The State of New Hampshire

ROCKINGHAM COUNTY **SUPERIOR COURT**

Say Pease IV, LLC and Say Pease, LLC

v.

New Hampshire Department of Revenue Administration

Docket No.: 09-E-0330

ORDER ON MOTIONS FOR SUMMARY JUDGMENT

The parties are before the Court on a de novo appeal of a decision by the Department of Revenue Administration imposing a tax on the transfer of interest in a real estate holding company from petitioner, Say Pease, LLC, to petitioner, Say Pease IV, LLC. The parties filed an Agreed Stipulation of Facts and List of Exhibits, a Motion to Bring Forward, and now move for summary judgment. The parties agree that there are no genuine issues of material fact in dispute, and, thus, ask the Court to decide the case on summary judgment grounds. The Court concludes the petitioners are entitled to summary judgment as follows.

The parties stipulate to, and the Court finds, the following relevant facts. Two International Group, LLC (TIG) is a real estate holding company, formed on June 23, 1997. Say Pease, LLC ("Say Pease") was one of TIG's four original members with a 47.5% interest in TIG. Pease was formed on June 16 1997,

In August of 1997, TIG leased a parcel of land at the Pease International Tradeport in Portsmouth, New Hampshire. In September of 1999, TIG obtained an $8,325,000 construction mortgage loan with First Essex Bank, FSB, for the construction of a multi-unit commercial office and related uses building known as "Two International." In August of

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2004, once the building was substantially leased to third party tenants, TIG sought permanent financing to replace the construction loan.

Merrill Lynch Mortgaging Lending, Inc., issued a "securitized" Mortgage Loan Commitment to TIG, in the amount of $10,500,000. In its commitment letter, Merrill Lynch included a condition typical in "securitized" mortgage loans whereby TIG and its members were required to be "single purpose bankruptcy remote entities" ("SPE"). The SPE requirement served the purpose of insulating the real estate owning entity (in this case, TIG), from any potential adverse consequences which might result from the ownership of investments other than the mortgaged property (in this case Two International), by TIG or any of its members.

Although TIG qualified as an SPE, Say Pease did not so qualify because it held membership interests in other entities that owned other real estate projects at Pease Tradeport. In order to satisfy Merrill Lynch's SPE requirements, the members of Say Pease formed a new LLC—Say Pease IV. Say Pease IV had the same members as Say Pease. Through an Assignment and Consent to Assignment Agreement dated September 23, 2004, Say Pease IV became the holder of the 47.5% interest in TIG. On September 23, 2004 Merrill Lynch obtained an appraisal of the TIG property which stated that the Fair Market Estimate was $12,700,000.

On October 26, 2004, TIG amended its Limited Liability Company Agreement, replacing Say Pease with Say Pease IV. On that same day, TIG obtained the $10,500,000 mortgage loan.

On October 6, 2005, the Audit Division of the New Hampshire Department of Revenue ("Audit") received TIG's 2004 New Hampshire Business Tax Return. Attached to TIG's Return was a Schedule K-1s for Say Pease and Say Pease IV. The Schedule K-1 for Say Pease reported a beginning ownership in TIG of 47.5% and a 0% ownership interest in TIG at the end of 2004. Conversely, the Schedule K-1 for Say Pease IV reported a beginning ownership interest in TIG of 0% and a 47.5% ownership interest in TIG at the end of 2004.

In June of 2007, Audit reviewed the changes in TIG ownership interests for the purpose of compliance with RSA Chapter 78-B, the Real Estate Transfer Tax. In doing so, Audit determined that the transfer was taxable under RSA 78-B:1-a, V.

Following an April 7, 2008 Proposed Tax Assessment, Audit issued a Notice of Assessment on May 13, 2008 against Say Pease and Say Pease IV claiming non-payment of Real Estate Transfer Taxes under RSA 78:B. The assessed amount of \$90,488.00 (\$45,244.00 for each Petitioner) was calculated as follows: \$12,700,000 (fair market value) times 47.5% (interest in TIG), which equals \$6,032,500, times 1.5% (transfer tax rate), which equals \$90,488,000. As of the May 13, 2008 Notice of Assessment, Audit calculated that each Petitioner owed \$74,305,000 in taxes, interest and penalties. This number has increased due to interest continuing to accrue at a rate of \$12.35 a day.

The Petitioners perfected their appeal through the Department's Administrative Appeal Process. Pursuant to RSA 21-J:28 (b) IV, this Court now has jurisdiction to hear this case de novo.

Specifically at issue in this case is whether, pursuant to RSA Chapter 78-B, the governing statute on real estate transfer tax, the transfer of interest in TIG from Say Pease to Say Pease IV was a bargained-for exchange, and thus a taxable "contractual transfer." RSA Chapter 78-B defines a "sale, granting, and transfer" as, "every contractual transfer of real estate, or any interest in real estate from a person or entity to another person or entity

. . . ." See RSA 78-B:1-a, II. The statute further defines a "contractual transfer" as "a bargained for exchange." RSA 78-B:1-a. II. Petitioners argue that the transfer was not bargained-for because it did not involve an exchange of cash. Respondent objects and argues that the transfer was bargained-for because it involved value of a different kind-- a 47.5% interest in TIG in exchange for assuming liability for the original and subsequent mortgages. In support of their arguments, both parties analogize the present case to two previous Superior Court decisions.

In Z.B.H Realty LLC v. NH Dept. of Rev. Admin., dated 8/25/09 (Nicolosi, J., Cheshire), the state assessed a tax on a property transfer to an LLC from one of its members. In order to determine whether the transfer was "contractual," the Court contemplated the meaning of "bargained-for," writing:

> 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). It contemplates 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 in Z.B.H. found that, in exchange for the land, the member received no promise, money, property, or services from the LLC. The transfer was, in essence, a gift. Because the Court found no bargained-for exchange, the transfer was not "contractual" and thus not taxable under RSA Chapter 78:B.

The Court reached a different conclusion in First Berkshire Trust v. NH Dept. of Rev. Admin., 9/28/09, (O'Neill, J., Hillsborough). In that case, First Trust, a real estate holding company, sought refinancing for certain properties so that it could emerge from bankruptcy. First Trust's lender, like the lender in the present case, required the creation of an SPE as a condition of refinancing. First Trust created an SPE known as First LLC and was First LLC's sole member. First Trust then transferred certain properties to First LLC. The deed stated in relevant part that the property in question was transferred "in consideration of the sum of Ten Dollars ($10.00) and other goods and valuable consideration" to be paid by First LLC. In exchange for the transfer of property, First LLC sought refinancing. As a result First Trust was able to avoid bankruptcy. The Court in First Berkshire held that the transfer did qualify as a bargained-for exchange because the parties exchanged promises of performance, explaining:

> 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.

Respondent urges the Court to find that the Petitioners exchanged performances similar to those exchanged in First Berkshire, arguing that Say Pease performed by transferring its interest in TIG to Say Pease IV and, in exchange, "was freed from its original debt and the liabilities of the new loan." In exchange for the 47.5% interest in TIG, the Respondent contends that Say Pease IV accepted the detriment of becoming "responsible, under TIG's operating agreement, for its share of the new $10,500,000 loan."

The Court finds that the present case is distinguishable from First Berkshire in three important ways. First, the possibility of refinancing in the present case does not carry with it the same weight as the refinancing in First Berkshire. In that case, First Trust was facing bankruptcy. The ability to refinance through a new LLC was vital to First Trust's existence. Therefore, its value, such that it constituted consideration, was derived from its importance to First Trust. Here, there are no facts to suggest that that Say Pease, Say Pease IV, or even the mortgagor, TIG, were facing financial difficulties. TIG simply sought more favorable financing. As the Court pointed out in First Berkshire, no tax obligation arises from refinancing a mortgage. Accordingly, the Court finds that the mortgages, to the extent that they pertain to the Petitioners, did not have sufficient value to the Petitioners to constitute consideration.

This case is also distinguishable from First Berkshire because the Petitioners, as non-mortgagors, had no legal authority to make promises concerning TIG's loans. The holding in First Berkshire is based, in part, on the fact that First Trust and First LLC were mortgagors. As such, they were in a position to make legally binding promises of performance. In the present case, however, TIG was the mortgagor for both the original and the refinanced loan. Though the present parties agree that the purpose of the property transfer was to *enable* TIG to qualify for refinancing, Say Pease IV could not be held liable to Say Pease if TIG failed to follow through with the refinancing.

Finally, and most significantly, this case is distinguishable from First Berkshire because neither of the Petitioners were personally liable for TIG's mortgages when the transfer took place. It is well established that the "owner of an interest in a limited liability company is not personally obligated for the debts of the company simply because of the ownership interest." See In re Felt Mfg. Co., Inc., 371 B.R. 589, 643 (Bkrtcy.D.N.H., 2007). The statute governing LLC member liability to third parties, RSA 304-C:25, states that:

> [T]he debts, obligations and liabilities of a limited liability company, whether arising in contract, tort or otherwise, shall be solely the debts, obligations and liabilities of the limited liability company and no member or manager of a limited liability company shall be obligated personally, for any such debt, obligation or liability of the limited

liability company solely by reason of being a member or acting as a manager of the limited liability company.

Though an LLC member's liability could be expanded by the LLC agreement, no such liability arose in this case. Paragraph 12.2 of the agreement, entitled "Profits and Losses," provides that "all net profits and net losses allocated to the members shall be allocated among them on the basis of their respective Interests." TIG can allocate net losses to its members' capital accounts at the end of the calendar year and members are obligated to TIG to replenish those funds according to Treasure Regulations. See TIG Agreement, Sections, 12.1(c), 12.2, and 17. The obligation to restore those funds is owed to TIG. Members would not have been personally liable to *debtors* unless the company went into dissolution—and then, only if the member's capital fund had a deficit. Respondent presented no facts to suggest that TIG suffered a net loss in the previous year, that Say Pease had a deficit in its capital account, that TIG predicted net losses for the following year, or that TIG was heading toward dissolution. In short, nothing had occurred to trigger Say Pease's personal liability for TIG's debts. Under these ordinary circumstances, Say Pease was safely within the protections of the LLC structure. TIG's original mortgage was not a burden that Say Pease would benefit from unloading. Nor was it a burden for Say Pease IV to accept in exchange for the benefit of gaining the interest in TIG. Thus there was no bargained for exchange between Petitioners.

Accordingly, the Court holds that the transfer is not a "contractual transfer," and is thus not taxable pursuant to RSA 78-B.

SO ORDERED

DATED: November 9, 2010

KENNETH R. McHUGH
Presiding Justice