

Regulations on Continuing Lien Exclusion From Consideration

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THE CITY OF NEW YORK
DEPARTMENT OF FINANCE

NOTICE OF RULEMAKING

Pursuant to the power vested in me as Commissioner of Finance by sections 389(b) and 1043 of the New York City Charter and section 11-2112(1) of the Administrative Code of the City of New York, I hereby promulgate the within amendments to the Rules Relating to the Real Property Transfer Tax.

/s/Andrew S. Eristoff
Commissioner of Finance

Section 1, Section 23-03 of Title 19 of the Rules of the City of New York relating to the Real Property Transfer Tax is amended to add a new subdivision (k) to read as follows:

(k) Excludible liens. (1) In the case of a deed, instrument or transaction conveying or transferring on or after August 28, 1997, a one, two, or three family house, an individual residential condominium unit, or an individual residential cooperative apartment, or an economic interest in any such property, the consideration for the conveyance or transfer shall not include the amount of any excludible lien on the property conveyed or interest transferred, as defined in paragraph (3) below, to the extent otherwise included in the consideration for the conveyance or transfer.

(2) Paragraph (1) shall not apply to a conveyance or transfer;

(i) to a mortgagee, lienor, or encumbrancer, whether or not (A) the grantor or transferor is or was liable for the indebtedness secured by the mortgage lien or encumbrance or (B) the mortgage, lien, or encumbrance is canceled of record; or

(ii) that qualifies as a “real estate investment trust transfer” as defined in subdivision E of Section 11-2102 of the New York City Administrative Code.

(3) For purposes of this subdivision (k), the term “excludible lien” means a mortgage, lien, or other encumbrance that was placed on the real property or economic interest before the delivery of the deed or the transfer and remains thereon after the date of the delivery of the deed or the transfer, unless any of the following applies:



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(i) The mortgage, lien, or other encumbrance was originally placed on the real property or interest therein in connection with, or in anticipation of, the conveyance or transfer, or was increased in amount in connection with, or anticipation of, the conveyance or transfer, to the extent of that increase in amount. A mortgage, lien, or other encumbrance will be considered to have been originally placed on the property, or increased in amount, in connection with or in anticipation of the conveyance or transfer if: (A) the documents relating to the mortgage, lien, encumbrance, the underlying indebtedness, or the conveyance or transfer indicate that the mortgage, lien, encumbrance or underlying indebtedness is part of a plan to eventually transfer or convey the property or interest therein, or (B) in the case of a mortgage lien or other encumbrance placed on the property within six months prior to the conveyance or transfer, if all of the relevant facts and circumstances indicate that the mortgage, lien, or other encumbrance has been placed on the property in connection with, or in anticipation of, the conveyance or transfer.

(ii) The mortgage, lien, or other encumbrance was placed on the real property or interest therein by reason of deferred payments of the purchase price whether represented by notes or otherwise.

(iii) The mortgage, lien, or other encumbrance is discharged, canceled, or reduced in amount, to the extent of the reduction in amount, in connection with the conveyance or transfer following delivery of the deed or transfer. A mortgage, lien, or other encumbrance will be considered to be discharged, canceled, or reduced in amount in connection with the conveyance or transfer if: (A) the documents relating to the mortgage, lien, encumbrance, the underlying indebtedness or the conveyance or transfer indicated that the discharge, cancellation, or reduction in amount is in connection with the conveyance or transfer, or (B) in the case of a discharge, cancellation, or reduction in amount within three months following delivery of the deed or the transfer, all of the relevant facts and circumstances indicate that the discharge, cancellation, or reduction in amount is in connection with the conveyance or transfer.

(iv) The terms of the mortgage, lien, or other encumbrance are materially altered in connection with, or in anticipation of, the conveyance or transfer.

(A) For purposes of this subparagraph (iv), the terms of a mortgage, lien, or other encumbrance on the property or interest therein will be considered to be materially altered in connection with, or in anticipation of, the conveyance or transfer if within six months prior to, or within three months following, the conveyance or transfer (a) the identity of the mortgagee or holder of the lien or encumbrance has changed, and (b) there has been a change of ten percent or more in the interest rate, or repayment term remaining as of the date of the alteration with respect to the mortgage, lien, or other encumbrance, and the facts and circumstances indicate that the alteration is in connection with, or in anticipation of, the conveyance or transfer.

(B) For purposes of this subparagraph (iv), any alteration in the terms of a mortgage, lien, or other encumbrance more than six months prior to or more than three months following the delivery of the deed or the transfer will be conclusively presumed not to be in connection with, or in anticipation of, the conveyance or transfer.



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(C) This subparagraph (iv) will not apply to a conveyance or transfer from one spouse to the other pursuant to the terms of a separation agreement or divorce decree or to a conveyance or transfer that would qualify as a bona fide gift under section 2303(j) (1) of these rules but for the presence of a mortgage, lien, or other encumbrance that qualifies as an “excludible lien” without regard to this subparagraph (iv).

(D) Increases and decreases in the amount of a mortgage, lien, or other encumbrance will not be considered material alterations. Subparagraphs (i) and (iii) of this paragraph (3) apply to increases and decreases, respectively, in the amount of any mortgage, lien, or other encumbrance.

(4) This subdivision (k) will apply to any portion of any unpaid principal of any mortgage on real property of a cooperative housing corporation that otherwise would be included in consideration in the case of an original transfer of shares in the corporation by the cooperative corporation or cooperative plan sponsor under sec. 11-2102.b(2)(i) of the New York City Administrative Code.

(5) The taxpayer shall bear the burden of proving that a lien or encumbrance qualifies as an excludible lien under paragraph (3) of these rules, and shall bear the burden of proving the amount of such lien or encumbrance at the time of the transfer or other conveyance. Sec. 11-2103 of the New York City Administrative Code.

(6) To illustrate:

Illustration (i): individual A owns a one-family house subject to a mortgage held by Bank X that is due and payable upon the sale of the house. The mortgage loan has a remaining principal balance of \$250,000, bears interest at seven percent and has a remaining repayment term of ten years. A sells the house to individual B for \$350,000. B pays \$100,000 in cash and obtains a mortgage loan from Bank Y for \$250,000. At the closing, Bank X assigns the mortgage on the property to Bank Y. The interest rate on the mortgage loan from Bank Y is nine percent and the repayment term is ten years. The terms of the mortgage on the property after the conveyance have been materially altered from the terms on the mortgage on the property before the conveyance: the mortgagee is different and the increase in the interest rate, from seven percent to nine percent, represents a greater than ten percent change. Based on the facts and circumstances, the material alteration of the mortgage is considered to be in connection with the transfer and the mortgage is not an excludible lien under section 2303 (k) (3) (iv) of these rules. The taxable consideration for the conveyance is \$350,000.

Illustration (ii): The facts are the same as illustration (i) except that the interest on the mortgage loan remains at seven percent after the assignment but the term is increased from ten to 15 years. The mortgage is not an excludible lien because the increase in the repayment term is greater than ten percent. If the interest rate and repayment term remain unchanged, or those changes are less than ten percent, the terms will not be considered to be materially altered and the mortgage will be an excludible lien.

Illustration (iii): The facts are the same as in illustration (i) except that individual A is the father of individual B and gives the house to B as a gift. B does not make a cash payment and refinances the



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mortgage loan with Bank Y. The mortgage is assigned as in illustration (i). The conveyance is a bona fide gift under section 23-03(j) (1) of these rules but for the presence of the mortgage. None of the exceptions in subparagraphs (i), (ii) and (iii) of paragraph (3) of this subdivision (k) applies to the mortgage. Subparagraph (iv) of Paragraph (3) of this subdivision does not apply to bona fide gift transfers. Therefore the mortgage is an excludible lien and there is no taxable consideration for the conveyance.

Illustration (iv): The facts are the same as illustration (i) except that the deed is delivered in January of 1998 and B acquires the house subject to the existing mortgage. B refinances the Bank X loan with Bank Y in June, 1998 and the assignment of the mortgage takes place at that time. Under subparagraph (iv) (B) of paragraph (3) of this subdivision, any alterations in the terms of the mortgage more than three months following the conveyance are conclusively presumed net to be in connection with, or anticipation, of the conveyance. Thus, the mortgage is an excludible lien regardless of alterations to its terms. The taxable consideration for the conveyance is \$100,000.

Illustration (v) Individual A is the sole owner of a cooperative apartment valued at \$400,000 and subject to a cooperative loan secured by the stock and proprietary lease and held by Bank X. The loan has a remaining principal balance of \$250,000, bears interest at seven percent and has a remaining repayment term of ten years. Pursuant to a divorce decree, A transfers the apartment to his spouse, B. Two months after the transfer of the apartment, B refinances the loan with Bank Y with no change in the principal amount. The cooperative loan from Bank Y bears interest at seven percent and has a repayment term of 30 years. Subparagraph (iv) of paragraph (3) of this subdivision does not apply to transfers between spouses pursuant to a divorce decree. Therefore, the lien securing the loan is an excludible lien. The taxable consideration for the transfer is \$150,000, the excess of the value of the apartment over the amount of the excludible lien.

Illustration (vi): The facts are the same as in illustration (v) except that A refinances the loan two months prior to the transfer but after the issuance of the divorce decree and A borrows an additional \$50,000. Subparagraph (iv) of paragraph (3) of this subdivision does not apply to increases or decreases in the amount of any mortgage, lien, or other encumbrance. Because the facts and circumstances indicate that increase of \$50,000 in the amount of the loan is in connection with or in anticipation of the transfer, \$50,000 of the amount of the lien securing the loan is not an excludible lien.

Illustration (vii): XYZ Corporation purchases a one-family house in poor condition in 1998 for \$50,000 intending to renovate the house and offer it for sale. To pay for the renovation expenses, XYZ obtains a loan of \$300,000 secured by a mortgage on the house. The mortgage loan agreement permits any buyer to assume the mortgage and requires XYZ Corporation to use its best efforts to sell the house following its renovation. In 2002, XYZ Corporation sells the house for \$500,000 to B, and B assumes the mortgage loan obligation at the same interest rate and for the same repayment term. Because the documents relating to the conveyance indicate that the mortgage is placed on the property as part of a plan to eventually transfer the property, the mortgage is considered to have been placed on the property in anticipation of the conveyance and is not excludible from consideration as an excludible lien. The taxable consideration for the conveyance is \$500,000.



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Illustration (viii): Individual A owns a one-family house subject to a \$300,000 mortgage held by Bank X. The mortgage loan bears interest at seven percent with a remaining term of 15 years. A agrees to sell the house to individual B for \$400,000. A's contract of sale with B provides for a cash payment at closing of \$100,000 and installment payments over 15 years totalling \$300,000 plus seven percent interest secured by a mortgage on the property. A repays Bank X in full and the mortgage held by Bank X is removed from the property and A records a new mortgage on the property. The \$300,000 mortgage held by A is not excludible from taxable consideration as an excludible lien because it did not exist on the property prior to the conveyance.

Illustration (ix) : Individuals A and B own a three-family house as tenants in common subject to a \$300,000 mortgage held by Bank X. The mortgage loan bears interest at 13 percent. In January, 1998 A sells his interest in the house to B for a cash payment of \$125,000 and subject to the existing mortgage. A and B also agree that B will have the mortgage discharged by June, 1998. In June, 1998 B pays Bank X the remaining amount due on the mortgage loan and the mortgage is discharged. Because the documents relating to the conveyance indicate that the discharge of the mortgage is part of a plan to convey the property, under subparagraph (iii) of paragraph (3) of this subdivision, the mortgage is considered to have been discharged in connection with the conveyance and is not excludible from consideration as an excludible lien. The taxable consideration for the conveyance is \$275,000.

Illustration (x) The facts are the same as in illustration (ix) except that A and B have no agreement regarding the discharge of the mortgage. Five months following the sale, B inherits \$1,000,000 and B decides to repay the balance due on the mortgage loan. Under the facts and circumstances, the mortgage is not considered to have been discharged in connection with the conveyance and, therefore, is considered to be an excludible lien.

Illustration (xi) : Individual A owns a one-family house subject to a mortgage held by Bank X. The mortgage loan has a principal amount of \$300,000 and bears interest at seven percent with a remaining term of 20 years. A sells the house to B for \$500,000. Bank X agrees to let B assume the \$300,000 mortgage on the house with no changes to the repayment term or interest rate. Bank X also agrees to lend an additional \$100,000 for the same 20 year term and at the same seven percent interest rate. Bank X increases the amount secured by its mortgage to \$400,000. The total consideration for the sale is \$500,000. The original \$300,000 mortgage is excluded from the taxable consideration as an excludible lien. The additional \$100,000 mortgage is not excludible from taxable consideration as an excludible lien because it did not exist on the property prior to the transfer. The taxable consideration for the conveyance is \$200,000.

Illustration (xii): The facts are the same as in illustration (xi) except that Bank X does not lend B additional funds. Instead, five months prior to the sale, Bank X agrees to lend A an additional \$100,000. A uses the funds to make improvements to the house that make it more marketable and the house is listed for sale immediately following completion of the improvements. The facts and circumstances indicate that the additional mortgage was placed on the property in anticipation of



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the sale. Therefore, the taxable consideration is \$200,000 consisting of the \$500,000 purchase price less all but \$100,000 of the mortgage.

Illustration (xiii): XYZ acquires a residential apartment building in 1998 for \$2 million cash. In 2002, XYZ obtains a mortgage loan from Bank A for \$1,750,000 to renovate the apartments pending a conversion of the building to cooperative ownership. The terms of the \$1,750,000 loan agreement require XYZ to use its best efforts to file an offering plan by the end of 2003. XYZ transfers the building to a cooperative housing corporation, C, and the offering plan becomes effective December 1, 2003. On January 15, 2004, pursuant to the offering, XYZ sells the stock and proprietary lease representing an apartment in the building for \$120,000. The proportionate amount of the \$1,750,000 mortgage on the building attributable to that apartment is \$70,000. The \$70,000 is not excludible from the consideration for the apartment because the documents relating to the loan indicate that the loan was placed on the property in anticipation of the conversion of the building to cooperative ownership and the sale of apartments.

BASIS AND PURPOSE OF AMENDMENTS

These amendments affect the portion of the Rules relating to the New York City Real Property Transfer Tax governing the exclusion from taxable consideration of certain excludible liens on the property or economic interest therein. Chapter 314 of the Laws of 1997 amended the enabling law and corresponding section of the New York City Administrative Code to exclude from consideration subject to the tax the amount of any mortgage, lien or other encumbrance existing on the property prior to the transfer and remaining thereon after the transfer. The exclusion only applies to transfers on or after August 28, 1997 of a one, two or three family house, individual residential cooperative apartment on individual residential condominium unit or an economic interest in such property. The exclusion does not apply to mortgages, liens or encumbrances placed on the property in connection with or in anticipation of the transfer or by reason of deferred payments of the purchase price. These amendments are intended to provide guidance to taxpayers as to when a mortgage, lien or other encumbrance will be considered to be placed on the property in connection with or in anticipation of the transfer and when a mortgage, lien or other encumbrance on the property following the date of delivery of the deed or transfer will be considered to be the same as the mortgage, lien or other encumbrance that was on the property prior to the transfer or conveyance. These amendments reflect court decisions under the comparable provisions of the rules that applied to transfers prior to February 1, 1982. See § 23-02, "Net Consideration".

/s/ Andrew S. Eristoff
Commissioner of Finance

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