STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
EAST 54TH STREET ASSOCIATES	:	DETERMINATION
for Redetermination or for Refund of Mortgage Recording Tax under Article 11 of the Tax Law with Reference to a Mortgage Recorded on April 24, 1987.	:	

Petitioner, East 54th Street Associates, c/o Bernard Freidman, 5 East 86th Street, New York, New York 10028, filed a petition for redetermination or for refund of mortgage recording tax under Article 11 of the Tax Law with reference to a mortgage recorded on April 24, 1987 (File No. 805197).

A hearing was commenced before Nigel G. Wright, Administrative Law Judge, at the offices of the Division of Tax Appeals, Two World Trade Center, New York, New York, on October 17, 1988 at 4:00 P.M. and continued to conclusion on December 1, 1988 at 10:15 A.M., with all briefs to be submitted by April 5, 1989. Petitioner appeared by Dreyer and Traub (Eugene Mittelman, Esq., and John S. Sinadinos, Esq., of counsel). The City of New York appeared by Peter L. Zimroth, Esq. (Glen Newman, Esq., of counsel) on October 17 and (Anshel David, Esq., and Frances Henn, Esq., of counsel) on December 10. The Division of Taxation appeared by William F. Collins, Esq. (Herbert Kamrass, Esq., of counsel).

ISSUES

I. Whether a mortgage which is indefinite in amount is to be taxed based on a sworn statement of the maximum amount actually due on the date of recordation or, alternatively, on the fair market value of the property, or whether the tax should be based on the highest fair market value of the property securing the lien at any time between its execution and recordation.

II. Whether, in the instant case, there has been an honest misconception as to the nature of the instrument or its taxability so as to qualify petitioner to pay a reduced tax based on a sworn statement of the maximum amount secured filed nunc pro tunc.

FINDINGS OF FACT

Prior to March 1985, petitioner, East 54th Street Associates ("Associates"), had eight notes outstanding to Dollar Dry Dock Savings Bank of New York ("Dollar Dry Dock") totaling $1,407,507.23. These notes weresecured by various mortgages on property located at 320 East 54th Street, New York City.

On March 8, 1985, Associates secured from Dollar Dry Dock a loan of $6,992,492.57 and signed a note to that effect. The loan was for the purchase of the East 54th Street property (for approximately $6,375,000.00) and for the development of that property into condominiums.

The term of the loan was for three years becoming due on March 8, 1988. All sums payable under the notes were payable out of the property at 320 East 54th Street and not otherwise from Associates.

(a) The loan was secured by a mortgage on the premises of 320 East 54th Street which had consolidated with it the mortgages securing the eight prior notes. This consolidated mortgage secured the total amount of $8,400,000.00 and constituted a single lien.

(b) The consolidated mortgage included the following terms:

(1) Associates had the right to prepay the entire balance of the mortgage indebtedness.

(2) The consolidated mortgage secured only the notes and mortgages specified and "no further or other indebtedness or obligation".

(3) The lien on the mortgage would automatically attach, without further act, to all after acquired property connected with the mortgaged property.

(4) The note and the lien would be increased by the amounts of any taxes, insurance payments, or other payments including the costs of any default that the mortgagee (Dollar Dry Dock) had to make on behalf of the mortgagor (Associates).

(5) The mortgage was also given as security "for any and all other sums, indebtedness, obligations and liabilities of any and every kind now or hereafter during the term hereof owing and to become due from Mortgagor [Associates] to Mortgagee [Dollar Dry Dock]". This is generally known as a "dragnet clause."

(6) No mortgage other than the mortgage in issue and one other intended to be recorded simultaneously would be placed against the premises without the prior written consent of the mortgagee which would not be unreasonably denied.

The note of $6,992,492.57 was partially paid off by Associates by the application to the note of a portion of the proceeds of the sale of each condominium unit. The eight notes totaling $1,407,507.23 were not paid off.

The consolidated mortgage was not recorded when it was first executed on March 8, 1985, but instead was recorded over two years later on April 24, 1987.

On April 24, 1987, the principal due on the consolidated mortgage had been reduced to $4,724,100.00. This consisted of $1,407,507.23 due under the eight earlier notes and $3,331,607.13 remaining due under the March 8, 1985 note.

A mortgage recording tax was paid by Dollar Dry Dock on April 24, 1987, in the amount of $157,331.25, computed on a mortgage amount of $6,992,492.57, the original principal amount advanced on March 8, 1985. Petitioner subsequently reimbursed Dollar Dry Dock for that payment.

The value of the property asserted by the Division is based on the prices of the condominium units at the time the mortgage was executed, which amounts to $11,589,661.00. Petitioner argues that the value of the property should be based on the value as of the date of recording the mortgage, April 24, 1987, or $4,800,000.00.

(a) Petitioner requested a refund on July 21, 1987 on the basis that the taxable amount

of the mortgage should be the amount owing on the date it was recorded, $3,331,607.43; the tax on such amount would be $74,961.17. Since $157,331.25 had been paid, the request was for the difference of $82,320.04.

(b) This refund request was denied by a letter of John Merrithew, Tax Auditor, on August 11, 1987. The denial was based on the ground that the mortgage "secures an indeterminate amount in addition to the stated amount of $8,400,000.00" and the tax should be based on "the greater of $8,400,000.00 or the fair market value of the real property".

An additional tax was asserted on August 11, 1987 (at the same time as the denial of the refund claim) on the basis that the mortgage was "indeterminate" under Tax Law § 256 because of the existence of the dragnet clause. The recording officer was instructed to note upon the recorded mortgage that tax remained due and that the provisions of Tax Law § 258 concerning the effect of nonpayment of tax would apply to such mortgage until the matter was resolved.

On September 14, 1987, petitioner requested that the Commissioner of Taxation issue an order permitting the recording officer to file a "maximum amount statement" nunc pro tunc as of April 24, 1987, the date of the recording of the mortgage. The effect of this would be to limit the taxable amount of the mortgage under Tax Law § 256. Two statements, one executed by an officer of Dollar Dry Dock dated September 2, 1987 and one by petitioner dated September 4, 1987, were submitted with this request. Both documents stated that when the consolidated mortgage was recorded, "the maximum principal debt or obligation which, under any contingency, was secured thereunder, and for which a New York State Mortgage Recording Tax was due and owing was $3,331,607.43." It was also stated therein that it was petitioner's intent that the mortgage secure the subject lien in the fixed amount of $8,400,000.00 and that "[i]t was not the intent...that the Consolidated Mortgage operate as ongoing security to secure unrelated transactions between the mortgagor and mortgagee." Further, it was asserted that when the mortgagee filed the mortgage, it was unaware that any such sworn statement was necessary.

The request to file a maximum amount statement was denied on October 1, 1987. The reason given for the denial was that the parties to the instrument and the recording officer all considered the instrument to be a mortgage the recording of which was taxable, and that therefore, there was not an honest misconception as to the nature of the instrument or its taxability as is required by Tax Law § 256.

SUMMARY OF THE PARTIES' POSITIONS

Petitioner contends that the amount of the mortgage recording tax due should be based on a sworn statement as to the maximum amount actually due under the mortgage at the time it was recorded pursuant to Tax Law § 256. Alternatively, petitioner contends that the tax should be based on the fair market value of the property to which it applies.

The Division of Taxation contends that petitioner's refund request should be denied and that the mortgage recording tax due on the mortgage should be based on the highest fair market value of the property securing the lien at any time between its execution and recordation, that the tax cannot be based on an amount less than that shown on the mortgage, and that the statements of maximum amount should be rejected.

CONCLUSIONS OF LAW

A. Tax Law § 253 provides that the amount of New York State mortgage recording tax

due when a mortgage is recorded is based on the "principal debt or obligation which is, or under any contingency may be secured at the date of execution thereof or at any time thereafter by such mortgage." However, if the principal indebtedness secured is not determinable from the terms of the mortgage, the amount due is determined under section 256. That section provides that such mortgage shall be taxable under section 253 "upon the value of the property as determined by the recording officer...unless at the time of presenting such mortgage for record the owner thereof shall file with the recording officer a sworn statement of the maximum amount secured." If such statement is filed, the amount expressed shall be the basis for assessing the tax. Tax Law § 256 further provides as follows:

> "Whenever any such mortgage shall have been recorded without the payment of tax as herein provided, and it shall thereafter be determined by the tax commission, after an opportunity to be heard by the parties in interest, that the failure to pay such tax was due to an honest misconception on the part of the recording officer or the owner of the instrument as to the nature of such instrument and its taxability under this article, the tax commission may make an order permitting the recording officer to file the aforesaid statement nunc pro tunc as of the date of the recording of the mortgage."

The purpose of Tax Law § 256 is to provide for a recording tax of mortgage instruments which are not and cannot be taxed elsewhere under Tax Law, Article 11 by reason of their indeterminable terms. Since some basis for a recording tax on indeterminable mortgages had to be made, the Legislature provided for two taxable alternatives, either on the appraised value of the mortgaged premises, or on the basis of a sworn statement setting forth the maximum amount secured or which under any contingency may be secured. Appraised value is to be used only where such sworn statement is not filed.

B. The specific addition of the last paragraph of Tax Law § 256 (L 1920, ch 75) recognizes the fact that mortgages, as a result of honest mistakes or misconceptions, may be "recorded without payment of the tax as herein provided" (i.e., upon basis of appraised value). Second, it also recognizes the need for the subsequent correction thereof by a sworn statement. An order nunc pro tunc under the prescribed conditions is authorized permitting the filing of the sworn statement effective on the date the mortgage was recorded. Consequently, "the payment of such tax may be made on the basis of such statement", as was possible initially had the mistake not been made, which expressly seeks to avoid and alleviate any tax upon the basis of appraised value.

Prior to the addition of the last paragraph of Tax Law § 256 by Laws of 1920 (ch 75) a tax correction was unauthorized, prohibiting the filing of an affidavit or statement of a designated amount at any time other than at the time of recording (1919 Annual Report of the State Tax Commission, 1920 NY Legis Doc No. 118, Vol. 37, at 35). Subsequently, it was recommended that sections 256 and 258 "be so amended as to permit the filing of a statement as to the amount secured by the instrument determined to be a mortgage nunc pro tunc if the commission is satisfied that the failure to file such statement and pay such tax at the time of recording the same was due to an honest misconception on the part of the recording officer and of the owner of the instrument..." (1919 Annual Report of the State Tax Commission, 1920 Legis Doc No. 118, supra). Although the above report seems to have been aimed primarily at instruments "not apparently mortgages upon their face", the actual statutory language adopted in the second paragraph of section 256 also includes all indeterminable instruments as well. This is demonstrated from its terms and its interlocking relationship with the provisions of the first paragraph. Thus, the wording:

> "Whenever any such mortgage shall have been recorded without payment of the tax as herein provided...due to an honest misconception...as to the nature of such

instrument and its taxability under this article"

includes not only those "instruments which are not mortgages upon their face", but also refers back to and includes (1) the two kinds of mortgages described in the first paragraph (i.e., those of an indeterminable nature and those securing the performance of contractual obligations); and (2) the particular basis upon which the tax is to be computed (i.e., the appraised value or the amount specified in a sworn statement).

C. In the instant case, the inclusion under the security of the mortgage of "any and all other sums...owing and to become due from mortgagor to mortgagee" (a "dragnet" clause) as well as the stated amount of $8,400,000.00 qualifies the mortgage as "indefinite" so that Tax Law § 256 applies. Since the future obligations which might come under the dragnet clause are completely undefined, section 256 (as, in fact, both parties agree) must apply. Where Tax Law § 256 applies, the effect is to establish the amount on which to compute the tax to be calculated under Tax Law § 253. That taxable amount is stated very specifically to be "the value of the property covered by the mortgage" or, if the taxpayer files a sworn statement of "the maximum amount secured or which under any circumstances may be secured", then the taxable amount is the amount specified in the statement. It is clear that the language of section 256 makes no reference to a minimum amount.

D. I find most of the arguments advanced by the Division are without any merit whatsoever. The Division's argument that the amount stated in the mortgage is a minimum on which to calculate the tax even where the value of the realty is much less is based on cases (Matter of Citizens National Bank v. State Tax Commission, 247 App Div 722; Matter of WBVM Associates, 120 Misc 2d 434) where the mortgage is definite on its face and is (so long as its provisions have not been subject to reformation in a court proceeding) therefore taxable under Tax Law § 253 without regard to the provisions of Tax Law § 256 with respect to indefinite mortgages. Also irrelevant are the cases which hold that an amount stated in a mortgage is taxable even though no amount has been so far advanced. In those cases (People v. Gass, 206 NY 609; Matter of Fox Lane Corp. v. Loughman, 225 App Div 417; Matter of Woodmere Knolls v. Procaccino, 52 AD2d 105) the amount stated could be advanced in the future and will be covered by the recorded mortgage. It is also clear that the taxable amount arrived at under section 256 is in complete substitution of and not in addition to any amount of "principle debt or obligation" which is otherwise taxable under section 253. And it is also clear that we are dealing with just one mortgage taxable under section 256 and not two separate mortgages which might be taxable under separate sections. There is one mortgage here which is taxable on an amount to be determined entirely under Tax Law § 256.

E. It is clear that the maximum amount statement is not an evidentiary document to be weighed by the recording officer in deciding what value to assign to the mortgage. The statute provides that if such a sworn statement is filed, the amount stated therein will determine the taxable amount. To prevent possible abuse, Tax Law § 256 further provides that if such a statement is utilized, the mortgagee and all persons claiming through him are forever barred from asserting any greater lien. (See, Miller, Hacking a Path Through the New York State Mortgage Tax Jungle, 43 Alb L Rev 37 [Rev 37 (1978)].) Thus, the mortgagor has as great an interest in declaring a correct figure in the sworn statement as he would have in recording a correct mortgage.

F. Thus, petitioner must be allowed to file, nunc pro tunc, a sworn statement of the "maximum amount secured or which under any contingency may be secured" under Tax Law § 256. The statute allows this only depending on there being "an honest misconception...as to the nature of such instrument and its taxability" under the mortgage tax. Whenever an erroneous amount is paid, there has had to be a misconception at least of the instrument's "taxability". The "nature" of the instrument, which can be the subject of any misconception,

clearly covers not only the identity of the instrument as a mortgage but also the identity of the instrument as an indefinite mortgage under Tax Law § 256. It is clear from the facts that at the time of recording both the recording officer and the bank misunderstood the taxability of the mortgage. Both parties mistakenly assumed the mortgage amount to be determinable from its terms. Had the recording officer been aware, he would not have recorded the mortgage based on a determinate amount but would have used one of the alternative methods under section 256.

It is found that there was an honest misconception and, therefore, petitioner will be allowed to file a maximum amount statement nunc pro tunc as of the date of the recording of the mortgage. Such statement should, of course, be filed with the recording officer. (It may be that the sworn statement in evidence in this case is not satisfactory because it may allow the mortgage to secure, in addition to a stated amount, other and unspecified "related" transactions between the mortgagor and mortgagee. However, this should be determined in the first instance by the recording officer.)

G. It is noted that the sworn statement presented in evidence in this case sets the amount secured at $4,724,100.00 which is below the $8,400,000.00 secured at the execution of the mortgage. (Whichever figure is taxable under Tax Law § 253 would be subject to reduction under Tax Law § 255 by the amount of the previously taxed mortgages of $1,407,507.23.) The difference between these figures is the amount by which the mortgage has been "paid down" and will not be taxed. It is true that Tax Law § 253 imposes the tax on the amount of principle debt or obligation secured "at the date of execution thereof or at any time thereafter". However, to apply this language literally to impose the tax on the original amount of a mortgage which has been paid down prior to recording would ignore the fact that the tax is fundamentally a recording tax and the amounts due prior to recording are unrelated to the recording and the protection provided by the recording act. As such, the tax would be a tax on intangible personal property existing at the date of execution. Such a tax on intangible personal property is proscribed by Article XVI section 3 of the New York State Constitution (Application of Downtown Athletic Club of New York, Inc., 280 App Div 363; Rathe v. Adirondack Concepts, Inc., 131 AD2d 81, 84). In short, to apply the tax to the initial value of the mortgage and thus tax the "paid down" amount would be impermissible.

H. If petitioner fails to furnish a sworn statement satisfactory to the recording officer, than the property under the mortgage would have to be valued. Despite the fact that evidence of value was taken during this hearing, it would be premature to make any finding concerning such value. Any finding of value would be unnecessary if, as expected, petitioner furnishes the sworn statement. Furthermore, section 256 states that such evidence of value shall be first taken by the recording officer and is subject to review by the State Tax Commissioner prior to any provision for review by the Division of Tax Appeals.

I. The petition of East 54th Street Associates is granted and petitioner is permitted to file a statement of the maximum amount secured nunc pro tunc pursuant to Tax Law § 256 and, further, that any determination of tax in this case shall be in accordance with this determination.

DATED: Troy, New York
October 10, 1989

/s/ Nigel G. Wright
ADMINISTRATIVE LAW JUDGE