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New York's Mortgage Tax Rules Burden Banks and Borrowers. But, There's a Solution.

*Michael J. Heller**

In this article, the author proposes a change to New York's mortgage recording tax to help simplify the process for demonstrating when no tax is payable.

Section 253 of the New York State Tax Law imposes substantial mortgage recording taxes on new mortgages secured by real property that are recorded in the state. Moreover, the law also provides for various local governments within the state, including New York City and some counties, to impose their own taxes on mortgages recorded in their jurisdictions.

The amount of the mortgage tax varies depending on, among other things, the amount of the mortgage, but it typically is significant.

For example, the tax rate for a commercial mortgage on a New York City property that is less than \$500,000 is \$2.05 for each \$100 of principal. Therefore, the tax to record a \$499,000 mortgage would be in excess of \$10,200.

Suppose, however, that the mortgage is \$500,000. The tax to record that mortgage is equal to \$2.80 for each \$100 of principal. Accordingly, the recording tax for a \$500,000 mortgage would be \$14,000.

In many instances, New York borrowers are involved in transactions in which they acquire a property burdened by an existing mortgage. In these cases, it might be possible to lower—or even eliminate—the mortgage recording tax by having the existing lender assign its mortgage to the purchaser's lender. That's because New York allows a party, when a mortgage is assigned or assumed, to take a credit on the mortgage tax payable for the unpaid principal balance of the existing mortgage.

Consider, for example, that a New York City property has a remaining mortgage balance of \$4 million and the borrower needs to finance a total of \$7 million to purchase the property.

The mortgage recording tax on a \$7 million mortgage would be \$196,000. If the borrower, however, could have the existing mortgage assigned to its new

* Michael J. Heller, a member of the Banking, Corporate, and Real Estate Practice Groups at Rivkin Radler LLP and a member of the Board of Editors of *The Banking Law Journal*, works extensively with bank clients on complex commercial loans, including Industrial Development Agency and Small Business Administration matters, and with private clients in real estate development and corporate transactions. He may be reached at michael.heller@rivkin.com.

lender and take credit for the mortgage tax previously paid on the unpaid principal balance of \$4 million, then the borrower would only have to pay mortgage tax on \$3 million. Thus, the borrower would pay a recording tax of only \$84,000—a savings of \$112,000.

Unfortunately, though, New York currently requires that borrowers and lenders jump through way too many hoops to avoid paying a mortgage recording tax in this kind of situation.

EXISTING LAW

Under existing New York law and practice, a borrower needs a physical assignment of the existing mortgage and the new lender's consolidation, extension, and modification agreement to be able to file an affidavit under New York Tax Law § 255¹ with the appropriate county clerk to demonstrate that the existing mortgage has been assigned to a new lender, thereby reducing (and potentially eliminating) the need for the borrower to pay mortgage recording tax.

The affidavit, typically referred to as a "255 Affidavit," sets forth the unpaid principal balance of the existing mortgage loan, the tax paid on any new funds,

¹ New York Tax Law § 255 provides:

1. (a)(i) If subsequent to the recording of a mortgage on which all taxes, if any, accrued under this article have been paid, a supplemental instrument or mortgage is recorded for the purpose of correcting or perfecting any recorded mortgage, or pursuant to some provision or covenant therein, or an additional mortgage is recorded imposing the lien thereof upon property not originally covered by or not described in such recorded primary mortgage for the purpose of securing the principal indebtedness which is or under any contingency may be secured by such recorded primary mortgage, such additional instrument or mortgage shall not be subject to taxation under this article, except as otherwise provided in paragraph (b) of this subdivision, unless it creates or secures a new or further indebtedness or obligation other than the principal indebtedness or obligation secured by or which under any contingency may be secured by the recorded primary mortgage, in which case, a tax is imposed as provided by section two hundred and fifty-three of this article on such new or further indebtedness or obligation. . . .

2. (a) If, at the time of recording such instrument or additional mortgage, any exemption is claimed under this section, there shall be filed with the recording officer and preserved in his office a statement under oath of the facts on which such claim for exemption is based. The determination of the recording officer upon the question of exemption shall be reviewable by the tax commission.

(b) If an exemption is claimed under this section, at any time after such instrument or additional mortgage is recorded and tax paid, there shall be filed with the tax commission, as part of the application for refund a statement under oath of the facts on which such claim for exemption is based. A copy of the order of refund of the tax commission shall likewise be filed with the recording officer and preserved in his office.

and the total amount of additional funding being advanced by the new lender. To take advantage of this section of the tax law and the accompanying regulations, however, a borrower actually must obtain an assignment of the existing mortgage loan from the existing mortgage lender.

As a practical matter, the steps necessary for the assignment are time consuming. They also add to a transaction's closing costs and generate excessive paperwork. The process requires that all notes be located and that copies of all previously recorded mortgages be obtained. Moreover, even in the best of circumstances, there is a risk that the chain of title can become clouded or confused.

Fortunately, there is a rather straightforward solution that, if adopted by the New York State Legislature, would ease the burdens on borrowers and lenders—and it would do so without affecting the total amount of funds payable to state and local governments.

THE SOLUTION

The way to streamline matters involves amending Tax Law Section 255 and its accompanying regulations to permit a borrower to take advantage of its provisions merely by filing a 255 Affidavit—without the need for the borrower to actually obtain an assignment of the existing mortgage—together with the recording of the transaction.

The borrower could support the 255 Affidavit with a payoff statement from the existing lender, which is provided as a matter of course in refinancings. The payoff statement would establish the outstanding principal balance of the existing mortgage. It then would be a straightforward matter to determine the amount of any new mortgage financing that would be subject to the mortgage recording tax.

THE BENEFITS

There are many practical benefits of this solution. A refinanced mortgage would be evidenced only by a new note and mortgage, clearly indicating the debtor or debtors and the lender, as well as the principal amount of the new loan secured by the mortgage. This may also reduce title claims and corresponding litigation.

In addition, simplifying the process of meeting Section 255's requirements would naturally expedite closings and eliminate the need for an existing lender to locate and provide original documents, to the benefit of both borrowers and lenders.

Transactions also would be clearer to the parties themselves, as well as to the general public.

And, to avoid any reduction in fees payable to county clerks, borrowers could be charged the same fee for filing a 255 Affidavit as currently is charged for the recording of an assignment of mortgage and the consolidation, extension, and modification agreement.

CONCLUSION

New York law clearly provides that there is no recording tax payable on an assignment of a mortgage. Current practice, however, makes taking advantage of that rule burdensome. The change in law suggested in this article would help eliminate a variety of costs and streamline real estate transactions in the state. Will the legislature act? Stay tuned.