

New York State Legislature Considers Extending Mortgage Recording Tax to Mezzanine Debt and Preferred Equity

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A New York State bill that seeks to charge a recording tax on mezzanine debt financings has been revised to extend the recording tax to preferred equity investments.

In January 2020, Senator Julia Salazar and Assembly Member Harvey Epstein introduced a bill (S7231/A9041) in the New York State Legislature proposing to charge a recording tax (similar to the mortgage tax) on mezzanine debt financings to help fund public housing. In August, the legislation was amended to extend the application of the mortgage recording tax to preferred equity investments.

Under the revised bill: (1) a financing statement evidencing any mezzanine debt or preferred equity investments related to real property would need to be filed concurrently with any related mortgage instrument, and (2) a recording tax would be imposed on such debt and/or investments at the time that the financing statement is filed at the applicable New York State mortgage recording tax rate (for commercial mortgages over \$500,000, the current rate for properties within New York City is 2.80%; for most counties outside of NYC, the rate is about 1%). The bill would not extend recording requirements or recording taxes to debt on cooperative or common shares of a residential dwelling.

While the proposed bill does not require the recording of mezzanine debt or preferred equity investments if no mortgage recording is also taking place, the failure to file the financing statement and pay the recording tax may prevent the makers of mezzanine loans from enforcing remedies under Article 9 of the UCC. The failure to pay applicable recording taxes would also prohibit subsequent mortgage recordings, including assignments of mortgage.

If enacted, the revised legislation is likely to have a significant impact on real estate financing and the structuring of real estate transactions in New York. Mezzanine loan and preferred equity investments would be treated more like mortgage loans and therefore the overall cost of such financings and investments would become more burdensome for borrowers and other transaction parties. The proposed bill would also subject such transactions to increased visibility by virtue of the financing statement being recorded against the real property.

As the bill remains in committee stage, there are a number of questions and uncertainties which will need to be addressed for any changes to become operational (for example, the bill fails to narrowly and precisely define mezzanine debt and preferred equity investments, and treats preferred equity as secured debt). We anticipate that interested parties will press on these items with the legislature in the coming weeks and months, and more clarity may be forthcoming with respect to any final resolutions. We will continue to monitor the progress of this bill and any changes to it, and will provide further updates.

If you have questions relating to a specific loan, please contact Timothy E. Davis (davist@whiteandwilliams.com; 215.864.6829) or another member of our Real Estate and Finance Group.

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