

M E M O R A N D U M

December 3, 1982

TO: REVIEW ATTORNEYS
FROM: DIANA J. LEE *djl*
Re: Undisclosed Sponsors

Reviewers should be scrutinizing any offering plan in which the owner of the property is not designated as a sponsor. Your examination is to determine whether the owner is also a party who makes or takes part in the offering. Under Section 18.1(c), sponsor is defined as:

"... any person, partnership, joint venture, corporation, company, trust, association or other entity who makes or takes part in a public offering or sale in or from the State of New York of securities..."

The key document in this examination is the agreement between the owner and the disclosed sponsor. In some instances, this document is a contract of sale conferring on the disclosed sponsor the status of contract vendee. The fact that sponsor is a contract vendee should not end the examination. It is possible that the owner should also be deemed a sponsor if the contract of sale is conditional on the conversion to cooperative or condominium ownership or, if the contract vendee nets little of the proceeds of the sale compared to the owner of the property.

Factors to be considered in making this determination are:

1. Are there individuals or entities who are principals of both the owner and the disclosed sponsor? If yes, there is a greater possibility that the disclosed sponsor is acting as an agent or front for the owner.

2. Is there any risk to the disclosed sponsor? For example, does the disclosed sponsor have to consummate the purchase of the property if the coop plan is not effectuated. If there is no risk to the disclosed sponsor, this is another indicia that he may be acting as an agent or front for the owner.
3. Does the owner have any control over the terms of the offering? For example, must he approve the terms of the offering plan? If so, this is some indication that the owner is making or taking part in the offering.
4. How are the profits of the offering to be divided? The smaller the share for the disclosed sponsor, the greater the possibility that the disclosed sponsor is really only acting as a broker or selling agent for or co-venturer with the owner.

Assume you have reached the conclusion that the owner should also be designated as one of the sponsors. The plan should be revised accordingly. This position will obviously be resisted by tax counsel for the owner since the sponsor has been interposed in an attempt to obtain capital gains treatment for the owner. The only exception is if the sponsor submits a written exemption request pursuant to Section 18.1(1) wherein the owner agrees to conditions subjecting the owner to liability under the Martin Act as a promoter and provides substantial parties other than the disclosed sponsor to back up all obligations of the sponsor under the offering plan. Such conditions may include but are not limited to:

1. Certain of the principals of owner signing the certifications. Principals of the owner who are not certifying must provide an affidavit that they are only passive investors.
2. Certain of the principals of owner personally guaranteeing all obligations of sponsor.
3. A statement in the offering plan that the owner is a promoter within the meaning of §352-e.
4. Full disclosure of the identity of the owners in the offering plan.

Please note that in any plan in which the owner is not one of the sponsors, regardless of whether or not your finding is that the owner is a sponsor, you must obtain a backup letter from the owner indicating agreement with all statements in the offering plan on the building condition, status of tenants and financial information.