Office of Chief Counsel
Internal Revenue Service

memorandum

CC:LM:FS:LI:TL-N-1967-01
DRMirabito

date: July 11, 2001

to: Eugene Spitzer, Group Manager, Group 1347
Attention: Ellen Labeck, Team Coordinator

from: Jody Tancer, Associate Area Counsel
(Financial Services:Long Island)

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subject: [redacted]
[redacted] **Cycle**

Our memorandum dated June 8, 2001 (the June 8th memorandum) provided advice to you on whether [redacted] was entitled to a deduction in the taxable year ended [redacted] for rent paid for the entire period [redacted] through [redacted] and on whether the Service might disallow a charitable contribution deduction claimed by [redacted] for a donation of appreciated stock. The June 8th memorandum has been reviewed by the Office of Chief Counsel. This memorandum is to supplement the earlier document. This memorandum should not be cited as precedent.

Please note that as a result of that review you may now rely on our advice to you as expanded or modified in this memorandum.

Issue 1.

Analysis of Internal Revenue Code § 467

You may rely on our advice that [redacted] ([redacted]) may only deduct in the taxable year ended [redacted] the amount of rent paid in [redacted] and [redacted] of that year. However, please note that [redacted] is not entitled to a deduction for the full amount of the rent paid ($[redacted]) since the Transmittal dated [redacted] from [redacted] includes an interest amortization schedule reflecting interest amounts payable by the lessor to the lessee totaling $[redacted]. This total amount constitutes a discount in consideration for the advance rental payment. Therefore, [redacted] must include in income for the taxable year [redacted] the amount of interest allocable to [redacted] and [redacted] as stated in the Transmittal. Alternatively, [redacted] may be allowed to offset the rental

amounts allocated to [redacted] and [redacted] by the interest allocable to those months. Thus, under the offset alternative, [redacted] would be permitted to deduct the amount of $[redacted] ($[redacted] for [redacted] and the amount of $[redacted] ($[redacted]) for [redacted].

Further, please note that the § 467 regulations do not apply to the modification as set forth in the Transmittal because that agreement was entered into prior to the effective date of these regulations.

Analysis of New York State Law

Please note that the Service should not argue that the Transmittal dated [redacted] was not a proper modification of the [redacted] Lease between [redacted] and [redacted]. Essentially, the argument under state law should not be raised as neither the tenant nor the landlord assert that the Transmittal does not reflect a valid agreement and because both parties performed in accordance with the terms of the Transmittal. Therefore, you should not rely on our discussion of state law in the June 8th memorandum.

Issue 2.

You may rely on our advice in the June 8th memorandum on this issue. In addition, please note:

1. Generally, a donor will not recognize gain on a contribution of appreciated property to charity. However, a donor may recognize gain where there is a prearranged plan that requires the donee to enter into transactions involving the donated property that benefit the donor. See Blake v. Commissioner, 697 F.2d 473 (2d Cir. 1982), aff'g T.C. Memo. 1981-579; Notice 99-36, 1999-1 C.B. 1284.

2. Internal Revenue Code § 170(e)(1)(A) provides that the amount of any charitable contribution of property shall be reduced by the amount of gain that would not have been long-term capital gain if the property had been sold by the taxpayer at fair market value at the time of contribution. Further, § 170(e)(1)(B)(ii) provides generally that donors making charitable contributions of capital gain property to or for the use of a privation foundation (as defined in Internal Revenue Code § 509(a)) other than a private foundation described in § 170(b)(1)(E), are not permitted a charitable contribution deduction for the amount of the contributed property that would have been long-term capital gain if the property contributed had been sold by the taxpayer at fair market value.

In addition, § 170(e)(5) is an exception to the general rule of § 170(e)(1) and allows a deduction for contributions of qualified appreciated stock. § 170(e)(5)(B) defines qualified appreciated stock as any stock of a corporation: (a) for which, as of the date of contribution, market quotations are readily available on an established securities market, and (b) which is capital gain property as defined in § 170(b)(1)(C)(iv). However, under § 170(e)(5)(C)(i), the term qualified appreciated stock shall not include any stock of a corporation in a contribution to which § 170(e)(1)(B)(ii) applied (determined without regard to § 170(e)(5)) to the extent that the amount of the stock contributed (including prior contributions of the donor) exceeds 10 percent in value of the outstanding stock of the corporation. You should replace paragraph 2. of page 15 with the above.

3. You may rely on our advice on page 15 that § 170(b)(2) does not apply to [redacted] as it is a Subchapter S corporation and that the Service may not disallow the claimed deduction solely on that ground. However, please note that the individual contribution limitation of § 170(b)(1) may apply to the shareholders.

4. The charitable contribution must be substantiated in accord with § 170(f)(8).

If you have any questions regarding this memorandum or the June 8th memorandum, please contact Diane Mirabito at (516) 688-1709.

DISCLOSURE STATEMENT

This writing may contain privileged information. Any unauthorized disclosure of this writing may have an adverse effect on privileges, such as the attorney client privilege. If disclosure becomes necessary, please contact this office for our views.

JODY TANCER
Associate Area Counsel
(Large and Mid-Size Business)

By: Diane R. Mirabito
DIANE R. MIRABITO
Attorney (LMSB)

Office of Chief Counsel
Internal Revenue Service

memorandum

CC:LM:FSH:LI:TL-N-1967-01
DRMirabito

date: June 8, 2001

to: Gene Spitzer, Group Manager, Group 1347
Attention: Ellen Labeck, Team Coordinator

from: Jody Tancer, Associate Area Counsel
(Financial Services and Health Care:Long Island)

subject: [redacted]
[redacted] **Cycle**

This memorandum responds to your memorandum dated April 30, 2001 requesting advice on the Issues listed below. This memorandum should not be cited as precedent.

ISSUES

1. Whether [redacted] is entitled to a deduction in the taxable year ended [redacted] for rent paid as of [redacted] for the period [redacted] through [redacted]

2. Whether the Service may disallow a charitable contribution deduction claimed by a Subchapter S corporation for the donation of appreciated stock?

CONCLUSIONS

1. Based on the information provided, at most [redacted] is entitled to a deduction in the taxable year [redacted] for rent paid for that taxable year only. However, we recommend further factual development of this issue.

2. Based on the information provided, the Service should not disallow the claimed charitable contribution at this time. Again, we recommend further factual development.

FACTS

The facts, as we understand them, are as follows:

Issue 1.

[redacted] ([redacted] or taxpayer) filed consolidated returns (Form 1120) for each of the taxable years ended [redacted], [redacted] and [redacted]. Each of these taxable years is currently under audit.

On [redacted], [redacted] ([redacted] or Tenant), a subsidiary of the taxpayer, entered into a consolidated, modified and restated lease (the Lease) with the [redacted] ([redacted]) for the period [redacted] through [redacted]. The Lease included [redacted] additional [redacted]-year renewal options. [redacted] was named in the Lease as a Guarantor. According to the copy you provided, the Lease contained the following terms:

Article [redacted] Rent

[redacted]

Section [redacted] Miscellaneous

[redacted]

According to Schedule of the Lease, Annual Fixed Rent was due as follows:

OFFICE SPACE

Lease Year	Monthly	Annually
	$	$

BASEMENT AND SUB-BASEMENT

	$	$

In a prior audited cycle, after analyzing Internal Revenue Code §§ 467(a)(1), 467(d)(1), 467 (b)(1), 467(b)(2), 467(b)(3), and 467(b)(4) and the decision in Picadilly Cafeterias, Inc. v. United States, 36 Fed Cl 330 (1996), the agent determined the extra rent deducted by the taxpayer as rent normalization[1] was improper. Ultimately, the Service and the taxpayer agreed that the taxpayer was only entitled to deduct rent expense per the rent payment schedules attached to the Lease rather than the rent normalization amount. Amended Forms 1120 were filed for the and taxable years removing the rent normalization amount from the returns. The present audit team agrees with the

[1] According to the prior agent's workpapers, per a financial statement footnote made by the taxpayer, the totals per a schedule of future minimum rental payments were expensed pro rata over the initial terms of the Lease. Further, since no Schedule M adjustments were made, the tax treatment was the same. The extra amount expensed for tax and book purposes was the difference between "straight line rent" and rent actually paid. The taxpayer referred to the extra expense as "rent normalization."

treatment of rent expense reflected in these amended returns.

However, even though the rent normalization amount for the taxable year [redacted] equaled $[redacted], the taxpayer did not file an amended return for that taxable year. Rather, the taxpayer/[redacted] first paid [redacted] increased monies in the amount of $[redacted] purportedly for increased rent for the period [redacted] through [redacted] ([redacted] payment of rent per the Transmittal). Second, the taxpayer netted the [redacted] rent paid and the rent normalization amount for [redacted] ($[redacted]); the net amount was $[redacted]. The taxpayer claims that the landlord requested these increased rental amounts and has provided a Telecopier Transmittal (Transmittal) dated [redacted] from [redacted] to substantiate the claim. We understand that the taxpayer's accountant informed the audit team that the Transmittal is the only document he has memorializing this agreement imposing higher rent for the specified [redacted] months. That Transmittal states:

[redacted]

The Transmittal calculates advance payment of rent as follows:

Period	Rent
[redacted]	$[redacted]

Below is our comparison of the monthly amounts of total Annual Fixed Rent (Office Space plus Basement Space) due under the Lease per its Schedule [redacted] and the monthly payments stated in the Transmittal:

Period	Lease Amount	Transmittal Amount	Difference
[redacted]	$[redacted]	$[redacted]	$[redacted]

You have informed us that the taxpayer takes the position that the Lease was substantially modified for the year and, under Internal Revenue Code § 467 and Treas. Reg. § 1.467-1(f), it is entitled to deduct rent expense per the Transmittal in the taxable year for the entire month period. The team takes the position that the taxpayer should have filed an amended return for the taxable year removing any rent normalization claimed and removing rent paid for the period through in the total amount of $. This amount would be allowable in the taxable year .

Issue 2.

( ) filed consolidated Forms 1120 for the fiscal years ended and . On , became a Subchapter S corporation with shareholders, and . Forms 1120S were filed for each of the taxable years ended and . On their individual returns, the shareholders each reported flow-through income and claimed deductions from . The audit of includes an examination of Please note that for purposes of this memorandum, we assume that is entitled to Subchapter S status.

On , contributed shares of common capital stock, with a fair market value of $, to the (the). On its Form 1120S for the taxable year claimed a contribution expense equal to the fair market value of the stock. 's basis in the stock was $; accordingly, the shareholders claimed flow-through deductions totaling $.

The audit team takes the position that an unrecognized gain in the amount of $ exists. This position is based on the fact that if had sold the stock rather than contributing it to the , a capital gain would have been realized. Accordingly, the shareholders received the benefit of the contribution deduction instead of having to pay a large capital gain tax.

ANALYSIS

Issue 1.

We understand from your memorandum requesting advice that the taxpayer argues only that the Lease was substantially modified pursuant to the pertinent regulations under Internal Revenue Code § 467 for the [redacted] taxable year. Accordingly, [redacted] is entitled to deduct rent expense per the rental payment schedule as modified by the Transmittal. Therefore, we address only that position and not any other arguments which might be raised under § 467. Further, we understand that the taxpayer has provided you with, and relies upon, the Transmittal dated [redacted] for support of its position. In addition, in our opinion, the Lease between [redacted] and [redacted] qualifies as a section 467 rental agreement under § 467(d).

Internal Revenue Code § 467

Temporarily putting aside the question whether the Transmittal effectively modified the Lease under New York state law, we first analyze the effect of § 467 and its pertinent regulations. In pertinent part, § 467(a) provides that a lessee under any section 467 agreement shall take into account for any taxable year the amount of rent accruing during such taxable year as determined under § 467(b)(1). The latter section provides that the determination of the amount of rent under any section 467 rental agreement which accrues during any taxable year shall be made by allocating rents in accordance with the agreement.[2] Under these statutes, we consider the Transmittal an agreement allocating rent such that the taxpayer may deduct the amount of $[redacted] in each of the months [redacted] and [redacted]. However, since the Transmittal specifically allocates rent to each of the months [redacted] through [redacted] those amount may only be deducted in the [redacted] taxable year. See Piccadilly Cafeterias, Inc. v. United States, 36 Fed Cl 330 (1996)

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[2] Please note that we do not think that the provisions of §§ 467(b)(2), (b)(3), or (b)(4) apply here as we do not see [redacted] or the taxpayer engaging in a tax avoidance transaction or view the Lease as a disqualified long-term agreement. Further, please note that for a lease agreement to be classified as a disqualified long-term agreement, it is necessary to determine, considering all the facts and circumstances, that a principal purpose for providing increasing rents is the avoidance of tax. Our position is consistent with that taken by the prior agent and we understand that the present audit team agrees with his analysis of these sections.

Treas. Reg. § 1.467-1(f) pertains to a substantial modification of a rental agreement.[3] Subsubparagraph (5) of this regulation contains two relevant definitions: (a) "Modification" of a rental agreement includes any alteration, in whole or in part, of a legal right or obligation of the lessor or lessee thereunder, whether the alteration is evidenced by an express oral or written agreement, conduct of the parties, or otherwise and (b) a modification is "substantial" only if, based on all the facts and circumstances, the altered legal rights or obligations and the degree to which they are altered are economically substantial. We understand that the key question regarding modification under this regulation pertains to whether the parties changed their legal rights or obligations. It appears from the language of the Transmittal and its full payment of the increased rent that [redacted] agreed to pay higher rent and therefore did change its legal obligation for this [redacted] month period. In addition, we think it probable that the Tenant would provide credible oral evidence that it considered itself bound by the terms of the Transmittal. Accordingly, we think that the taxpayer meets the first definition of "modification." Moreover, it is possible that the changes to the rent due per the Transmittal constitute a substantial modification of the Lease because they are economically substantial under § 1.467-1(f)(5)(ii). However, we do not have any information regarding the taxpayer's financial position and therefore cannot give you an opinion on whether the increased rent rises to the level of economically substantial.[4]

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[3] No case law exists discussing the meaning of a substantial modification under the statute and we have found no other guidance on this issue.

[4] Treas. Reg. § 1.467-1(f)(6) provides a number of safe harbors such that a modification of a rental agreement is <u>not</u> a substantial modification under certain circumstances. However, unless the change in the amount of fixed rent allocated to a rental period that, when combined with all previous changes in the amount of fixed rent allocated to the rental period, exceeds one percent of the fixed rent allocated to that rental period prior to the modification, a modification falls outside the safe harbor rules of subsubparagraph (6). We conclude that the instant modification of the Annual Fixed Rent would be substantial under the cited provision. Our comparison above of the rental amounts due under the Lease and the Transmittal shows that the difference for each month listed exceeds [redacted]% and therefore this safe harbor does not apply here.

In summary, we agree with the audit team's position under the terms of § 467.

New York State Law

Although we concluded above that federal law alone allows deductibility of the subject expense, we also consider whether the Lease was not effectively modified by the Transmittal under state law. If the Lease was not so modified, then the Service could disallow a deduction claimed for any rent beyond that specified in Schedule [redacted] attached to the Lease. Four sections of New York's General Obligation Law (GOL) apply here:

1. § 5-703(2)(McKinney's 1963), known as the Statute of Frauds, provides, in relevant part, that a contract for the leasing for a longer period than one year of any real property or any interest therein is void unless the contract or some note or memorandum thereof is in writing, signed by the party to be charged or his agent authorized by writing. Since the Lease is for an interest in real property for a term longer than one year and is a writing signed by [redacted], it is subject to § 5-703.

2. § 5-701 (a)(1)(McKinney's 1978), also known as the Statute of Frauds, states that all agreements which by their terms are not to be performed within one year from the making thereof are void unless in writing and subscribed by the party to be charged therewith. Unless there has been execution and delivery of a lease meeting the one year requirement, there is no valid written agreement. Beck v. New York News, Inc., 92 A.D.2d 823 (1st Dept.), aff'd, 61 N.Y.2d 620 (1983); see also Alan Skop, Inc. v. Benjamin Moore, Inc. 909 F.2d 59, 60 (2d Cir. 1990). The Lease also satisfies this statute of frauds.

3. § 15-301 (McKinney's 1963) states that a written instrument which contains a provision to the effect that it cannot be changed orally, may only be changed by an executory agreement in writing and signed by the party against whom enforcement of the change is sought or by an agent. Since the Lease requires all modifications to be in writing, Section 37.4 is enforceable under New York law. L & B 57th Street, Inc. v. E.M. Blanchard, Inc., 143 F.3d 88, 93 (2d Cir. 1998).

4. § 5-1103 provides that an agreement, promise or undertaking to change or modify any lease shall not be invalid because of the absence of consideration, providing that the agreement, promise or undertaking changing or modifying such lease shall be in writing and signed by the party against whom it is sought to enforce the change or modification or an agent thereof.

After reviewing these statutes and case law, we base our position that the Transmittal does not equal a modification of the Lease on the following:

1. Section [redacted] of the Lease requires all modifications of the lease to be in writing and signed by both Landlord and Tenant to be effective.

We do not view the Transmittal as a writing effective to change the Lease under GOL §§ 5-703, 5-701, or 15-301. First, as noted above, since the Lease is subject to the Statutes of Frauds, modifications to it must also be in writing subscribed by the party to be bound. In Lancaster At Fresh Meadow v. Suderov, 162 N.Y.S.2d 162(S. Ct. 1957), aff'd, 5 A.D.2d 1015 (2d Dept. 1958), the Court found that modification of the contract [sale of real property] was as subject to the Statute of Frauds as was the original contract itself. Therefore, the modification, too, or some note or memorandum thereof, had to be in writing "subscribed by the party to be charged, or by his lawful agent *thereunto authorized by writing* ." (emphasis in original) See also L & B 595 Madison, Inc. v. Ravagnan, 242 A.D.2d 413 (1st Dept. 1997).

However, please note that at least one decision exists holding that documents such as the Lease in issue are not subject to the Statute of Frauds. See Weiner v. McGraw-Hill, Inc., 57 N.Y.2d 458 (1982), in which the highest New York State court held that contracts theoretically performable within a year, even if unlikely to be so performed, are not subject to GOL § 5-701. Although the Lease continues from [redacted] through [redacted], it could be terminated at any time should the Guarantor file a bankruptcy petition (Section 21.1), should the Tenant fail to pay the annual rent (Section 21.3), or should there be an act of condemnation (Article 28). Accordingly, if a court were to hold the Lease subject only to § 5-701 and not to § 5-703, modifications to the Lease would not have to be in writing. In that event, we think that the taxpayer could provide credible oral testimony that it orally agreed to modify the Lease and was required to pay extra rent.

Secondly, the Service may be able to successfully argue that the Transmittal (a document sent by facsimile to [redacted]) was not even signed by the Landlord. No signature on behalf of [redacted] appears on the copy you provided. Nor is [redacted] included in [redacted] to the Lease, List of Designated Attorneys. Therefore, a question exists as to whether [redacted] was [redacted]'s authorized agent. The highest New York state court held in Parma Tile Mosaic & Marble Co., Inc. v. Estate of Short, 87 N.Y.2d 524 (1996), that the mere act of identifying and sending a document to a particular destination does not, by itself, constitute a

signing authenticating the contents of the document for Statute of Frauds purposes. The Court construed GOL § 5-701(a) to contain two threshold requirements for proving the existence of a binding agreement, promise or undertaking: a writing, and a subscription of the writing by the party to be charged therewith. Further, since the Legislature selected these objective elements to determine, in the first instance, the existence of an enforceable agreement, promise or undertaking, the absence of a writing or a subscription cannot be remedied by arguing that obligations were nevertheless incurred. Thus, the Court rejected the plaintiff's contention that the intentional act of programming a fax machine, by itself, sufficiently demonstrates to the recipient the sender's apparent intention to authenticate every document subsequently faxed. Rather, the Court required the parties to demonstrate the intent to authenticate the particular writing at issue. Under this case, the Transmittal would have no effect on the Lease provisions unless the taxpayer and [redacted] produces further documentation or credible oral evidence on this issue.

Please note that a exception to § 5-703 exists for partial performance. See Klein v. Klein, 79 N.Y.2d 876 (1992) (narrow partial performance exception to § 5-703 for alleged oral agreement between former spouses). The seminal state case on this exception is Rose v. Spa Realty Associates, 42 N.Y.2d 338 (1977). The Court of Appeals, construing § 15-301, held that if the only proof of an alleged agreement to deviate from a written contact is the oral exchanges between the parties, the writing controls. However, if the partial performance be unequivocally referable to the oral modification, then the requirement of a writing under § 15-301 is avoided. This exception for partial performance was further discussed in Anostario v. Vicinanzo, 59 N.Y.2d 662, 663 (1983), a case involving § 5-703. The Court stated that the doctrine of part performance may be involved only if plaintiff's actions can be characterized as unequivocally referable to the agreement alleged. Moreover, it was not sufficient that the oral agreement gives significance to plaintiff's actions; rather, the actions alone must be "unintelligible or at least extraordinary", explainable only with reference to the oral agreement (cites omitted). See also L & B 57th Street, Inc. v. E.M. Blanchard, Inc., 143 F.3d at 93 (lease required all modifications to be in writing and to overcome that provision the parties had to show (under the Rose standard) that the only inference possible from their conduct is that an oral agreement had been concluded between the parties).

The exception for partial performance would not pertain here if a court did not view the Transmittal as being unequivocally referable to an oral agreement to increase the rent due for the

period [redacted] through [redacted]. As noted above, Sections [redacted] of the Lease provide for additional rent payments due to increases in certain taxes, damage to the premises, mechanic liens, etc. In addition, the Transmittal merely refers to "advance payment of rent" and lists an amount of rent due for each of the months [redacted] through [redacted] but does not separate the listed monthly rent due for each month into amounts for Office Space and Basement and Sub-Basement Space as does Schedule [redacted] to the Lease. Accordingly, it is possible that the payments made by [redacted] for the period noted could have been for such additional expenses expressly provided for in the Lease. However, please note that if the taxpayer were to substantiate any additional rent as provided for in the listed sections of the Lease, it would be entitled to an larger rent deduction under the Lease. Again, further factual development is needed, including whether [redacted] ever agreed to an oral modification of the rent schedule, whether it understood that the Transmittal pertained to rent for Office Space and Basement and Sub-Basement Space only, and whether it understood that the specified rent could be increased by additional rent as noted in the Lease.

Third, please also note that in determining whether an oral modification of a written document such as the Lease is effective, courts will consider whether it is customary to put such agreements in writing. We assume that it is customary in the real estate industry for modifications of leases to be in writing; you may wish to determine the custom of the industry in support of this point. In any event, in the absence of custom, courts will assume that a transaction of sufficient substance or complexity will usually require a writing. PA Bergner & Co. v. Martinez, 823 F. Supp. 151, 158 (S.D.N.Y. 1993). In this case, the Lease is a lengthy, detailed document providing for many contingencies. We think it likely that a court would view the alleged modification under which [redacted] agreed to pay its landlord extra rent as of sufficient substance to require a writing. See also Adler & Shaykin v. Wachner, 721 F. Supp. 472, 477 (S.D.N.Y. 1988) (whether the alleged oral agreement between the parties is the sort of complex arrangement which is customarily reduced to writing). In this regard, the Service's position would be weakened if the taxpayer presented credible oral evidence that it did not formally amend the Lease as required because of a long standing business relationship with [redacted] and because the Lease would be modified for a relatively short period.

2. The Transmittal requests comments on the scheduled rent increases.

Because of this language we do not view this document to reflect a modification to the Lease agreed to and signed by the Tenant. The request for comments indicates to us that the parties have not concluded their negotiations and have not reached a meeting of the minds, the fundamental tenet for a contract. Greystone Partnerships v. Koninklijke, 815 F. Supp. 745, 754 (S.D.N.Y. 1993)(considering provisions of § 5-701). However, the Service's position would again be vulnerable if credible evidence was produced that the parties had reached a meeting of the minds and the Transmittal did not accurately reflect that agreement due to a poor choice of words by [redacted].

Further, the Transmittal states that the [redacted] family "[redacted]" the "[redacted]" of the [redacted] family (and presumably the [redacted] of [redacted] and the taxpayer). In our opinion, the quoted language indicates that the taxpayer agreed only to assist the Landlord for a relatively short period ([redacted] months) of financial difficulty rather than agreeing to an alteration of its entire lease which extended until at least [redacted]. The legislative history of the statute provides support for this position. One of the primary purposes of § 467 was to prevent, in effect, giving an interest-free loan to taxpayers by allowing them to delay the payment of their taxes. H.R. Rep. No. 98-432, Part II, 98th Cong., 2d Sess. 1246 (1984). Disallowing the prepaid rent deduction would be consistent with Congressional intent to prevent a windfall interest-free loan to Advance. See Piccadilly Cafeterias, Inc. v. United States, supra.

3. Arguably, the conduct of the taxpayer in paying the requested increased rent per the Transmittal could be seen as an alteration evidenced by the conduct of the parties.

The taxpayer could argue that its conduct (paying the full amount of increased rent) ratified the rent increase. In Diocese of Buffalo, N.Y. v. McCarthy, 91 A.D.2d 213 (4th Dept. 1983), the Court held that an unauthorized execution of an instrument affecting the title to land or an interest therein may be ratified by the owner of the land or interest so as to be binding upon him. However, such an act of ratification required a clearly expressed assent to the transaction and might not be inferred from doubtful or equivocal acts. Should the taxpayer argue that [redacted] ratified the payment of extra rent, the Service could encounter difficulties rebutting such information. Further, payment in full probably would be considered an unequivocal act ratifying the Transmittal.

In addition, two cases have held that payment alone, even though in full, is not an act of part performance. See Rork v. Orcutt, 53 N.Y.S.2d 354, 356 (S. Ct. 1945), and Robbins v.

Kearing, 66 N.Y.S.2d 537, 540 (S. Ct. 1946)(citing Rork v. Orcutt). Therefore, we do not think that [redacted] gave effect to the Transmittal by its conduct in paying the increased rent in full. However, please note that neither case has been cited for this proposition since 1946.

4. There is no evidence that [redacted] received any consideration for its agreement to pay increased rent.

GOL § 5-1103 provides that an agreement to change or modify a lease shall not be invalid due to a lack of consideration provided that the agreement modifying such lease shall be in writing and signed by the party against whom it is sought to enforce the modification. See New York State Energy Research and Development Authority v. Nuclear Fuel Services, Inc., 714 F. Supp. 71, 74 (W.D.N.Y. 1989)(oral modification of contract for storage of nuclear fuel, to have been valid, needed the support of consideration); Colonie Construction Corporation v. DeLollo, 25 A.D.2d 464 (3d Dept. 1966)(oral modification increasing price of real property unenforceable because oral agreement did not comply with statute of frauds and lacked consideration). In addition, a federal court construing § 15-301, Merrill Lynch Interfunding, Inc. v. Argenti, on remand, 155 F.3d 113, 122 (2d Cir. 1998), found that an action does not amount to partial performance sufficient to overcome the statute where that action confers no benefit on the party against whom enforcement is sought.

We do not see any benefit to the taxpayer in agreeing to pay increased rent other than the tax benefits. Accordingly, we think the Service could prevail on this argument. However, it is possible that a court could consider the $[redacted] discount [redacted] obtained by prepaying its rent as consideration. In addition, we doubt that the taxpayer agreed to pay higher rent without any quid pro quo. Perhaps the Landlord agreed to increase the amount of space available to [redacted] or to redecorate its premises. Again, further factual development will be crucial to the Service's success on this question.

In summary, we think that the Service would successfully defend its position that the Transmittal does not equal an alteration evidenced by an express agreement, conduct of the parties, or otherwise. In that event, the taxpayer would be limited to rental deductions as specified in the Lease. But we recognize that there is case law opposed to this position and the Service faces considerable hazards in sustaining its position. Therefore, further factual development is crucial. We recommend that you attempt to determine: (1) why the parties agreed to the increased rent for the period [redacted] through [redacted] (2)

why the period of increased rent was apparently limited to that period; (3) whether the taxpayer signed any document pertaining to the increased rent for that period; (4) what consideration [redacted] received in return for its agreement to pay higher rent; (5) the financial condition of [redacted] at the time of the proposed increased; (6) the taxpayer's financial condition at the time of the proposed increase; (7) why [redacted] and [redacted] allegedly modified the Lease through the Transmittal rather than amending the Lease in writing consistent with Section [redacted] of the Lease; and (8) what amount of rent did [redacted] pay after [redacted] the amount listed in Schedule [redacted] ($[redacted]) or the increased amount per the Transmittal ($[redacted])?

Once further factual development occurs and upon your request, we will be happy to provide additional advice on this issue. Alternatively, you may wish to consider our comments on the Service's litigation hazards in reaching a resolution of this issue.

Issue 2.

Taxpayers are entitled to structure their transactions so as to obtain the maximum benefit legally obtainable. Gregory v. Helvering, 293 U.S. 465 (1935). Accordingly, we do not think the Service may disallow the claimed charitable contribution deduction simply because [redacted] could have sold the stock in issue, creating a sizable capital gain due, rather than donating it to the [redacted].

Internal Revenue Code § 170(a) generally allows as a deduction any charitable contribution (as defined in subsection (c))when verified under the pertinent regulations. We assume from the document you provided that the audit team is prepared to accept that [redacted] has properly verified its contribution and the amount of the deduction is not in contention.

However, other subsections of § 170 restrict the general rule. We do not have sufficient facts to advise you now on whether the deduction in issue may be disallowed in full or in part under § 170. So we suggest that you consider developing facts relevant to the listed Code sections with a view to challenging the claimed deduction on grounds other that the one presently proposed:

1. Section 170(c) includes in the definition of a charitable contribution a contribution or gift to or for the use of a "foundation" meeting certain requirements in § 170(c)(2). See also Treas. Reg. § 1.170A-1. Donors must demonstrate that their

donees are organizations described in § 170(c). See Jennings v. Commissioner, T.C. Memo. 2000-366. If the facts support this argument, you may wish to challenge the claimed deduction on the ground that the [redacted] does not meet these criteria.

2. Section 170(e)(5)(C) states that a donor may not contribute more than 10% of the stock of a corporation. You may wish to determine whether [redacted]'s contribution of [redacted] shares of [redacted] common capital stock exceeds the 10% maximum. If so, then the provisions of § 170(e)(5)(A) should not apply here. See Internal Revenue Code § 509(a)(2) and Treas. Reg. § 1.509(a)-5(1) for a discussion of the meaning of "private foundation."

3. Section 170(f), entitled Disallowance of Deduction in Certain Cases and Special Rules, provides that no deduction shall be allowed for a contribution to or for the use of an organization or trust described in Internal Revenue Code §§ 508(d) [Special Rules with Respect to Section 501(c)(3) Organizations, Gift or Bequest to Taxable Private Foundation] or 4948(c)(4) [Application of Taxes and Denial of Exemption with Respect to Certain Foreign Organizations] subject to the conditions specified in those sections. You may wish to develop facts allowing for a disallowance of the subject deduction under this section.

4. Please note that the legislative history of Internal Revenue Code § 1366, Pass-Thru of Items to Shareholders, provides that the corporate limitation on charitable contributions will no longer apply to Subchapter S corporations. H.R. Rep. No. 826, 97th Cong., 2d Sess. 14 (1982); S. Rep. No. 640, 97th Cong., 2d Sess., 16 (1982); Committee Report on P.L. 97-354 (Subchapter S Revision Act of 1982.) Therefore, we do not think you may disallow this deduction under § 170(b)(2).

Again, upon your request and further factual development, we will be able to provide additional advice on this issue.

This opinion is based upon the facts set forth herein. It might change if the facts are determined to be different. If the facts change, this opinion should not be relied upon. Please note that under routing procedures which have been established for opinions of this type, we have referred this memorandum to the Office of Chief Counsel for review. That review might result in modifications to the conclusions herein. We will inform you of the result of the review as soon as we hear from that office, which should be in approximately 10 days. In the meantime, the conclusions reached in this memorandum should be considered to be only preliminary.

DISCLOSURE STATEMENT

This writing may contain privileged information. Any unauthorized disclosure of this writing may have an adverse affect on privileges, such as the attorney client privilege. If disclosure becomes necessary, please contact this office for our views.

JODY TANCER
Associate Area Counsel
(Large and Mid-Size Business)

By: Diane R. Mirabito
DIANE R. MIRABITO
Attorney
(Large and Mid-Size Business)