

New York State Department of Taxation and Finance
Office of Counsel
Advisory Opinion Unit

TSB-A-10(2)R
Real Estate Transfer Tax
April 29, 2010

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. M090714A

The petition was filed by name [REDACTED] (“Petitioner”), a shareholder in a corporation that operates a New York City residential cooperative apartment building under the supervision of the New York State Division of Housing and Community Renewal (“DHCR”) on a not-for-profit basis for persons who meet certain income eligibility requirements. She asks whether the New York State real estate transfer tax (RETT) will be applicable if a Voluntary Reconstitution Plan to convert the building into a private cooperative is executed.

We conclude that the conversion of the not-for-profit housing company (PHFL company) to a private cooperative housing corporation (BCL corporation) constitutes a conveyance by the plan sponsor of the real property comprising the cooperative dwelling, subject to the RETT. In addition, upon conversion, the shares in the BCL corporation will be deemed to have been conveyed to the shareholders of the PHFL company who have not opted out, as an original conveyance of shares in the BCL corporation, and thus subject to the RETT. This conveyance may be exempt to the extent that there is no change in beneficial ownership. To the extent that the conveyance does not qualify for the exemption, it may qualify for a credit. The conveyance of stock to the PHFL company by shareholders who elect not to participate in the BCL corporation will also be subject to the RETT.

Petitioner also asks how to calculate the RETT if liability for the tax is found, and that will be discussed below.

Facts

[REDACTED] (“the Sponsor”), organized under Article II of the Private Housing Finance Law (“PHFL”), owns real property in New York City and operates the property under supervision of the DHCR. As such, the property is subject to the rules and regulations of the Mitchell-Lama program, which prevent shareholders of the Sponsor from realizing the market value of their interest in the property upon its sale.

A Voluntary Reconstitution Plan (“the Plan”) to convert the Sponsor to private cooperative ownership has been drafted. Under the Plan, the Sponsor would amend its existing Certificate of Incorporation filed pursuant to the requirements of the PHFL, so that the resulting certificate of incorporation complies with provisions of the Business Corporation Law (BCL). Upon withdrawal from the Mitchell-Lama Program, the Sponsor would cease to be subject to the restrictions under the PHFL. After the dissolution and reconstitution of the Sponsor, the cooperative housing corporation would operate on a for-profit basis and have all the power and authority of a corporation formed under the BCL. The waiting lists of income-eligible applicants would be eliminated, control over maintenance and assessments would be transferred to the reconstituted corporation, and shareholders would be free to sell their interests in the real property for market value, subject to certain conditions commonly applied to co-operative housing sales. After the dissolution and reconstitution of the

Sponsor, the Sponsor would operate on a for-profit basis and have all the power and authority of a corporation formed under the BCL.

After privatization, the share allocations of the Sponsor would be adjusted to reflect the value of the apartments as determined by new criteria in the Plan. All shareholders of the Sponsor immediately prior to privatization would have the right to exchange their existing shares for shares in the reconstituted corporation allocated to their present apartment or, in the alternative, to surrender their shares of the Sponsor and (i) remain as tenants under annual leases or (ii) vacate their apartment. Those electing to rent or vacate (“non-participants”) will not receive the fair market value of shares in the BCL corporation, but rather will receive a return of their equity as valued for purposes of the PHFL company.¹ All shares allocated to apartments occupied by non-participants will initially be owned by the BCL corporation and may thereafter be sold to investors, subject to the non-participants’ leases.

Analysis

New York State imposes a tax (known as the real estate transfer tax or RETT) on each conveyance of real property or interest therein when the consideration exceeds five hundred dollars or a fractional part thereof.² An additional tax is imposed on each conveyance of residential real property or interest therein when the consideration for the entire conveyance is one million dollars or more.³ A conveyance of real property or interest therein is not limited to a deed transfer, but includes the transfer or transfers of any interest in real property by any method, including but not limited to sale, exchange, assignment, surrender, mortgage foreclosure, transfer in lieu of foreclosure, option, trust indenture, taking by eminent domain, conveyance upon liquidation or by receiver, or transfer or acquisition of a controlling interest in any entity with an interest in real property.⁴

While the ownership of the real property would not be conveyed in the conventional sense to a newly formed corporation, there must be dissolution of the Sponsor in order to remove the restrictions of the Mitchell-Lama Program.⁵ The dissolution and reconstitution will result in significant changes in the financial benefits and restrictions appurtenant to the shares in the Sponsor prior to the conversion and after the conversion. As a result, there is a substantive change in the nature of the ownership of the entity that owns the property. Accordingly, the conversion from a PHFL company to a BCL corporation constitutes a conveyance by the Sponsor to a cooperative housing corporation of the real property comprising the cooperative dwelling, a transaction that is subject to the RETT under §1402(a) of the Tax Law. The consideration for the conveyance is the amount of cash received by the Sponsor; the amount of any mortgages, liens, or encumbrances on the real property; and the fair market value of the shares in the cooperative housing corporation after reconstitution.⁶ In general, the transaction described above would be deemed to constitute a mere change of identity or form of ownership or organization to the extent that the ownership percentages of shares in the BCL corporation for each apartment remained the same as the percentages in the PHFL company. However, the exemption provided under §1405(b)(6) of the Tax Law for conveyances that effectuate a

¹ See Rights of Existing Shareholders, p. 122 of The Plan.

² §1402(a) of the Tax Law.

³ §1402-(a)(a) of the Tax Law.

⁴ §1401(e) of the Tax Law.

⁵ §35(3) of the PHFL.

⁶ 20 NYCRR §575.11(a)(12).

mere change of identity or form of ownership or organization does not apply to conveyances to a cooperative housing corporation of real property comprising the cooperative dwellings

In addition to the conveyance of the real property to the BCL corporation upon conversion from a PHFL company to the BCL corporation, the shares in the BCL corporation will be deemed to have been conveyed by the Sponsor to the shareholders of the PHFL company (those who have opted to become shareholders in the reconstituted cooperative – “participants”) as an original conveyance of shares representing each shareholder’s ownership interest in the BCL corporation, with an appurtenant proprietary lease for each shareholder’s respective unit. This conveyance is also subject to the RETT.⁷ Consideration for each original conveyance of shares of stock in the BCL corporation means the price actually paid or required to be paid for the real property, including payment for an option or contract to purchase real property, the cancellation of debt or obligation, and the amount of any lien.⁸ However, to the extent that the conveyance of the shares in the BCL corporation to the participating shareholders of the PHFL company effects a mere change in the identity or form of ownership or organization where there is no change in beneficial ownership, the mere change exemption under §1405(b)(6) of the Tax Law may apply.

As previously noted the RETT applies to transfers by a sponsor to a cooperative housing corporation of the real property comprising the cooperative dwellings, notwithstanding that there may have been no change in beneficial ownership. In the case of the original conveyance of shares of stock in a cooperative housing corporation in connection with the grant of a proprietary leasehold, however, a credit is allowed. The credit is a proportionate part of the tax paid upon the conveyance of the real property by the sponsor to the cooperative housing corporation against the tax imposed on the original conveyance of shares of stock in the cooperative housing corporation in connection with the grant of a proprietary lease.⁹ Thus, to the extent that the mere change rule is not otherwise applicable, any RETT due on the original conveyance of shares in the BCL corporation to the Participants, in conjunction with a proprietary lease, may be offset by a credit. The amount of the credit is determined by multiplying the amount of tax paid upon the conveyance to the cooperative housing corporation by a percentage representing the extent to which such conveyance effectuated a mere change of identity or form of ownership, and then multiplying the resulting product by a fraction, the numerator of which shall be the number of shares of stock conveyed by the BCL corporation with a proprietary lease for the units, and the denominator of which shall be the total number of shares of stock of the cooperative housing corporation, including any stock held by the corporation.

The conveyance to the PHFL company by non-participants of their shares in the company prior to its conversion, along with their occupancy agreements that they agree to terminate, is considered a subsequent conveyance of stock in a cooperative housing corporation, which is subject to the RETT.¹⁰ The consideration for such subsequent transfers will be the equity payment received by the non-participants.

The sale by the Sponsor of BCL shares allocated to the apartments of the non-participants is also subject to the RETT.

⁷ 20 NYCRR §575.8(a)(1).

⁸ §1401(d) of the Tax Law.

⁹ §1405-B(a) of the Tax Law and 20 NYCRR §575.8(c).

¹⁰ 20 NYCRR §575.8(a)(2).

It should be noted that, pursuant to §1402-a(a) of the Tax Law, if the consideration for the conveyance of shares related to an individual cooperative apartment unit is \$1 million or more, the conveyance will be subject to an additional 1% tax at the time of conveyance. However, as stated above, the mere change exemption may apply if the conveyance effectuates a mere change of identity or form of ownership or organization.

DATED: April 29, 2010

/S/
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