of $36,500,000 by Petitioner to the United Nations Development Corporation ("UNDC") pursuant to a sublease agreement represented payment for the transfer of a sublease interest in Two U.N. Plaza that is subject to RPTT, rather than a payment of rent subject to the City Commercial Rent Tax ("CRT").

II. Whether the agreements to extend the statute of limitations on assessment of RPTT extended the limitation on assessment of RPTT with respect to the sublease estate, notwithstanding that the address stated thereon was the address of an adjacent but related property.

FINDINGS OF FACT

1. Petitioner, RHM-88, LLC, is a limited liability company organized and existing under the laws of the State of Colorado. Petitioner, an affiliate of Regal Hotel Management Inc., was formed to acquire and operate the U.N. Plaza Hotel ("Hotel") located in the City.

2. The Hotel is comprised of approximately twelve floors[2] which are located contiguously in each of two towers. Each tower is situated on a separate parcel of land in the City and each has a different street address with a different block and lot designation on the tax map.

3. One tower is located at 787/793 1st Avenue, which has a tax map designation of Manhattan Block:1337, Lot:1101, County of New

[2] Pursuant to the "Plan" referenced in the Sublease and Exhibit H to the Declaration of Condominium, the hotel portion of One U.N. Plaza is comprised of floors 29 through 39 and the hotel portion of Two U.N. Plaza is comprised of floors 29 through 40.

York, State of New York (the "First Tower"). The address of the First Tower is also referred to as "One U.N. Plaza." This tower is 39 stories.

4. The other tower is located at 332/334 East 45th Street, which has a tax map designation of Manhattan Block:1337, Lot:14, County of New York, State of New York (the "Second Tower"). The address of the Second Tower is also referred to as "Two U.N. Plaza." This tower is 40 stories.

5. The land and improvements located at One U.N. Plaza, and the building located at Two U.N. Plaza, were owned by UNDC and/or the City for all relevant periods prior to the transactions with Petitioner. The land located at Two U.N. Plaza was owned by a New York general partnership, Bishop Trading Company ("Bishop"), for all relevant periods.

6. UNDC is a local development corporation, organized pursuant to the New York State Not-For-Profit Corporation Law, that is involved in the development and operation of several parcels of land located near the United Nations headquarters building in the City.

The Transactions

7. On August 1, 1972, the City leased to UNDC the land and improvements at One U.N. Plaza for a term of 99 years ("1972 City Lease"). The 1972 Lease was amended by several agreements,[3] pursuant to which UNDC constructed the improvements that comprised One U.N. Plaza.

[3] One agreement dated May 18, 1981 states that the 1972 Lease is subordinate to the Bishop Lease; one dated March 31, 1994 concerns the "Third Phase" involving 3 U.N. Plaza; and one dated March 10, 1995 concerns renting space to UNICEF.

8. On August 1, 1980, Bishop leased the land at Two U.N. Plaza ("Bishop Parcel") to UNDC for a 99-year term which expires on July 31, 2079 ("Bishop Lease").

9. The Bishop Lease provided that UNDC construct a new building on the Bishop Parcel within five years of the initiation of the lease. The building so constructed was the Second Tower. At the end of the lease period, the agreement further provides that any building constructed on the land would revert to Bishop "without payment or offset."[4] Article XXIX of the Bishop Lease permits assignment and subletting by UNDC.

10. The Bishop Lease contemplates the operation of businesses together on Lots 1101 and 14 and specifically provides that the constructed building ". . . [M]ay be connected with the building that now exists on the property immediately east of the leased premises known as One United Nations Plaza." Further, for the duration of the lease, "title to any New Building to be constructed by Tenant . . . shall remain in Tenant."[5]

11. The Bishop Lease also granted UNDC an Option to Purchase ("Bishop Option"), at fair market value, the land and the structures extant on the Bishop Parcel at the start of the lease ("Option Premises"). The Bishop Option specifically excluded the value of any subsequent structures which would be constructed by UNDC on the premises (*i.e.*, the Second Tower) since, pursuant to the Bishop Lease, UNDC would build and hold title to such improvements for the term of the lease. UNDC was required to issue, and did issue, a Special Obligation Bond of $1,250,000 to secure the Bishop Option.[6]

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[4] Bishop Lease, Article XIII, Section 1.

[5] Bishop Lease Article XIII, Section 1

[6] *See*, Bishop Option, Clause 2, which provides that should the Option not be exercised, Bishop was entitled to retain the consideration.

12. The Bishop Option can be exercised any time between August 1, 2020 and July 31, 2025, a period approximately half-way through the term of the Bishop Lease. The Bishop Lease specifically provides that UNDC may assign the Option only if UNDC entered into a transaction whereby it assigned all of its interest as a tenant, stating that it was "the intention of the parties . . . that the Option granted . . . shall at all times be held by the same entity as shall be the then tenant under [the Bishop] Lease."

13. On or about May 8, 1981, UNDC and the City amended the 1972 City Lease ("1981 Amendment"), agreeing that UNDC would: (a) construct the Second Tower on the Bishop Parcel on or before January 25, 1984 pursuant to the Bishop Lease;[7] and (b) convey the Second Tower to the City. The 1981 Amendment has a 99-year term. Pursuant to the 1981 Amendment, the parties agree that the City would lease back the Second Tower to UNDC in exchange for UNDC paying base rent, additional rent and net annual rent to the City's Real Property Division, principally from the proceeds of the building operation and other UNDC projects. The 1981 Amendment includes a provision that UNDC can exercise the Bishop Option at the request of the City; can assign its interest in the Bishop Option; or, if the Bishop Option is exercised, convey its interest in the fee on which the Second Tower is located to the City.

14. The U. N. Plaza Hotel was operated in parts of the First Tower and the Second Tower until July 1997 through a sublease from UNDC to the Hyatt Corporation.[8]

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[7] The acquisition, construction and subsequent lease of the Second Tower was approved by the Board of Estimate at the recommendation of the City Planning Commission on August 21, 1980, the same month that the Bishop Lease was entered into.

[8] It appears that the Hyatt organization operated the Hotel prior to this transaction pursuant to the "Hyatt Agreement," which agreement terminated as of the date of the Purchase and Sale. *See*, Purchase and Sale Agreement, §8.2(w). According to §16.2 of the Purchase and Sale Agreement, UNDC managed the Hotel "with support from Hyatt."

15. In 1997, the City put out for bid to several hotel owners and operators, the sale of its real property interest in the hotel portion of the First Tower and the transfer of its Sublease interest in the hotel portion of the Second Tower. Petitioner was the successful bidder.

16. On May 6, 1997, Petitioner, UNDC, the City and the New York City Economic Development Corporation ("NYCEDC") entered into a Purchase and Sale Agreement ("Purchase and Sale Agreement") for the acquisition and transfer of the City's interests in the U.N. Plaza Hotel. The Purchase Price was $102,000,000 which was allocated between the property at One U.N. Plaza, the Sublease at Two U.N. Plaza, and an amount attributable to furniture, fixtures and equipment.

17. Under the Purchase and Sale Agreement, Petitioner purchased the lobby and floors of the hotel located in the First Tower (the "Hotel Unit") as part of a condominium transfer. Pursuant to a Condominium Declaration, two units were established at One U.N. Plaza. One condominium unit was comprised of the Hotel Unit,[9] and the other condominium unit was comprised of office space on the remaining floors and common areas of Tower One. The City conveyed the Hotel Unit to NYEDC and NYEDC then conveyed the Hotel Unit to Petitioner.[10] On July 23, 1997, Petitioner acquired fee simple title to the Hotel Unit (the "Fee") for $60,651,375.

18. Article 2 of the Purchase and Sale Agreement specifically provides that UNDC "demise" to Petitioner "a Sublease estate" ("Sublease") in the portion of the hotel located in Two U.N. Plaza"

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[9] The Hotel Unit is located on the 27th through the 39th floors of Tower One and certain common areas. *See, fn. 2, supra*.

[10] NYCEDC was involved in the transaction because the City Charter required that for the City to dispose of any interest in real property, it would have to be done through a public auction, whereas if the City transferred its interest to NYCEDC, then the transaction could be a private sale.

(the "Hotel Premises"). As required, UNDC delivered the Sublease at closing in exchange for $36,500,000.

19. Section 8.4.2 of the Purchase and Sale Agreement provided that Petitioner would be responsible for paying any taxes, including (a) RPTT due on the "Real Property" (which pursuant to Section 3.1 is comprised of the "Hotel Unit and Sublease Estate, collectively") and (b) "any commercial rent and occupancy tax payable in respect to the portion of the Purchase Price allocable to the Sublease Estate."[11] The parties agreed that any RPTT payable would be credited against the purchase price that Petitioner otherwise owed UNDC.

20. On or about July 23, 1997, Petitioner filed an RPTT return reporting the purchase of the Fee for a consideration of $60,651,375, and paid $1,592,098.59 in RPTT. The return indicated the address and tax map block and lot designation for One U.N. Plaza as being Manhattan Block:1337, Lot:1101. The deed was recorded on October 29, 1997. Documents and testimony indicate that a representative of the City prepared the RPTT return.

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[11] Section 8.4.2 specifically states: "Purchaser shall pay . . . at Closing (i) any RPT[T] . . . that may be payable in connection with the transfer of the Real Property and other transactions contemplated herein, and (ii) if the conveyance of the Hotel Unit is exempt from RPT[T], any RPT[T] which would be applicable to the transfer of the Hotel Unit from EDC to Purchaser but for such exemption. Seller and Purchaser further agree that Purchaser shall receive a credit against the Purchase Price in the amount of any such RPT[T] . . . paid by Purchaser pursuant to clause (i) or (ii) of the preceding sentence. At or prior to Closing, the City, EDC, Seller and Purchaser each agree to complete and execute any returns and/or statements required in connection with the RPT[T] . . .. In addition, Purchaser shall pay any commercial rent and occupancy tax payable in respect to the portion of the Purchase Price allocable to the Subleasehold Estate, which shall be payable as and when due." Section 3.1 of the Agreement defines "Real Property" to include the Hotel Unit and the Sublease.

While UNDC and Petitioner, as Tenant, were the principal parties to the Purchase and Sale Agreement and the Sublease, a Deputy Mayor and the Acting Corporation Counsel were also signatories to each agreement. The City signed the Sublease, however, only as an acknowledgment of certain provisions of that agreement. It is noted that Petitioner does not assert that the City should be estopped from asserting RPTT liability against it with respect to the Sublease because the City was a signatory to the Purchase and Sale Agreement which provides that if RPTT is applicable with respect to the Sublease, the purchase price otherwise payable by Petitioner to UNDC would be reduced by the amount of that RPTT liability.

21. On or about July 23, 1997, UNDC and Petitioner entered into the Sublease of the Hotel Premises. The Sublease is for a fixed term of 82 years, expiring on July 30, 2079. Upon the expiration of the Sublease, the use and possession of the Hotel Premises reverts absolutely to UNDC for a period of one day; *i.e.*, until the termination of the Bishop Lease. At closing, Petitioner paid $36,500,000, which was characterized in the Sublease as rent, "for the entire term." Petitioner also agreed to pay certain enumerated Tenant's Charges.

22. Under the Sublease, the Bishop Option may be exercised by UNDC upon six months' notice[12] and proof of fiscal ability to pay. Petitioner can force UNDC to exercise the Bishop Option. If the Option is exercised, upon UNDC's acquisition of the Option Premises and conveyance to the City, the City must establish a condominium similar to the arrangement for the First Tower. The City must then transfer the condominium unit containing the Hotel Premises to NYCEDC, which must then transfer "for no additional payment" the deed to the condominium unit containing the Hotel Premises to Petitioner.

23. On or about July 23, 1997, Petitioner filed an RPTT return with respect to the Sublease, reporting the grant of the Sublease from UNDC to Petitioner. The return reported no consideration and indicated that no RPTT was due. The return stated the address and tax map block and lot designation for Two U.N. Plaza as being Manhattan, Block:1337, Lot:14. The Sublease was recorded on December 16, 1997.

24. A single unitary hotel is operated by Petitioner on the Fee and the Sublease, with a single parking facility below grade, a single entrance on 45th Street for the hotel, and a separate

[12] The term of the Notice to exercise runs from February 1, 2020 to January 1, 2025.

entrance on 45th Street for a restaurant. The entrance on First Avenue is strictly for the U.N. office space in the building and provides no access to the hotel.

25. The Purchase and Sale Agreement reflects the parties' intentions with respect to the acquisition and operation of the hotel. The Agreement memorializes the sale to Petitioner of the Hotel Unit located at One U.N. Plaza and specifically incorporates, by reference, the terms and conditions of the Sublease of the Hotel Premises at Two U.N. Plaza.

26. The Closing Statement references a purchase price of $102,000,000, which includes the payments from Petitioner to UNDC for the "1 UN PLAZA CONDOMINIUM" and the "2 UN PLAZA SUBLEASE."

The Audit

27. On or about November 18, 1998, the City Department of Finance ("Department") commenced an audit of Petitioner for RPTT ("Audit"). The Audit was assigned the audit number "19347" ("Audit Number"). Baruch Beer, a Special Auditor in the Department's RPTT Group, conducted the Audit.

28. Mr. Beer maintained a written log for Audit #19347 ("Log"), with the first entry starting in November 1998. In the Log, Mr. Beer recorded the day-to-day contacts and details of the Audit, including telephone conversations with Petitioner's various representatives and discussions with Department personnel. Eleven pages of the Log were submitted into the record for the period beginning "11/8/98" and ending with the entry dated "7/12/01."

29. On November 18, 1998, Mr. Beer sent Petitioner a letter requesting information from Petitioner as grantee of a transfer with respect to "757/793 1st Avenue, Block:1337 Lot:1101, County: N.Y."

(One U.N. Plaza, the address of the Fee) which occurred on "07-23-1997" ("Information Letter").[13] The Information Letter bore the Audit Number "19347," specifically requested that Petitioner send the auditor a copy of the sales agreement and closing agreement with respect to the identified transfer and requested that Petitioner "[P]lease refer to the audit number above" in its reply.

30. On December 8, 1998, Petitioner's representative, Joseph D. Farrell, Esq., then of Coudert Brothers, LLP, responded in writing to the Information Letter, transmitting copies of the Purchase and Sale Agreement, the Closing Statement and the RPTT Return for the transfer of the Fee. The correspondence bore the reference "RHM-88, LLC/Block 1337, Lot 1101," but not the Audit Number.

31. Although the Information Letter referenced only the address of the Fee, during the Audit, Petitioner and Respondent, in correspondence and otherwise, addressed issues concerning the tax ramifications of both the Fee and the Sublease. Frequently, correspondence which pertained to issues concerning the Sublease, referenced "Audit Number 19347" and/or "RHM-88 LLC/Block 1337, Lot 1101".

32. In the December 29, 1998 Log entry, the auditor noted the terms of the purchase and recorded the consideration as $59,100,000 for the sale, and $36,500,000 for the Sublease as per Petitioner's schedules. The auditor also noted his intention to ask the attorney why no RPTT had been paid on the "sublease to purchaser."

33. In the September 9, 1999 Log entry, the auditor noted that Petitioner's representative explained that the payment for the Sublease was "all prepaid rent and is not taxable." Further, Mr.

[13] The Log indicates that the Information Letter was prepared on November 8, 1998.

Beer noted that he was discussing the case with other Department personnel with respect to possible CRT liability for the Sublease.

34. On September 9, 1999, Mr. Farrell sent Mr. Beer a copy of the Sublease. The reference line of that letter was encaptioned "RHM-88, LLC/Block 1337, Lot 1101" (the address of the Fee) and did not bear the audit number.

35. In the October 19, 1999 Log entry, the auditor noted that he and other Department audit personnel, including Eduardo Balthazar, were considering whether RPTT or CRT should be asserted with respect to the Sublease.

36. In the November 23, 1999 Log entry, the auditor indicated that he had been informed by Petitioner that a CRT return was being filed with respect to the Sublease and that it was Petitioner's position that for CRT purposes the amount of rent paid should be allocated over the term of the lease.

37. In the December 9, 1999 Log entry, where the auditor wrote that he prepared RPTT and CRT assessment worksheets for the case, he also commented that in the case of CRT, the tax amount is "offset [by] revenue received" (*i.e.* hotel room revenue).

38. In the February 2, 2000 Log entry, the auditor noted that the statute of limitations on assessment "expires in July for RPTT & poss. earlier for CRT."

39. On or about February 9, 2000, Mr. Farrell transmitted to the Department two City CRT returns for the 1997/1998 period and the 1998/99 period ("CRT Returns").[14] The accompanying correspondence bore the reference: Block 1337, Lot 1101 (the address of the Fee).

[14] The CRT Returns were sent to NYC Department of Finance, P.O. Box 3213, Church Street Station, New York New York 10242-0323, as per the instructions on the CRT forms.

The CRT Returns were signed by an officer of Petitioner's managing member, Regal Hotel Management, Inc., and were dated February 8, 2000. They were filed on behalf of RHM-88 LLC (the Petitioner), REGAL U.N. PLAZA HOTEL, at the address: One United Nations Plaza, New York, New York 10017-3515. Although the CRT Returns address only the CRT liability of the Sublease, the second page of each CRT return identifies the premises with respect to which each return was filed as "One United Nations Plaza, 10017-3515" (the address of the Fee). Each return reported gross annual rent paid of $439,759 with gross deductions of $7,791,682 for 1997-1998, and $8,488,707 for 1998-1999 (which were identified on appended schedules as "West Tower Revenue").[15] The gross rent amount reported represented Petitioner's position that the amount paid pursuant to the Sublease, $36,500,000, was rent which should be taken into account on an amortized annual basis for CRT purposes.

40. On the same date, February 9, 2000, Mr. Farrell sent Mr. Beer a letter which discussed the Sublease and submitted copies of the CRT Returns. The letter indicated the response was submitted "in connection with the above-referenced audit" which was recited in the reference line as Audit #19347. Further, the reference line referred to "RHM-88, LLC/Block 1337, Lot 1101" (the address of the Fee). The letter, however, solely addressed the tax treatment of the $36,500,000 payment under the Sublease.

41. On July 13, 2000, John Gallucio, Esq., of Coudert Brothers, LLP, sent a letter to the Department with a reference line "RHM-88, LLC/Block 1337, Lot 1101" (the address of the Fee). Although the letter indicated that it was transmitting certain material "[i]n connection with the above-referenced entity and property," it only addressed the issue of when and where the CRT

[15] The schedules indicate that the revenue reported represented income from 152 rooms or 36% of the total rooms.

Returns were filed. The letter does not bear the audit number, but Mr. Beer is copied on the correspondence.

42. On October 5, 2000, another of Petitioner's representatives, Charles E. Aster, Esq. of Coudert Brothers, sent a letter to the Audit Department [sic] of the Department. While the letter was addressed to Eduardo Baltazar, the salutation was to Mr. Beer. Although the letter indicated it was being submitted with respect to "this audit," it only presented Petitioner's position with respect to the CRT consequences of the prepayment of rent under the Sublease. The reference line of this correspondence is "RHM-88, LLC/Block 1337, Lot 1101/Audit #19347" (the address of the Fee). Petitioner's representative noted in that letter that its position with respect to the CRT (*i.e.*, that amortization of the $36,500,000 Sublease payment over the term of the lease was permissible) had been confirmed by a Department employee, "Tony Deluca," in an April 24, 1997 telephone conversation.

43. On October 13, 2000, Mr. Farrell transmitted to the Department copies of the Bishop Lease, the Condominium Declaration for One United Nations Plaza and the Mortgage. The reference line of the correspondence was "RHM-88,LLC/Block 1337, Lot 1101/Audit #19347."

44. On May 17, 2001, Mr. Aster wrote Michael Newmark, Esq. of the Department. The letter discussed Petitioner's position with respect to any tax liability for the Sublease. The letter referred to the UN Plaza Hotel as the "Property" and the Sublease as pertaining to a "portion of the Property." The correspondence bears a reference line "RHM-88 LLC/Block 1337, Lot 1101/Audit #19347."

45. Mr. Beer testified that during the period in issue, in the normal course of business, the Department did not index RPTT returns. Rather these returns were physically maintained in the

order in which they were received. At that time, the information contained in RPTT returns was not accessible through the Department's FAIRTAX computerized tracking program.

46. Mr. Beer testified that he understood during the course of the Audit that City tax parcel Manhattan Block:1331 Lot:1101 (the address of the Fee) encompassed both the Fee and the Sublease.

47. Mr. Beer further affirmed that during the course of the Audit it was his impression that no RPTT return had been filed with respect to the Sublease and that the RPTT return filed for the transfer encompassed both the Fee and Sublease transactions.[16]

48. During the course of the Audit, Petitioner twice agreed, in writing, to extend the period of limitation on RPTT assessment by executing Consents Extending Period of Limitation for Assessment of Real Property Transfer Tax ("Consents"). Individuals in the Department prepared the Consents and the auditor transmitted them to Petitioner's representative.

49. The first consent covered the period from July 23, 2000 to January 31, 2001 ("First Consent") and the second consent covered the period from January 31, 2001 to July 31, 2001 ("Second Consent"). Although the First Consent was not available for submission into the record, the representatives of the parties agreed to its existence and terms (*i.e.*, that it was identical in format to the Second Consent). The Second Consent, a copy of which was admitted into evidence, referred to Audit Number 19347, with a listed Property Address of 787/793 1st Avenue A/K/A One U.N. Plaza,

[16] Mr. Beer reviewed Exhibit 21 (the Department's copy of the RPTT return for the Sublease) and testified that he only had received a copy of that RPTT on December 10, 2001, which was after the Notices were issued. T. 354.

New York, 10017 (the address of the Fee).[17] The Second Consent was signed on behalf of the Petitioner by Lyle L. Boll, Senior Vice President and General Counsel of Regal Hotel Management, Inc., Petitioner's managing member, and was dated "21 Nov 00." Petitioner's representative transmitted the Second Consent to Mr. Beer by facsimile on November 22, 2000. The transmittal document referenced an extension of the statute of limitations to July 31, 2001 "with respect to audit #19347."

50. Mr. Beer noted in his Log entry for July 12, 2001 that "[N]o RPTT return [was] filed" for the Sublease transaction.

51. On July 13, 2001, the Department issued a Notice of Determination of RPTT due with respect to the Fee in the total amount due of $8,635.07 ("Fee Notice"). The Fee Notice referenced Audit Number 19347 and the address 757/793 1st AVENUE [sic] Block:1337 Lot:1101 County: NY (the address of the Fee). This notice represents the assessment of additional RPTT computed against the increase to the purchase price for a gross-up attributable to taxes paid. (*See,* Finding of Fact 18, *infra*.) Petitioner paid this deficiency on August 28, 2001.

52. On July 13, 2001, the Department also issued to Petitioner a Notice of Determination asserting RPTT due in the amount of $1,373,586.16, with respect to the Sublease ("Sublease Notice"). The Sublease Notice referenced Audit Number 24439 and the address TWO U.N. PLAZA Block:1337 Lot:14 County: NY (the address of the Sublease). This notice represents the assessment of RPTT computed against the $36,500,000 paid with respect to the Sublease.

[17] The Consent in the record was a copy of the Consent signed by Petitioner's representative and did not bear the signature of a Department representative. However, Code §11-2116(c) only requires that the taxpayer "consent in writing" to the extension of the statute of limitations. Further, the auditor's log indicates that the consents were subsequently signed by Department personnel.

53. Petitioner filed a Petition on October 9, 2001, and an Amended Petition dated October 11, 2001, requesting redetermination of the RPTT deficiency asserted with respect to the Sublease transaction.

STATEMENT OF POSITIONS

Petitioner asserts that it is not liable for RPTT on the Sublease transaction as the consideration for the Sublease was rent subject to the CRT. Alternatively, Petitioner argues that if it is liable for additional RPTT, the assessment on July 13, 2001 was barred as the statute of limitations on assessment ran on July 23, 2000.

Respondent argues that the Sublease transaction was the transfer of a Sublease interest, the consideration for which is subject to RPTT. Respondent asserts that the statute of limitations on assessment of additional RPTT had not run on July 13, 2001, as the First Consent, executed prior to July 23, 2000, and the Second Consent, executed on November 21, 2000, extended the statute of limitations on assessment of RPTT until July 31, 2001 for both the Fee and the Sublease. Respondent asserts that Petitioner and Respondent intended the Consent to apply to both the Fee and the Sublease and therefore there was mutual mistake in the preparation of the Consent which only referenced the address of the Fee.

CONCLUSIONS OF LAW

Prior to 1997, the City operated the U.N. Plaza Hotel through a local development corporation, UNDC, pursuant to a management agreement with the Hyatt Corporation. The Hotel was located on contiguous floors of two adjacent buildings situated on separate parcels of land at 45th Street and First Avenue in Manhattan and was operated as a single business from these sites.

In 1997, the City decided to sell its interests in the Hotel and put it out for bid to major hotel corporations. The general terms of the bid were for the sale of the relevant portions of the land to which the City had title and of the building located at One U.N. Plaza (which the City leased to UNDC), and the sublease of the land (title to which was held by the Bishop Trading Company) and the building located at Two U.N. Plaza (which the City also leased to UNDC). Petitioner was the successful bidder, agreeing to a purchase price of $102,000,000, approximately $60,000,000 of which was attributed to the sale of the hotel properties at One U.N. Plaza and $36,500,000 of which was attributed to the Sublease of the hotel properties at Two U.N. Plaza.

The City, UNDC and Petitioner clearly intended to enter into one overall agreement which encompassed the sale and transfer of the relevant properties located at One and Two U.N. Plaza comprising the Hotel. The parties did not contemplate two independent transactions. However, in order to convey the Hotel it was necessary to structure the offering as two transactions: (1) the sale of the City's fee interest in the Hotel Unit located at One U.N. Plaza; and (2) the sublease of UNDC's lease interest in the Hotel Premises located at Two U.N. Plaza. Each of the two agreements, the Purchase and Sale Agreement and the Sublease, materially references the other and contemplates that Petitioners will ultimately own condominium units in each tower.[18]

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[18] *See, e.g.,* Purchase and Sale Agreement, the 5th, 7th and 12th "whereas" clauses, which specifically reference the Hotel Premises lease; §2.1 which lists as a term of the Agreement the lease of the Sublease estate at Two U.N.Plaza; §8.2 which requires the delivery of the executed Sublease and memorandum in "statutory and recordable form executed and acknowledged by Seller" as a condition of the Agreement; and §18.14 which states: "[T]his Agreement and the Sublease constitute the entire agreement and understandings among the parties hereto concerning the subject matter hereof . . .." *See, also*, the 5th "whereas" clause of the Sublease, which speaks of the "conveyance" of the Hotel Unit and the lease of the Hotel Premises; §16.01(b) of the Sublease, with respect to assignment, ". . . it being the intention of the parties that this Sublease and the [Hotel Unit] remain in common ownership;" and §19.03 of the Sublease: "It is a condition of this Sublease that Tenant own this hotel unit in the One United Nations Plaza Condominium . . . and operate the Hotel Premises [Two UN Plaza] and One United Nations Plaza Hotel as a single full service first-class hotel."

For One U.N. Plaza, pursuant to the Condominium Declaration, the City created two condominium units - one unit comprised of the Hotel property (Hotel Unit) and one unit comprised of the remaining office facilities - and transferred the Hotel Unit to Petitioner. Pursuant to Sublease §29.14(d) (addressing the exercise of the Bishop Option) a condominium "regime" for Two U.N. Plaza is to be established which would be similar to the One U.N. Plaza Condominium Declaration, *i.e.*, one unit for the Hotel Premises and one for the rest of the property. Lyle Boll, Senior Vice President and General Counsel of Petitioner's managing member, Regal Hotel Management, described the transactions as follows: "[The property] was sold as a hotel, but the City simply was not able to sell the hotel in the ordinary sense . . . It had half of a hotel to sell, and then it had half of a hotel to lease." T. 438.

The initial issue is whether the consideration paid for the Sublease is rent paid by a tenant to a landlord which is exempt from the RPTT as it is subject to the CRT. The RPTT is imposed when real property and/or interests therein are transferred. *595 Investors Limited Partnership v. Biderman*, 140 Misc. 2d 441 (N.Y. Sup. Ct., 1988). Code §11-2102 imposes a tax "on each deed at the time of delivery by a grantor to a grantee when the consideration for the real property and any improvements thereon . . . exceed twenty-five thousand dollars." The Code defines a "deed" to be "any document or writing . . . whereby any real property or interest therein is . . . sold, transferred, assigned or otherwise conveyed." Code §11-2101.2. For RPTT purposes, a "deed" includes "any . . . document or writing whereby any Sublease interest in real property is granted, assigned or surrendered." Code §11-2101.2. *See, Matter of Kaufman v. Shorris*, 162 A.D.2d 399 (1st Dept. 1990), motion for leave to appeal denied 76 N.Y.2d 710 (1990) (transfer of Sublease interest as tenant in common to partnership); *Matter of Levinsky v. Kraut*, 121 A.D.2d 723 (2nd Dept. 1986). *See, also*, FHD(228)-RP-4/89-(0-0-0) (the transfer of a Sublease interest to a newly formed

partnership is subject to RPTT).[19] Therefore, the Sublease is a deed pursuant to the RPTT.

RPTT is computed against the consideration for the taxable transaction,[20] which is defined to include the "price actually paid or required to be paid for the real property or economic interest therein." Code §11-2101.9. In the case of a transfer of a Sublease interest in real property, the Code provides that taxable consideration is 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); a landlord is "[a] person who grants the right to use or occupy premises to any lessee, sublessee, or concessionaire" (Code §11-701.2); and a "tenant" is defined as "[A] person paying or required to pay rent for premises as a lessee" (Code §11-701.3). The determinative issue, therefore, is whether the $36,500,000 lump-sum payment which Petitioner made in exchange for the Sublease was rent paid to UNDC as a landlord or whether it was consideration for UNDC's transfer to Petitioner of its entire interest in the Hotel Premises at Two U.N. Plaza.

The Sublease specifically defines the $36,500,000 payment as "rent . . for the entire term" and provides that "no additional rent or other amounts shall be payable by Tenant during the Term [excepting certain tenant's charges]". Sublease §2.04.

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[19] The written memorialization of a transaction which effects a transfer of a Sublease interest is considered a deed for RPTT purposes. *See*, Finance Letter Ruling 31 (April 10, 1989), where the Department noted that the tax "applies to every surrender of a Sublease interest to a lessor made pursuant to or evidenced by a document or writing in which such interest is surrendered." *See, also*, Finance Letter Ruling 15 (February 23, 1983), regarding an assignment of a lease in bankruptcy.

[20] The threshold amount of consideration that will subject a transfer to RPTT is an amount which exceeds $25,000. *See*, Code §11-2102 which establishes RPTT rates according to the amount of taxable consideration. For the period in issue, 1997, the RPTT was imposed at a rate of 1.425% on consideration of $500,000 or less and 2.625% where the consideration is more than $500,000.

Notwithstanding that this agreement identifies the parties as landlord (UNDC) and tenant (Petitioner), it is the substance of a transaction which controls for tax purposes. *See*, *Frank Lyon Co. v. United States*, 435 U.S. 561, 573 (1978); *Commissioner v. Tower*, 327 U.S. 280, 291 (1946). *See, also*, *Matter of Plaza 43 Associates*, TAT(E) 99-16 (CR) (City Tax Appeals Tribunal, 2004), where the Appeals Division of this Tribunal, citing *Feder v. Caliguira*, 8 N.Y.2d 400, 404 (1960), held:

> . . . the terminology used by the parties is not controlling . . . [Instead, the Court] must look to the rights the agreement confers and the obligations it imposes in order to determine the true nature of the transaction and the relationship of the parties.

Although the Sublease defines the $36,500,000 payment as rent, other provisions of that agreement must be considered in order to determine whether the parties intended that it be a lease agreement or a transfer of UNDC's entire interest in the Hotel Premises. *Tillman v. Commissioner*, T.C. Memo 1996-8 (1996). Where a lessee "parts with his entire interest he has made a complete assignment." *Bostonian Shoe Co. v. Wulwick Assoc.,* 119 A.D.2d 717, 719 (2d Dept. 1986)) citing *Woodhull v. Rosenthal,* 61 N.Y. 382, 391 (1875. A transaction is an assignment if the benefits and burdens of ownership have passed. *Frank Lyon, supra at* 585. Here, the rights and obligations of the parties, as expressed in the Sublease and the relevant portions of the Purchase and Sale Agreement, evidence as complete a transfer of UNDC's interest in the Subleased portion of Tower Two as was possible, and thus the agreement is more in the nature of an assignment rather than a lease.

The transfer of the Sublease interest to Petitioner is a means to the desired end of the acquisition and operation of a single hotel at U.N. Plaza. The documents memorializing the transaction establish the intent of the parties to transfer from UNDC to Petitioner all of the interest it had in the hotel property. Thus,

UNDC sold all that it had to sell for a single lump sum payment: the Fee and the interest of UNDC in the Bishop lease, including its interest in the Bishop Option.

In its totality, the Sublease lacks the traditional characteristics of a lease. *See*, *International Trade Administration v. Rensselaer Polytechnic Institute*, 936 F.2d 744, 751 (2d Cir. 1991), where the Court of Appeals for the Second Circuit noted that where there is a pre-payment of rent, an unusually long term and allocation of responsibilities between landlord and tenant, the economic substance of the transaction is more closely a sale than a "true" lease. Here, Petitioner and UNDC have entered into an eighty-two year agreement where a lump sum payment was due initially, there are no future continuing payment obligations (other than payment of the proportionate share of expenses) and, most significantly, the agreement can be terminated after half the term by the exercise of an option to purchase the underlying parcel without a refund to Petitioner of the proportionate amount of pre-paid rent or a payment to UNDC (the purported landlord) for the acquisition of twelve floors of the Second Tower.

Petitioner's rights with respect to the Bishop Option provide the strongest support for the conclusion that Petitioner and UNDC did not intend a landlord-tenant relationship. Both Agreements provide that the Bishop Option may be exercised at any point during a five-year period occurring in the middle of the Sublease. If the Bishop Option is exercised by UNDC, Petitioner is only required to pay its proportionate share of the extant fair market value of the underlying land of the Two U.N. Plaza parcel to be paid to an unrelated third-party. In return, Petitioner receives the Second Tower condominium hotel unit (which includes both the value of the underlying land and the Hotel Premises). UNDC retains no interest in the Hotel Premises, including relinquishing any reversionary interest under the Sublease. Moreover, should UNDC refuse to

exercise the Bishop Option, Petitioner can force the exercise of that option. The agreements establish that the parties intended that the Sublease would be extinguished once the Bishop Option was exercised. Petitioner is not required to compensate UNDC for early termination of the Sublease and UNDC is not required to return any portion of the "advance rent" initially paid. Finally, upon the exercise of the Bishop Option, the benefits and burdens of ownership of the Hotel Premises unit will pass to Petitioner.

For a sublease to exist, the leased premises must revert to the sublandlord sometime before the end of the lease period. A retention of even a small reversionary interest has been held sufficient to characterize and agreement as a sublease. *See, for example, Bostonian Shoe Co., supra,* where a 12-hour reversionary interest was adequate to substantiate a sublease. However, UNDC's *de minimis* one-day reversionary interest in the Hotel Premises is highly contingent as the exercise of the Bishop Option would terminate any interest UNDC has in the Hotel Premises at a point substantially before that potential *de minimis* reversion could occur.

The record establishes that the parties envisioned a transaction which would resemble, as closely as possible, a sale. Joseph Gunn, Senior Counsel for the City Economic Development Division and a participant in the U.N. Plaza Hotel negotiations, testified that the $36,500,000 payment was "for the transfer of the entire sublease interest of the hotel within Two U.N. Plaza" (T. 424)[21] and that this part of the transaction was "like a sale." (T. 424). He further testified: ". . . if you are going to ask someone to . . . pay a lump sum like they were buying the property you need to make the product or the interest that they are buying resemble an out and out fee purchase." (T. at 433). The Sublease which

[21] However, on cross-examination, Mr. Gunn also characterized the transaction as a granting, not a transfer, of a sublease. (T.427.)

executed that intent, was therefore a transfer of UNDC's interest in real property subject to the RPTT and no part of the consideration was paid as rent from a tenant to a landlord.

As Petitioner transferred an interest in real property subject to the RPTT when it entered into the Sublease, the next inquiry is whether Respondent timely assessed RPTT on that transaction. The issue is whether the consents to extend the limitation on assessment to July 31, 2001 apply to both the Sublease transaction as well as the Fee.

The Code provides that an assessment of additional RPTT may not be made "after the expiration of more than three years from the date of the filing of a return; provided however, that where no return has been filed as provided by law the tax may be assessed at any time." Code §11-2116(b). The RPTT return reporting the Sublease transaction was filed on July 23, 1997. Therefore, a *prima facie* case was made that the unextended statute of limitations on assessment would have run on July 23, 2000.

Where a statute of limitations has otherwise run, the burden of going forward to establish an exception to the time limitation is on the agency. *Adler v. Commissioner*, 85 T.C. 535, 540 (1985). Therefore, Respondent must establish that the statute of limitations is not a bar. *Adler, supra.*

The statute of limitations on assessment may be extended where the taxpayer consents to the extension in writing. Code §11-2116 (c). Petitioner twice consented in writing to extend the statute of limitations on assessment of additional RPTT. While the First Consent is not in the record, the Second Consent indicates an agreement to extend the limitation for assessment to July 31, 2001. The Second Consent was signed by Lyle Boll as Senior Vice President of Regal UN Plaza LLC, the managing member of Petitioner, on

November 21, 2000, and was signed by a representative of the Department on December 6, 2000. As the parties agree that the Second Consent follows the First Consent in form and substance, if the Second Consent applies to the Sublease transaction, the assessment at issue was timely made.

A consent to extend the limitation on assessment is not strictly a contract (*Piarulle v. Commissioner*, 80 T.C. 1035 (1983)), but is a unilateral waiver of a defense (*Stange v. U.S.*, 282 U.S. 270, 276 (1931)). However, since the Consent is a written document, contract principles may be applied to interpret the agreement. *Schulman v. Commissioner*, 93 T.C. 623 (1989). The objective manifestation of mutual assent as evidenced by the parties' overt acts determines whether the parties have made an agreement. *See, generally*, Restatement (Second)of Contracts §19 (1981).

The Second Consent which extended the limitation on assessment of additional RPTT extended the statute with respect to transfers of a property with the address of 787/793 1st Ave A/K/A One UN Plaza, New York NY 10017 (the address of the Fee) and an audit number "19347". Under general principles of construction, where the agreed upon language is clear and unambiguous, the language of the consent controls. *See,* by illustration, *Matter of Control Data,* TAT(H)93-114(CR), TAT(H)93-115(CR) (City Tax Tribunal, Administrative Law Division, March 5, 1996). However, it is Respondent's position that the Second Consent (and thus both Consents) also apply to the Sublease transaction even though the address of the subleased property, 332/334 East 45th Street, Two U.N. Plaza, is different than the address on the Second Consent, 757/793 1st Ave. (the address of the Fee). Therefore, Respondent argues, the Second Consent (and thus both Consents) should be reformed to correct the parties' mutual mistake in drafting the document.

A mutual mistake is found where the "agreement in written form does not match what was really intended by the parties." *Woods v. Commissioner*, 92 T.C. 776, 782-6 (April 11, 1989). *See, also, Bower v. Commissioner*, T.C. Memo 1992-446 (August 10, 1992). Under contract principles, a mutual mistake in drafting may be reformed based on extrinsic evidence. *See, generally*, Restatement 2d, Contracts §152, 155. Where there is a mistake in drafting, and there is clear and convincing evidence that the parties intended to extend the limitation on assessment, the consent will be reformed. *Woods, supra at 782.* Since only the writing may be reformed, mutual mistake is often referred to as "scrivener's error." *Buchine v. Commissioner,* 20 F.3d 179 (5th Cir. 1994), *rehear. denied*, 26 F.3d 173 (1994).

In order to determine whether there was a mutual mistake in executing the Consents, objective manifestation of the intent of the parties is examined. *Kelly v. Commissioner*, T.C. Memo 1990-202 (April 19, 1990). Such manifestation is established by reference to the parties' "overt acts, not the parties' secret intentions." *Kronish v. Commissioner*, 90 T.C. 684, 693 (1988). The overt acts must support a finding that the Consents applied to extend the statute of limitation for all aspects of the Hotel transaction, both the Fee and the Sublease. It is noted that the only events which are relevant are those which establish what Petitioner and Respondent believed at the time they signed the consent, *Sager v. Commissioner*, T.C. Memo 1988-193 (May 3, 1988). Therefore events which occurred after December 6, 2000, are not considered.[22]

[22] Although the Second Consent bears only the signature of Lyle Boll, this is not a significant defect. The statute only requires the consent of the taxpayer in writing to extend (Code §11-2116(c)) and further the auditor's log identifies the individuals who signed the two consents on behalf of the department at log entries dated May 30, 2000 and December 6, 2000.

During the course of his audit, Mr. Beer was not aware that an RPTT return had been filed with respect to the Sublease and was operating under an impression that the RPTT return which was filed under the address of the Fee encompassed the Sublease transaction as well. He therefore believed that the Consents applied to both. Mr. Beer did not have actual knowledge of the filing of an RPTT return for the Sublease until the audit was closed, and given the uncontroverted testimony to the Department's return retention procedures at the time of audit (T. 267-70), he cannot be held to have had constructive knowledge of that return.[23]

Petitioner argues that at all times it treated the Sublease as a separate and discrete transaction with an address separate from the Fee. However, on February 9, 2000, nine months before the second Consent was signed, Petitioner submitted the CRT Returns to the Department, and copies to the auditor, to establish its position with respect to the CRT taxability of the Sublease transaction. These returns described the Sublease premises by the address and property designation of the Fee, Block 1337, Lot 1101, One U.N. Plaza, which would indicate that Petitioner also believed that the address of the Fee included the Sublease. Moreover, it is axiomatic that the Department is entitled to rely on the information contained in the most recent returns filed by a taxpayer; *i.e.* based on the filed February 2000 CRT returns, for purposes of determining City taxation of the Sublease, the address of the Fee includes the Sublease.

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[23] Petitioner argues that the auditor never requested an extension for the Sublease. Testimony and documentary evidence establish that, at the time the Consents were executed, Mr. Beer believed that no RPTT return for the Sublease had been filed by Petitioner. See, *e.g.*, T.271, 281, 288-90; Motion Ex.9 to Affirmation in Opposition, Auditor's Log, entries for December 29, 1998, and September 9, 1999. The only information which Petitioner communicated to Mr. Beer during audit was its belief that if any tax was due, CRT was due, and that CRT returns would be filed. Further, Petitioner does not appear on this record to have ever advised Mr. Beer that an RPTT return had been filed with respect to the Sublease.

The extrinsic evidence presented establishes that both parties believed that the transactions were separate parts of a single event: the sale/transfer to Petitioner of the hotel property. Both parties also believed that the address of the Fee encompassed both the Fee and Sublease properties.

Petitioner offered the testimony of Mr. Farrell to support its assertions concerning the scope of the Consent. Mr. Farrell, who was identified by Petitioner's present representative as simply "a person with power of attorney for Petitioner," did not prepare the Consent form, nor was he a signatory. Moreover, Mr. Farrell did not testify that he advised the signatory, Mr. Boll, regarding the scope of the Consent. Therefore Mr. Farrell's testimony as to his intentions is irrelevant.[24] The testimony of Mr. Farrell's colleague, Mr. Aster, is even less compelling. Mr. Aster simply testified that he was never asked to extend the statute of limitations and that he never intended to do so. (T. 61.) Notably, Petitioner did not present any direct testimony concerning the Consent by the person who actually signed the extension, Lyle Boll, although Mr. Boll testified about other aspects of the transaction.

Finally, it is apparent that Petitioner considered itself liable for the additional RPTT asserted on the Fee, which represented tax on the gross-up of the purchase price to include transfer taxes paid pursuant to the Purchase and Sale Agreement with

[24] Mr. Farrell testified that the extension covered only the "fee side" (T. 181) and that Petitioner "agreed to a six-month extension." (T. 182.) But even if Mr. Farrell had testified that he had so advised Mr. Boll as to the alleged limited scope of the Consents, his testimony concerning the Consents does not meet the *Kronish* requirements for the best evidence of Petitioner's intention at the time of entering into the agreement. As the Court noted in *Kronish*, "[T]he taxpayer's private intentions are not determinative of whether the parties entered into an agreement .. ." *See, also, U.S. v. Burlington Resources Oil*, 2000 U.S.Dist C. Lexis 22001, 86 A.F.T.R.2d (RIA) 5282 (May 18, 2000).

respect to the Fee.[25] If the Consents were meant only to apply to the Fee, they would not have been necessary since the $6,205.50 "open" issue could have been resolved before the July 23, 2000 unextended expiration of the statute. The record indicates that only the potential $1,373,586.16 tax liability for the Sublease was discussed after the first Consent was executed and, therefore, the only conceivable purpose for twice extending the statute of limitations was to allow an additional period of time to resolve the issue of RPTT liability for the Sublease.

It is clear that by Consents, the parties intended to extend the statute of limitations on the assessment of RPTT with respect to the Sublease to July 31, 2001. Thus, the objective evidence presented establishes that there was mutual mistake in the wording of the Consent which must be reformed to prevent an unintended and unexpected windfall. *Woods, supra.*[26]

ACCORDINGLY, IT IS CONCLUDED THAT the transfer to Petitioner of the Sublease was a grant of a Sublease interest in Two U.N. Plaza the consideration for which, $36,500,000 was subject to the RPTT. The Consent to extend the limitation on assessment of RPTT, signed by Lyle Boll on November 21, 2000, should be reformed to reflect the parties' agreement that it applied to the transfer of both the Fee and the Sublease. Therefore, the limitation on assessment of

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[25] See, *e.g.*, T. 186, where Mr. Farrell testified that there was a "slight miscalculation" with respect to the "correct amount" of RPTT due on the fee, and T. 187 where he testified that the Fee Notice was "essentially an adjustment because of the failure to include in the consideration for calculation purposes the State transfer tax that had been paid."

[26] It also might be concluded that since Petitioner used the address of the First Tower as the address of the Second Tower in the filed CRT Returns there was a latent ambiguity in the Consents such that the parties reasonably believed that the address of the Fee also was the address of the Sublease. *See, Woods v. Commissioner, supra,* where the Tax Court noted that there is latent ambiguity in an instrument where "the language . . . is clear and suggests a single meaning, but some collateral matter makes the *meaning* of the instrument uncertain." *Woods at 781.*

additional RPTT on the Sublease was extended to July 31, 2001 and the Notice dated July 13, 2001, was timely issued. As Petitioner is liable for RPTT on the Sublease transaction, the July 13, 2001 Notice of Determination asserting RPTT in the amount of $1,373,586.16 plus interest thereon is sustained in full.

DATED: January 11, 2006
New York, New York

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ANNE W. MURPHY
Administrative Law Judge