THE STATE OF NEW HAMPSHIRE

HILLSBOROUGH, SS. NORTHERN DISTRICT

SUPERIOR COURT

First Berkshire Business Trust,
First Berkshire Business Property, LLC,
Second Berkshire Business Properly, LLC

v.

G. Philip Blatsos, Commissioner of the New Hampshire Department of Revenue Administration,
New Hampshire Department of Revenue Administration

Docket No. 07-E-0357

ORDER

Hearing held (07/20/09) in reference to Petitioners' Motion for Summary Judgment (filed 04/14/09) and Respondents' Motion for Summary Judgment (filed 04/14/09). Subsequent to review, the Court renders the following determination(s).

By way of brief background, the Petitioners are appealing a Final Order from the New Hampshire Department of Revenue Hearings Bureau finding that Petitioners must pay a real estate transfer tax, interest, and penalties. The Petitioners consists of three separate business organizations: First Berkshire Business Trust ("First Trust"); First Berkshire Properties, LLC ("First LLC"); and Second Berkshire Properties, LLC ("Second LLC"). First LLC was formed on March 19, 2003, and is 100% owned by First Trust. Second LLC was formed on May 22, 2003, and is 100% owned by First Trust. This Appeal arises out of two separate real estate transactions involving real property located at 200 John E. Devine Road in Manchester, New Hampshire ("the Property").

In 2002 and early 2003, First Trust was facing bankruptcy in the Southern District of New York. As a result, First Trust used Wells Fargo Bank to refinance nineteen

properties, including the Property. Wells Fargo required the creation of a single purpose entity ("SPE"), subsequently known as First LLC, as a condition to the refinancing. Wells Fargo required that First LLC be listed as the borrower of funds for the Property, that title to the Property be in the name of First LLC, and that a deed be executed to confirm that First LLC is listed as the legal owner of the Property. On April 7, 2003, First LLC entered into a mortgage with Wells Fargo Bank on the nineteen properties, including the Property. On April 11, 2003, a deed ("First Deed") from First Trust to First LLC was recorded in the Hillsborough County Register of Deeds. The First Deed states that the Property was deeded from First Trust to First LLC "in consideration of the sum of Ten Dollars ($10.00) and other good and valuable consideration" to be paid by First LLC. As a result of the transfer and subsequent refinancing, First Trust was able to avoid bankruptcy.

After the April 2003 refinancing, First Trust sought out better financing terms for a specific subset of the nineteen Wells Fargo financed properties, including the Property. First Trust then formed Second LLC in anticipation of the need for a SPE for the second refinancing of the Property. ING provided refinancing for six properties, including the Property. First Trust informed ING that it had created Second LLC in anticipation of the refinancing. ING approved this financing structure. On June 23, 2003, a deed ("Second Deed") from First LLC to Second LLC was executed. Second Deed was recorded in the Hillsborough County Registrar of Deeds on July 9, 2003. Second Deed states that the Property was deeded from First LLC to Second LLC "in consideration of the sum of Ten Dollars ($10.00) and other good and valuable consideration" to be paid by Second LLC.

On October 6, 2004, the Department of Revenue Administration ("the Department") issued notices of assessment, including additional tax, penalties and

interest ("the Assessment"), in the amount of $102,271.84 against First Trust and First LLC and in the amounts of $100,556.16 against First LLC and Second LLC. The Petitioners filed a Petition for Redetermination with the Department on December 2, 2004. Administrative hearings were held on November 3, 2005 and March 16, 2006. On July 30, 2007, the Department issued its Final Order upholding the Department's Assessment. The Department has stipulated to a revised Assessment figure of approximately $316,920.00 for additional tax, penalties, and interest calculated through March 31, 2009.

The Petitioners now bring this Appeal asserting that the Assessment violates RSA Chapter 78-B because no "sale, granting and transfer" of real estate occurred within the meaning of the statute. Specifically, the Petitioners argue that no contractual transfer occurred because there was no bargained-for exchange as the LLCs did not exist separate from their parent company, First Trust. The Petitioners further contend that even if this was a transfer of real estate, at least three exceptions to RSA 78-B:1 apply which prevent this taxation.

The Respondents object and argue that a bargained-for exchange took place when the LLCs received the property by warranty deed because even if the transfer occurred between related entities, the entities were legally separate and distinct from each other. The Respondents further assert that a bargained for exchange is not required for a contractual transfer, but even if it was required, a contractual transfer is, by definition, a bargained for exchange. Finally, the Respondents contend that the legislative history and amendments to RSA Chapter 78-B demonstrate that the legislature intended for transfers between related entities to be taxable.

The Court has jurisdiction to hear this Appeal, de novo, pursuant to RSA 21-J:28-

b, IV. In deciding this motion for summary judgment, "the [C]ourt must consider the evidence in the light most favorable to the party opposing the motion and take all reasonable inferences from the evidence in that party's favor." Barnsley v. Empire Mortgage Ltd. P'ship V, 142 N.H. 721, 723 (1998). "Summary judgment is appropriate when the evidence demonstrates that there is no genuine issue of material fact and that the moving party is entitled to judgment as a matter of law." Grossman v. Murray, 141 N.H. 265, 269 (1997). The Court, however, will not "weigh the contents of the parties' affidavits and resolve factual issues." Iannelli v. Burger King Corp., 145 N.H. 190, 193 (2000) (citation omitted). If "a reasonable basis exists to dispute the facts claimed in the moving party's affidavit . . . summary judgment must be denied." Id. The parties have agreed that there is no genuine issue of material facts. Therefore, the Court focuses only on the issues of law.

For the purposes of ease and clarity, the Court applies the analysis below only to the transaction which occurred between First Trust and First LLC. However, because the transaction between First LLC and Second LLC mirrors that of First Trust and First LLC, the conclusions reached below apply to both transactions.

RSA Chapter 78-B (2003 & Supp. 2008) governs the tax on the transfer of real property. Therefore, the Court first addresses whether the transaction between First Trust and First LLC is a sale or transfer of real estate as defined by this Chapter. RSA 78-B:1(a) (2003) states,

> A tax is imposed upon the sale, granting and transfer of real estate and any interest therein including transfers by operation of law. Each sale, grant and transfer of real estate, and each sale, grant and transfer of an interest in real estate shall be presumed taxable unless it is specifically exempt from taxation under RSA 78-B:2.

A "sale, granting and transfer" is defined as, "every contractual transfer of real estate, or

any interest in real estate from a person or entity to another person or entity, whether or not either person or entity is controlled directly or indirectly by the other person or entity in the transfer." RSA 78-B:1-a, V (emphasis added). A contractual transfer is defined as "a bargained-for exchange of all transfers of real estate or an interest therein, including but not limited to .... [f]rom any other interest holder to an organization in which he owns an interest." RSA 78-B:1-a, II.

In matters of statutory interpretation, the Court "first examine[s] the language of the statute, and where possible, ascribe[s] the plain and ordinary meanings to the words used. When a statute's language is plain and unambiguous, [the Court] need not look beyond it for further indication of legislative intent." Town of Acworth v. Fall Mt. Reg'l Sch. Dist., 151 N.H. 399, 401 (2004) (citation omitted). "An ambiguous tax statute will be construed against the taxing authority, rather than the taxpayer." In re Denman, 120 N.H. 568, 571 (1980).

Based on the plain language of RSA 78-B:1, the Court finds that the transfer of property to First LLC by warranty deed is a real estate transfer subject to the real estate transfer tax. Under RSA 78-B:1 a transfer tax must be paid whenever there is a transfer of property from one entity to another. Here, the property was transferred from one entity, First Trust, to another entity, First LLC. Although First Trust wholly owns First LLC, they are separate businesses, each entity is registered separately, and each entity has its own Operating Agreement. Therefore, First Deed, the warranty deed in this case, represented the transfer of real property from one entity to another.

The fact that First Trust wholly owns First LLC does not preclude a finding that this transaction was a transfer under RSA Chapter 78-B. Even if, as the Petitioners assert, First Trust had complete control over First LLC, thereby limiting its ability to

"bargain" in this contractual transfer, RSA 78-B:1-a, V states that "every contractual transfer of real estate" "whether or not either person or entity is controlled directly or indirectly by the other person or entity in the transfer" is a sale or transfer subject to RSA Chapter 78-B. An entity that is directly controlled by another entity likely has a reduced ability to bargain or to reject a transfer of property; however, under the plain language of the statute, the entities are not exempt from the transfer tax statute.

The Petitioners base their argument on the definition of contractual transfer, which RSA 78-B:1-a, II defines as "bargained-for exchange" and argues that because First Trust owned First LLC, it could not have engaged in a bargained-for exchange with itself and thus there was no contractual transfer. The Petitioners cite a number of cases from other jurisdictions which they contend supports this argument. At the hearing, the Respondents distinguished the Petitioners' case citations and emphasized that a bargained-for exchange involves a benefit and a detriment, which exists in this case because of the mortgage on the Property.

As previously determined, the fact that an entity is controlled by the entity with which it is transacting, does not preclude a finding of a contractual transfer under RSA Chapter 78-B. Therefore, the Court looks to whether a bargained-for exchange occurred. The Court finds that the term bargained-for exchange is not ambiguous and applies the plain meaning of the term. A bargained-for exchange means that the promisor manifests an intent to induce a promise or performance and the promisee manifests a corresponding intention. See Panto v. Moore Business Forms, 130 N.H. 730, 740 (1988). The terms appear to contemplate the exchange of a promise for a promise or a promise for performance, or vice versa. See Black's Law Dictionary, 169–70 (9th ed. 2009) (defining "bargain" as "an agreement between parties for the exchange

of promises or performance," and defining "bargained for exchange" as "[a] benefit or detriment that the parties to a contract agree to as the price of performance").

The Court finds that First Trust and First LLC engaged in a bargained-for exchange and thus a contractual transfer occurred subjecting the entities to the transfer tax under RSA Chapter 78-B. First Trust and First LLC exchanged performances in this real estate transaction. First Trust performed by transferring the Property and the mortgage to First LLC. In exchange, First LLC performed by accepting the Property and the mortgage and subsequently refinancing the mortgage. In doing this, First Trust received the benefit of not being forced into bankruptcy and the detriment of no longer owning the Property, while First LLC received the benefit of owning the Property and the detriment of paying the mortgage on said Property. Therefore, applying the plain meaning of bargained-for exchange, the entities did have a bargained-for exchange and a contractual transfer occurred. Because there was a contractual transfer of real estate from one entity, First Trust, to another entity, First LLC, there is a "sale, granting, and transfer" of real estate and it is subject to the transfer tax. RSA 78-B:1.

The Petitioners assert that like Crescent Miami Ctr., LLC v. Florida Dep't of Revenue, 903 So.2d 913 (Fla. 2005) this situation is simply a change in the form of ownership of property, without consideration, and is not subject to the real estate transfer tax. The Petitioners argue that "a change in the form of ownership of property, without an exchange of value, does not constitute consideration." Pet. Mtn. At 17 (quoting Crescent, 903 So.2d at 918). The Court finds Crescent distinguishable from this case because Crescent only addressed the transfer of a title, not the transfer of a title and a mortgage. Here, First Trust transferred the Property and the mortgage on the Property. Additionally, here, there was consideration for the Petitioners' transfer in the

form of the mortgage on the Property. See RSA 78-B:1-a, IV. Accordingly, the Court finds Crescent Miami Center inapplicable.

Moreover, the Court finds Mandell v. Gavin, 816 A.2d 619 (Conn. 2003) and Tranfo v. Gavin, 817 A.2d 88 (Conn. 2003) equally inapplicable. The Petitioners assert that like Mandell and Tranfo, there was no consideration for the transfers because there was no bargained-for exchange. In Mandell, the Court found that there was no bargained-for exchange because the transferor acted "unilaterally" when he transferred the property, the transferee was a "passive recipient" of the property, and the property was not transferred in exchange for any performance or return promise. Mandell, 816 A.2d at 625. Here, First LLC did not passively receive the Property because it received the Property under the expectation that it would refinance the Property and subsequently did refinance the Property. Further, as stated above, there was an exchange of promises because of the existence of the mortgage at the time of the transfer and the subsequent refinance of the mortgage by First LLC. Accordingly, Mandell and Tranfo are inapplicable to the facts of this case and the Petitioners are subject to the real estate transfer tax under RSA Chapter 78-B.

The Petitioners next argue that they are exempt from the transfer tax under three express exceptions outlined in RSA 78-B:2. Specifically, the Petitioners assert that they qualify under the exceptions outlined in RSA 78-B:2, III, IV, and V. First, the Petitioners contend that this is a "refinancing transaction" and is exempt under RSA 78-B:2, V because it is analogous to a correctional or confirmatory deed which does not change the beneficial interest in the property. Exton Plaza Assocs. v. Cmmw., 763 A.2d 521 (Pa. Cmmw. Ct. 2000). RSA 78-B:2, V states that the real estate transfer tax shall not apply to "a deed or other instrument which corrects a deed or other instrument

previously given." The Court is not persuaded that RSA 78-B:2, V applies to this situation because there is no evidence of any mistakes in the prior deed, which needed correcting. Further, there was no evidence that the original deed was intended to convey the Property to First LLC but the deed erroneously conveyed the Property to First Trust and this deed was needed to correct the Property's ownership. Finally, the Court does not find Exton analogous to Petitioners' situation. In Exton the deed "accomplished nothing more than recording a name change after a reorganization from a general partnership to a limited partnership" and "did not effect a meaningful transfer of title." 763 A.2d at 523. In Exton there was no other corporation involved, whereas, here, there is the development of an entirely new corporation, not the modification of a current business structure. Further, Exton is limited by the Commonwealth Court of Pennsylvania's recent ruling in Gudzan v. Cmmw., 962 A.2d 718, 723 (Cmmw. Ct. Pa. 2008). Gudzan limited Exton's holding to transfers occurring as a result of a change in the business structure of an entity. Id. The transfer which occurred here, was not the result of a change in the business structure, but the creation of an entirely new corporation and the subsequent transfer of property to that corporation. Accordingly, the Petitioners do not meet the real estate transfer tax exception outlined in RSA 78-B:2, V.

The Petitioners next assert that they fall within the exception of RSA 78-B:2, III, which states that the real estate transfer tax does not apply "[t]o a mortgage or other instrument given to secure payment of a debt or obligation." The Court find this exception inapplicable because First Trust did not transfer the Property or the mortgage to First LLC to secure a payment of a debt that First Trust owed First LLC. Similarly, the Court finds RSA 78-B:2, IV inapplicable because First Trust did not discharge the

Property or the mortgage to First LLC "solely to release security for a debt or obligation." Therefore, none of the exceptions listed in RSA 78-B:2 apply to the Petitioners and the Petitioners are subject to the real estate transfer tax.

Despite the Petitioners' repeated assertions that they should not be subject to the real estate transfer tax because this is a "refinancing," the Court finds that this is not simply a refinancing. First Trust transferred the Property and its mortgage to First LLC. Subsequently, First LLC refinanced the mortgage on the Property. There is no tax obligation arising from the refinancing of the mortgage. Nevertheless, a tax obligation did arise as a result of the transfer of the Property and its mortgage, which occurred prior to the refinancing.

The Petitioners further assert that this transaction is a "transfer in form and not substance" and is therefore not taxable under RSA 78-B:9. Pet. Mtn. at 19. The Petitioners assert that under RSA 78-B:9 II, "if there is occasion to determine if there has been a sale, grant or transfer of real estate within this state, the commissioner shall look to the substance of the transaction or series of transactions to determine if a sale, grant or transfer of real estate has occurred." The Court finds that even if the Department looked at the substance of the transfer, it could reasonably conclude that a substantive transfer occurred under the plain language of RSA Chapter 78-B because one entity transferred property to another entity. This is a type of transfer recognized by the legislature as eligible for taxation, therefore, it is a transfer in substance, not merely a transfer in form.

The Petitioners contend that Department's interpretation of RSA Chapter 78-B violates the New Hampshire Constitution. The Petitioners assert that it is unconstitutional because it "would subject to tax those refinancing that use single

purpose entities while exempting from tax those refinancing that do not use single purpose entities." Pet. Mtn. at 22. Part I, Art. 23, and Part II, Art. 5 and 6 of the New Hampshire Constitution "work in conjunction to ensure the fairness of any scheme of taxation enacted by our legislature." Smith v. Dept. of Revenue Admin., 141 N.H. 681, 686 (1997). The Petitioners correctly note that "these three constitutional provisions require that taxation be just, equal, and proportional; in addition, our constitution demands that classifications be made between types of property, not taxpayers." Id. However, the Court is persuaded that under the Department's analysis, the taxpayers are still being treated the same. No taxpayer who chooses to refinance is taxed on that refinance. Further, all transfers of Property from one entity to another entity are taxed on that transfer. There is no unequal, unjust, or disproportionate result.

Because the Court has determined that this is a sale, grant or transfer of real estate and the Petitioners do not meet any of the exceptions set forth in RSA 78-B:2, the Court must determine the amount of tax, if any, to be imposed on said transfer. The Petitioners assert that the tax imposed should be based on the price paid for the property, which is $10.00. See RSA 78-B:1-a, IV. The Petitioners further argue that the Department cannot base the tax on the fair market value of the Property because there was no proof refuting the $10.00 purchase price. The Respondents contend that the Petitioners should be taxed on the full market value of the Property because the transferee in this case, First LLC, assumed an obligation from the transferor, First Trust, in the form of a mortgage on the Property. See RSA 78-B:1-a, IV. Further, the Respondents assert that the Department had the authority to determine the fair market value of the Property because the Petitioners did not represent the fair market value in the transfer. See RSA 78-B:9, III.

The rate of tax imposed on a transfer of real estate is: ".75 per $100, or fractional part thereof, of the price or consideration for such sale, grant, or transfer; except that where the price or consideration is $4,000 or less there shall be a minimum tax of $20." RSA 78-B:1, I(b). "Price or consideration" is defined as:

> the amount of money, or other property and services, or property or services valued in money which is given in exchange for real estate, and measured at a time immediately after the transfer of the real estate. The value of such consideration in contractual transfers where the property exchanged includes the surrender of rights or choses-in-action by the transferee, including the surrender of shareholder or beneficial interest holder rights in liquidation of a corporation or other entity, the forgiveness of an obligation owed to the transferee, or the assumption of an obligation by the transferee, shall be no less than the fair market value of the real estate or interest in such real estate as determined by the department pursuant to RSA 78-B:9, III.

RSA 78-B:1-a, IV. (emphasis added). Under RSA 78-B:9, III,

> [i]f there is occasion to determine if the stated price or consideration is the actual paid or required to be paid or consideration, then the commissioner shall have the power, barring specific proof to the contrary, to determine the actual price or consideration by the fair market value of the real estate.

Here, the Property was deeded from First Trust to First LLC "in consideration of the sum of Ten Dollars ($10.00) and other good and valuable consideration." Ex. A-6. The Court agrees with the Petitioners that the price of the property is $10.00. However, the Property was transferred for $10.00 and "other good and valuable consideration." Here, the "other good and valuable consideration" includes the mortgage on the Property. It is clear the legislature intended that when a piece of property is transferred with a mortgage, the mortgage serves as consideration. See RSA 78-B:1, I(b) ("The value of such consideration in contractual transfers where the property exchanged includes . . . assumption of an obligation by the transferee...."). Further, because the mortgage was included in the transfer of the Property, the Petitioners assumed the

obligation of the mortgage. Where the transferee assumes an obligation, such as a mortgage, the value of said consideration "shall be no less than the fair market value of the real estate as determined by the department pursuant to RSA 78-B:9, III." RSA 78-B:1-a, IV. Therefore, the Department had the authority to determine the fair market value of the Property and the Department properly assessed the tax on the fair market value of the Property. Accordingly, as to this issue, the Petitioners' Motion for Summary Judgment is **DENIED** and the Respondents' Motion for Summary Judgment is **GRANTED.**

In addition to the assessment of tax on the fair market value of the Property, the Department assessed interest on the amount of tax that the Petitioners owed. The Petitioners do not appear to object to the assessment of said interest. The Court agrees with the Department that the interest was properly applied to the amount owed by the Petitioners. RSA 21-J:28 (2000) states, in relevant part,

> [f]or all taxes administered by the department, interest on amounts not paid when due shall be computed at the annual underpayment rate . . . from the prescribed payment date or original statutory due date to the date payment is actually made.

Because the interest assessed is not a "penalty," see RSA 21-J:32, RSA 21-J:33, and the application of interest is not discretionary, see RSA 21-J:28 (stating interest "shall" be computed), the Department correctly assessed interest in this case. Accordingly, as to interest, the Respondents' Motion for Summary Judgment is **GRANTED.**

The Petitioners next dispute the penalties imposed on them by the Department. The Department imposed a 10% failure to pay penalty on the Petitioners under RSA 21-J:33. The Respondents argue that these penalties are appropriate because the Petitioners did not prove that "they exercised ordinary business care and prudence, but

were, nonetheless, unable to pay the taxes due prior to the statutory filing date, due to circumstances beyond their control." Resp. Mtn. at 12. The Petitioners assert that the penalty is illogical and unfair because they could not have known, as a legal matter, that any taxes would be due. The Petitioners further analogize to the federal income tax system which requires that taxpayers know of the demand for taxes prior to being subject to penalties for failure to pay that tax.

Under RSA 21-J:33, a penalty may be assessed against a taxpayer who fails to pay tax when due. RSA 21-J:33 (Supp. 2008) states, in relevant part,

> [i]f the failure to pay is not due to fraud, the penalty shall be equal to 10 percent of the amount of the nonpayment or underpayment. This penalty shall not be applied in any case in which the failure to pay was due to reasonable cause and not willful neglect of the taxpayer.

The taxpayer bears the burden of proving that "the failure to file a tax return or to pay a tax timely was due to reasonable cause, rather than willful neglect...." Appeal of Steele Hill Dev., Inc., 121 N.H. 881, 885 (1991).

RSA Chapter 21-J does not define the terms "reasonable cause" or "willful neglect." However, the United States Supreme Court interpreted language identical to that of RSA 21-J:33 when it interpreted Internal Revenue Code section 6651(a). See United States v. Boyle, Ex', 469 U.S. 241 (1985). The Boyle Court stated that "willful neglect" is a "conscious, intentional failure or reckless indifference." Id. at 243. "Reasonable cause" exists where there is an exercise of ordinary business care and prudence, and the taxpayer was nevertheless unable to file the return within the prescribed time. Id. at 246.

The Court finds that the Petitioners' conduct did not amount to willful neglect. There is no evidence that the Petitioners transferred the Property in this manner in an

attempt to avoid paying the transfer tax. The Petitioners were required by the lender to create the single business entities and transfer the Property and mortgage to the single business entities in order to secure refinancing. Moreover, the Petitioners did not willfully ignore the transfer tax statute, but paid only the amount that they believed was owed. Although the Petitioners erred in the amount owed, they did not fail to pay a transfer tax. Accordingly, the Petitioners did not willfully neglect to pay the transfer tax.

The Court further finds that the Petitioners' failure to pay the transfer tax was due to reasonable cause. The transfer of property to a single business entity is a unique situation, one that has not yet been addressed by New Hampshire statutes or case law. This was not a case of a taxpayer simply failing to meet a tax deadline, but was the result of misinterpretation of the law concerning real estate tax transfers. Although the Court now finds that the Petitioners erred in their interpretation of the law, the Court is persuaded that a misinterpretation of law concerning a novel issue that has not yet been addressed in this jurisdiction does not justify the imposition of penalties. Accordingly, the Department's imposition of penalties is **REVERSED.**

The Petitioners represented to the Court that the Department had stipulated to a revised Assessment figure of approximately $316,920.00 for the transfer tax, penalties and interest, calculated through March 31, 2009. The Court directs that the Department shall calculate the amount of taxes and interest due consistent with the provisions of this Order .

Consistent with the above, the Court finds that the transfer of the Property from First Trust to First LLC and subsequently from First LLC to Second LLC is a sale, grant and transfer of the Property under RSA 78-B:1. Accordingly, the transfers are subject to the real estate transfer tax. Additionally, the Department properly imposed a tax on the

transfers based upon the fair market value of the Property because the transferee in each transaction assumed the liability of a mortgage with the Property transfer. The Department, however, erred in imposing penalties on the Petitioners because reasonable cause existed in the Petitioners misapplication of the transfer tax statute and subsequent tax payment. Accordingly, Petitioners' Motion for Summary Judgment is **GRANTED, IN PART** and **DENIED, IN PART** and the Respondents' Motion for Summary Judgment is **GRANTED, IN PART** and **DENIED, IN PART,** consistent with the above.

SO ORDERED.

9/28/09
Date

James D. O'Neill, III
Presiding Justice