

# Proposed Expansion of New York State Real Estate Transfer Tax

March 27, 2017

On January 23, Governor Cuomo introduced proposed legislation to the New York State Legislature implementing his 2017-2018 budget proposal. One proposal (contained in the Revenue Article VII Bill) would expand the New York State Real Estate Transfer Tax (“NY State RETT”) to apply to transfers of minority interests in certain entities holding New York State real property if the value of the real property is at least 50% of the value of all of the entity’s assets. If enacted, this would amount to a significant expansion of the tax. There is a separate New York City real estate transfer tax which is not implicated by the Governor’s proposal. See Part JJ (p. 206) of the [proposed legislation](#) and Part JJ (p. 39) of the official [Memorandum of Support](#).

On March 15, the New York State Assembly and New York State Senate each passed one-house budget resolutions and corresponding legislation. The Assembly’s [version](#) of the budget adopted the NY State RETT minority transfer legislative language proposed by Governor Cuomo without change. The Senate’s [version](#) removed the proposed changes to the NY State RETT entirely. The passage of the one-house budget resolutions marks the official start to the final negotiations over the state budget in advance of the new fiscal year, which begins April 1.

**Current Law.** NY State RETT is generally imposed at a rate of 0.4 percent on transfers of interests in real property, including transfers of a “controlling interest” in an entity with an interest in New York real property (regardless of the relative value of the entity’s real estate assets). A “controlling interest” generally means 50% or more of the voting stock of a corporation or 50% or more of the capital, profits or beneficial interest in a partnership, association, trust or other entity. Separate transfers may be aggregated in some circumstances.

**Proposed Legislation.** Governor Cuomo’s budget proposal would extend NY State RETT to transfers of any percentage interest, including a minority interest, in certain entities that own real property located in New York with a fair market value of at least 50% of the total value of the entity’s assets. The entities covered by the proposal are partnerships, LLCs, S-corporations and non-publicly traded C-corporations with fewer than 100 shareholders.

- The rule appears to reach transfers of interests in all partnerships, LLCs and S-corporations that own sufficient amounts of New York State real property, regardless of how many equityholders such entity has. For example, this rule could apply to tax transfers of interests in a master limited partnership that, while publicly traded, is a partnership both for state legal and tax purposes. Although this rule does not appear to be targeted at REITs (which are C-Corporations for U.S. federal income tax purposes), the drafting creates some ambiguity as to whether this rule may apply to tax transfers of interests in REITs that are organized as LLCs or partnerships (even if the REIT is publicly traded). It could also apply to REITs organized as C-corporations that do not have 100 shareholders at the time of the transfer (for example, during the first taxable year for which the entity elects to be taxed as a REIT).
- The tax would be applied to “consideration” equal to the gross value of the entity’s real property located in New York multiplied by the percentage of the entity transferred. This may require an appraisal of the assets of the entity, so as to determine both whether the tax applies and, if it

does, the amount of “consideration” subject to tax. Gross real property value will often far exceed the actual consideration received for the equity transfer, which is based on net equity value.

- The proposal contains an “anti-stuffing” rule that disregards assets acquired within the preceding two years of the transfer when determining the value of all of the entity’s assets for purposes of calculating whether the entity owns real property located in New York with a fair market value of at least 50% of the total value of its assets (but not when determining the value of the entity’s real property located in New York, which, in turn, is relevant for determining the amount of “consideration” subject to tax). As currently drafted, this rule would appear to trigger application of the NY State RETT to any transfer of an interest in an entity within its first two years of operations if the entity holds any New York real estate at all.
- The proposal does not replace the current controlling interest provision. It is unclear whether the two provisions might inappropriately overlap in certain contexts, particularly when aggregation rules apply.

As currently drafted, the proposed expansion of the NY State RETT would be effective on the date on which the budget legislation is enacted into law and would apply to transfers occurring on and after that date.

**Next Steps.** As noted above, the passage of the one-house budget resolutions marks the official start to the final negotiations over the state budget. Each chamber’s budget may be viewed as an “opening bid.” In past years, this negotiation has taken the form of closed-door meetings between the Governor, the leaders of the majority conferences in both houses (Assembly Speaker Carl Heastie (D-Bronx) and Senate Majority Leader John Flanagan (R-2d (parts of Long Island))) and, in recent years, Independent Democratic Conference leader Jeff Klein (D-Bronx/Westchester). The Independent Democratic Conference released its **own** budget resolution on March 15<sup>th</sup> as well, which declined to adopt the Governor’s proposed expansion of the NY State RETT.

The budget is due before April 1, the start of the new fiscal year. While past governments have, at times, delivered budgets after this deadline, Governor Cuomo has generally met (or almost met) this deadline. In any event, we expect to see a draft of the negotiated budget this week.

As a final note, New York City imposes a separate tax on the transfer of real property located in New York City. This tax is similar, but not identical, to the NY State RETT, and it is imposed at a higher rate (2.625% on the transfer of commercial properties worth more than \$500,000, with a lower rate imposed on the transfer of commercial properties worth less than \$500,000 and on the transfer of residences). While we have seen no indication thus far that New York City will follow suit if the minority transfer proposal is enacted at the state level, we will continue to watch for efforts in New York City to enact a similar measure, which would have a more significant effect given the higher tax rate imposed.

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