CROSS-BORDER FINANCE ALERT

What Cross-Border Practitioners Need to Know about New York Mortgage Tax

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The quirks inherent in New York State's mortgage recording statutes often cause out-of-state practitioners some frustration, especially if they practice in a jurisdiction that does not have a mortgage recording tax. If your cross-border deal includes real estate collateral, then you should be aware of the below New York mortgage tax basics and peculiarities.

1. The Basics

New York imposes a substantial mortgage tax on all mortgages recorded in the State. The tax is generally paid by the mortgagor, and the rate differs by County, type of mortgage (i.e. residential vs. commercial), and mortgage principal amount. The most common rate for a commercial mortgage is 1% of the principal amount, but it can also range to as high as 2.8% of principal for certain transactions in New York City. From a practical perspective, if you don't pay the tax you will not be able to record your mortgage. From a legal perspective, failure to pay the tax is a bar against enforcement, assignment, and discharge of the mortgage. The desire to save on the mortgage tax encourages the consolidation of existing mortgages rather than a discharge when a loan is refinanced, and contributes to substantial complexity in structuring and formality of otherwise straightforward mortgage lending transactions.

2. Mortgage Recording Tax – You Need to Cap the Principal Amount Secured

In New York you need to set the maximum amount of principal secured by the New York property within the mortgage. This will establish the mortgage tax liability. 'Last dollar' language should also be included in the mortgage. A typical last dollar clause states that so long as the aggregate amount of the secured obligations exceed the maximum secured amount under the mortgage, any payments of the secured obligations shall not reduce the maximum secured amount. In addition to the maximum principal amount secured, the mortgage may also secure interest payable on the indebtedness secured by the mortgage, and incidental amounts such as expenses incurred by the lender to preserve the value of the mortgage. No mortgage tax is paid to secure these items. Breakage costs associated with an interest rate swap agreement may also be included as incidental amounts if certain conditions are satisfied.

3. Mortgage Recording Tax – The Existing Mortgage Has Value

In New York, particularly in the context of a refinance, it is a benefit to the borrower for the existing mortgage to be assigned to the new lender. The assignment of an existing mortgage to the new lender allows the borrower to avoid paying mortgage tax on the existing amount of principal secured by the assigned mortgage, which is typically then consolidated with the new money portion of the refinance to form a new lien in the consolidated amount. The documentation necessary to assign, modify and consolidate a mortgage is formulaic and cumbersome, but will serve to save the borrower money. On a large transaction, the savings can be considerable. It is also important to negotiate with the lender a clause in any new mortgage pursuant to which the lender commits to an assignment of the existing mortgage to a new lender. This way, the borrower is ensured the ability to take advantage of mortgage tax previously paid upon its refinance.

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4. Beware of Revolving Credit Mortgages

As you might imagine, the mortgage tax creates some issues when parties want to use New York real property to secure revolving debt. For certain commercial loans of up to $3,000,000, New York has a statutory "credit line mortgage" that allows, provided mortgage tax has been initially paid on the maximum secured amount, advances and re-advances without triggering additional mortgage tax liability. Because of the small cap and certain other limitations, the "credit line mortgage" is rarely utilized on cross-border deals. Unfortunately, outside of the "credit line mortgage" context, New York generally considers a revolving debt re-advance to be a disbursement of new money requiring a modification to the underlying mortgage and payment of additional mortgage tax. This can significantly increase the cost and risk of securing revolving debt with a New York mortgage. In certain circumstances there are ways to structure a revolving credit transaction to minimize New York mortgage tax concerns. So if you have a transaction that includes revolving credit and New York real property as collateral, it is important to reach out to New York counsel early in the process to determine whether the proposed collateral structure works and to explore potential alternatives.

Aside from the above, there are myriad other issues that may be encountered in the context of New York mortgage lending and mortgage tax, some of which will be covered in future installments. Overall, the peculiarities of the New York mortgage tax rules can be overcome and your deal can likely get done, but it is important to engage New York counsel in the structuring phase of the process.

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