Department of Taxation and Finance Declaratory Ruling on Extending The Draw Period Under a Home Equity Credit Line Mortgage

By Michael J. Berey

The New York State Department of Taxation and Finance (the "Department") recently issued an Advisory Opinion and a Technical Services Bulletin concerning the application of sect 253-b of the Tax Law to "credit line mortgages" which secure at any time a principal amount which is less than $3 million.

Section 253-b was amended effective November 6, 1996 by Chapters 489 and 490 of the Laws of 1996 to afford commercial credit line mortgages securing less than $3 million the benefits made available in 1985 under sect 253-b to mortgages on real property principally improved or to be improved by a one to six family, owner-occupied residence or dwelling. Under the statute, "no further tax shall be payable on advances and re-advances by the lender under the recorded primary mortgage, provided such advances or re-advances are made to the original obligor or obligors named in such recorded primary mortgage."

Under this Section, a "credit line mortgage" is defined to include any mortgage or deed of trust, other than a mortgage or deed of trust made pursuant to a building loan contract as defined in Section 13 of the lien law, which states that it secures indebtedness under a note, credit agreement or other financing agreement that reflects the fact that the parties reasonably contemplate entering into a series of advances, or advances, payments and re-advances, and that limits the aggregate amount specified in such mortgage or deed of trust. (I)

A reverse mortgage under Real Property Law sectsect 280 and 281 is not a credit line mortgage for the application of sect 253-b.

The Department’s position on the application of sect 253-b to such commercial credit line mortgages has been anticipated to resolve a number of issues. Would, for example, a credit line mortgage securing less than $3 million which was a part of a larger credit facility have the benefit of the statute? Could a recorded credit line mortgage be "spread" to encumber other real property? Might a credit line mortgage not made pursuant to a formal building loan agreement be used to fund improvements to real property ? Many of the questions that have been posed are addressed in the Bulletin and the Advisory Opinion discussed below.

On June 25, 1999, the Department’s Taxpayer Services Division, by its Technical Services Bureau, issued TSB-M-99(1)R entitled "Application of the Mortgage Recording Tax to Commercial Credit Line Mortgages." The Department, in that Bulletin, has taken the following positions on sect 253-b.

1. A revolving credit mortgage for $3 million or more recorded prior to November 6, 1996, the date on which Chapters 489 and 490 of the Laws of 1996 took effect (the “Effective Date”), cannot be reduced to be less than $3 million and receive the benefits of sect 253-b.

2. A mortgage securing both a credit line of less than $3 million and also a non-revolving credit obligation will not receive the benefits of sect 253-b. The Department has informally advised this author that the mortgage cannot secure both revolving and non-revolving obligations, regardless of the maximum aggregate principal amount that could be secured between them at any one time.

3. A mortgage securing a credit line of less than $3 million will not receive the benefits of sect 253-b if the secured obligation is part of an overall credit facility exceeding $3 million.

4. Separate credit line mortgages, on even separate and distinct real property interests, having the same or related mortgagors and being part of the same or related transactions will be aggregated to determine if the under $3 million cap is exceeded.

5. A credit line mortgage, resulting from the severance of an unsecured term loan of any amount into a credit facility of less than $3 million and a term loan of any amount, can be recorded on or after the Effective Date and obtain the benefits of sect 253-b.

6. On the transfer of real property subject to the lien of a credit line mortgage on which mortgage tax is paid by the grantee, the grantee cannot obtain the benefit of the statute for any future re-loans or re-advances. sect 253-b limits its benefits to the original obligor.

7. The same borrower can with the same lender enter into a later, separate credit line mortgage on different property securing a distinct credit agreement so long as the second transaction was not contemplated at the time of the first. This would not be the case, and the benefit of the statute would not be afforded, if the mortgages secured $3 million in the aggregate at any one time and were spread and consolidated, cross-defaulted or cross-collateralized.

The two mortgage transactions would be deemed related, treated as a single mortgage and aggregated when a different lender provides the second credit line mortgage loan and simultaneously takes the other, prior credit line mortgage by assignment, regardless of whether the mortgages are spread and consolidated, cross-defaulted or cross-collateralized.

8. A credit line mortgage can be spread to encumber other real property, with the prior real property mortgaged being released, even when the mortgage is assigned to an unrelated mortgagee. However, the benefits of sect 253-b will not be afforded when there is a change in the identity of the obligor, even if the new mortgagor is controlled by the same person or entity. The statute provides that advances and re-advances must be “made to the original obligor or obligors named in such recorded primary mortgage.”

9. The benefits of sect 253-b are not available to a credit line mortgage resulting from the modification of a non-credit line mortgage, even when the original mortgage was recorded after the Effective Date. According to the TSB, the benefits of the statute are to be applied to newly created credit line mortgages recorded after the Effective Date, not credit lines resulting from the modification of an existing recorded conventional mortgage. This position applies as well to credit line mortgages on real property principally improved or to be improved by a one to six family, owner-occupied residence or dwelling.

An Advisory Opinion was also issued by the Technical Services Bureau on April 7, 1999 (II) in response to a request for the Department’s position on whether a credit line mortgage under sect 253-b includes a mortgage executed to secure the repayment of advances and re-advances made either (a) to reimburse a borrower for expenses incurred for improvements made to real property or (b) to enable such improvements to be made when, in either instance, there is no agreement between the borrower and the lender which includes the borrower’s express promise to make an improvement.

As noted above, sect 253-b provides that a credit line mortgage does not include “a mortgage or deed of trust made pursuant to a building loan contract as defined in subdivision thirteen of section two of the lien law.” Lien Law sect 2(13) defines a “building loan contract” as “a contract whereby a party thereto [the lender] in consideration of the express promise of any owner to make an improvement upon real property, agrees to make advances to or for the account of such owner to be secured by a mortgage on such real property.” (emphasis added)

In its Advisory Opinion, the Department takes the position that a mortgage executed to secure the repayment of advances and re-advances made either to fund or to reimburse a borrower for the making of improvements upon real property will not qualify as a credit line mortgage under sect 253-b, regardless of whether a formal building loan agreement is filed. It holds that any limiting conditions in the mortgage or related loan documents relating to the use of the funds will constitute an “express promise” of the borrower to make improvements to real property, and the mortgage will therefore be deemed to have been made pursuant to a building loan contract. This position would also apply to credit line mortgages on real property principally improved or to be improved by a one to six family, owner-occupied residence or dwelling.

The Department has set forth its position on how to apply sect 253-b to commercial credit line mortgages securing less than $3 million. Among other things, clearly a commercial credit line mortgage may not be used to fund improvements, spread to a different parcel of real property and there also be used to fund construction.

Endnotes

(I) Section 281 of the Real Property Law affords lien priority for future advances made within 20 years of the recording of a “credit line mortgage” as defined in that section. Under Chapter 183 of the Laws of 1999, a reverse mortgage loan is not subject to the 20 year limitation.

(II) Petition No. M981215A.

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