STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
LONG ISLAND LIGHTING COMPANY	:	DETERMINATION DTA NO. 809930
for Revision of a Determination or for Refund of Mortgage Recording Tax under Article 11 of the Tax Law.	:	

Petitioner, Long Island Lighting Company, 175 East Old Country Road, Hicksville, New York 11801, filed a petition for revision of a determination or for refund of mortgage recording tax under Article 11 of the Tax Law.

Petitioner, by its representative, Herbert M. Leiman, Esq., and the Division of Taxation, by its representative, William F. Collins, Esq. (Donald C. DeWitt, Esq., of counsel), executed a consent to have the controversy determined on submission without hearing, with all briefs and documentary evidence to be submitted by December 15, 1993. Petitioner filed affidavits on October 29, 1993 and a brief on December 17, 1993.[1] The Division of Taxation filed its brief on November 26, 1993. Upon review of the entire record, Arthur S. Bray, Administrative Law Judge, renders the following determination.

ISSUE

Whether a mortgage offered for recording on October 26, 1989 was exempt from mortgage recording tax.

FINDINGS OF FACT

The parties, by their respective representatives, executed a Stipulation of Facts. The

[1]It is recognized that petitioner's brief was filed two days late. Under the circumstances presented herein, the short delay does not warrant rejecting petitioner's brief (see, Matter of Angelico, Tax Appeals Tribunal, June 16, 1993).

stipulation is reproduced here in its entirety as Findings of Fact "1" through "25" with minor editing. For clarification, the footnotes and portions of certain documents have been added to the stipulated facts.

Petitioner, Long Island Lighting Company ("LILCO"), is a corporation incorporated under the laws of the State of New York and having its principal place of business at 175 East Old Country Road, Hicksville, New York 11801.

On December 31, 1985, LILCO entered into certain agreements, as described below, with Bankers Trust Company ("Bankers Trust"), Citibank, N.A. ("Citibank"), the New York State Energy Research & Development Authority ("NYSERDA") and The Connecticut National Bank (the "Trustee") in connection with the issuance of the 1985 Series A Adjustable Rate Pollution Control Revenue Bonds in the principal amount of $100,000,000.00 and the 1985 Series B Adjustable Rate Pollution Control Revenue Bonds in the principal amount of $50,000,000.00.

On September 22, 1975, LILCO entered into an agreement with Niagara Mohawk Power Corporation ("NMPC") to fund its 18% share of all costs required to construct the Nine Mile Point Nuclear Power Station, Unit 2 in Oswego, New York.

On August 22, 1984, LILCO and Citibank executed a mortgage in the amount of $1,295,000.00. This instrument was recorded in the Office of the County Clerk of Nassau County on August 30, 1984 in Liber 10929 of Mortgages, Page 1 (the "Old Third Mortgage").

On October 30, 1985 and later amended on December 4, 1985 and June 25, 1986, the Public Service Commission of the State of New York (the "PSC") issued an order authorizing the initial issuance of the debt contemplated by the issuance of the 1985 Series A and 1985 Series B Adjustable Rate Pollution Control Revenue Bonds.

On December 31, 1985, LILCO and Bankers Trust entered into an agreement, pursuant to which Bankers Trust provided, in favor of the Trustee, its Irrevocable Letter of Credit No. A-97817-S in the amount of $108,875,000.00. This letter of credit expired on March 16, 1989.

On December 31, 1985, LILCO and Citibank entered into an agreement, pursuant to

which Citibank provided, in favor of the Trustee, its Irrevocable Letter of Credit No. NABG-E20337H in the amount of $54,437,500.00. This letter of credit expired on March 16, 1989.

On December 31, 1985, Guaranty Agreements each dated December 1, 1985 and later amended as of June 15, 1987, July 15, 1988, February 1, 1989 and August 1, 1989 were entered into between NMPC and Bankers Trust and NMPC and Citibank (collectively referred to as the "Guaranty Agreements").

On December 31, 1985, LILCO and NMPC entered into an agreement which set forth the company's obligations to NMPC in exchange for execution of the Guaranty Agreements (the "LILCO/NMPC Agreement"). Pursuant to this agreement, the company executed a promissory note to NMPC in the amount of $165,000,000.00 (the "Note"), as evidence of the company's obligation to NMPC.

On March 27, 1986, LILCO and NMPC executed a mortgage in the amount of $85,000,000.00 to partially secure the Note. This instrument was recorded in the Office of the County Clerk of Nassau County on March 31, 1986 in Liber 11461 of Mortgages, Page 441 (the "Old Fourth Mortgage").

The Old Fourth Mortgage contained provisions which stated:

> "WHEREAS, in consideration of the execution and delivery by NMPC of the Guaranty Agreements, the Company has agreed to secure hereunder its obligations to NMPC as provided in the LILCO/NMPC Agreement up to an aggregate total amount, whether for principal, interest, fees or otherwise, of $85,000,000 (eighty-five million dollars) (such obligations in such aggregate amount being the "NMPC Reimbursement Obligations");
>
> "NOW, THEREFORE, THIS MORTGAGE WITNESSETH, that to secure the payment of and the performance by the Company of the NMPC Reimbursement Obligations and the performance of the covenants herein contained and in consideration of the premises and of the covenants herein contained and of the sum of $1 paid to the Company by NMPC at or before the ensealing and delivery hereof, the receipt whereof is hereby acknowledged, the Company by these presents does . . . mortgage . . . unto NMPC the following property . . . ."

On March 31, 1986, LILCO paid the full amount of the mortgage tax, as calculated on New York State Form MT-15 NYC, to the Clerk of Nassau County in the amount of $928,776.00 for the recording of the Old Fourth Mortgage.

On April 22, 1986, LILCO, Citibank, as mortgage agent, and NMPC entered into an

Agreement of Spreader, Consolidation and Modification. This instrument was recorded in the Office of the County Clerk of Nassau County on April 22, 1986 in Liber 11487 of Mortgages, Page 149 (the "Spreader").[2]

On June 30, 1986, NMPC, Bankers Trust and Citibank executed an Assignment of Mortgage, Security Interest and Right to Proceeds. This

instrument was recorded in the Office of the County Clerk of Nassau County on August 11, 1987 in Liber 9834 of Deeds, Page 851 (the "1986 Assignment").[3]

On February 3, 1989, LILCO negotiated an extension of the original letters of credit until March 1991.

On February 3, 1989, LILCO and NMPC executed an agreement extending NMPC's guaranties (the "Consent and Agreement").

On May 31, 1989, LILCO filed a petition dated May 30, 1989 under N.Y. Pub. Serv. Law § 69 seeking authority to replace the existing letters of credit with substitute letters of credit.

In a letter dated August 11, 1989, the Secretary of the PSC informed LILCO that PSC approval was not required for this transaction.

As part of the negotiations for the replacement of Letter of Credit bank, Citibank required LILCO (i) to deliver an $85,000,000.00 mortgage which was pari passu to the Third Mortgage, (ii) to have NMPC assign the Note to Citibank, and (iii) to have mortgage title insurance issued on behalf of Citibank.

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[2]This agreement, among other things, consolidated the Old Third Mortgage with the Old Fourth Mortgage.

[3]By this document, NMPC assigned its right, title and interest in (1) the Old Fourth Mortgage, (2) the Consolidation Agreement, (3) following the consolidation date, the Third Mortgage (as defined in the Consolidation Agreement), (4) the Collateral Agreement (as defined in the Consolidation Agreement) and (5) the NMPC Reimbursement Obligations (as defined the Fourth Mortgage).

On October 26, 1989, LILCO and Citibank entered into two separate Amended and Restated Reimbursement Agreements each dated as of October 13, 1989 which provided for letters of credit which were intended to replace the original Citibank and Bankers Trust letters of credit.

On October 26, 1989, the Note was modified by LILCO and Citibank and then executed as the Amended and Restated Promissory Note in the amount of $165,000,000.00.

On October 26, 1989, LILCO and Citibank executed a mortgage dated as of October 13, 1989 in the amount of $85,000,000.00. This instrument was recorded in the Office of the County Clerk of Nassau County on October 26, 1989 in Liber 13253 of Mortgages, Page 1 (the "Fourth Mortgage").

Among the paragraphs included in the Fourth Mortgage were the following:

> "WHEREAS, to induce the Bank [Citibank] to provide the Letters of Credit and in consideration of the execution and delivery by the Bank of the Letters of Credit, the Company [LILCO] has agreed to secure hereunder its obligations to the Bank first as provided in the $54 Million Reimbursement Agreement and then as provided in the $108 Million Reimbursement Agreement, up to an aggregate total amount, whether for principal, interest, fees or otherwise, of $85,000,000 (such obligations in such order, and in the aggregate amount of $85,000,000, whether for principal, interest, fees or otherwise, being the "Bank Reimbursement Obligations");
>
> "WHEREAS, it is the intent of the parties hereto not to cancel or extinguish the BT [Bankers Trust] Letter of Credit Obligations, the Citibank Letter of Credit Obligations or the Company's Bond Obligations, but to continue and confirm them as modified by the terms of the Reimbursement Agreements;
>
> "NOW, THEREFORE, THIS MORTGAGE WITNESSETH, that to secure the payment of and the performance by the Company of the Bank Reimbursement Obligations, and as a condition precedent to the obligation of the Bank to issue the Letters of Credit, and in consideration of the premises and of the covenants herein contained and of the sum of $1 paid to the Company by the Bank at or before the ensealing and delivery hereof, the receipt whereof is hereby acknowledged, the Company by these presents does . . . mortgage . . ., unto the Bank, the following property . . . ."

On October 26, 1989, the company, Citibank, as Mortgage Agent, and Citibank, as Letter of Credit bank, executed an Intercreditor Agreement dated as of October 13, 1989, which evidenced the Letter of Credit banks' pari passu position with the Third Mortgage banks.

The Intercreditor Agreement contained a paragraph which stated:

> "WHEREAS, the parties have been advised by the Company that it is the intention of the Company to continue and confirm, by the execution and delivery of the Termination Agreement, the Surrender Agreement and the Fourth Mortgage . . ., the security, which has remained unchanged since the issuance of the Bonds . . . previously provided to the Letter of Credit Banks . . . ."

On October 26, 1989, an Assignment and Transfer of Mortgage, Interest, Security Interest and Right to Proceeds dated as of October 13, 1989 from Bankers Trust and Citibank to NMPC was executed. This instrument was recorded in the Office of the County Clerk of Nassau County on October 26, 1989 in Liber 13253 of Mortgages, Page 204 (the "1989 Assignment").

The Assignment and Transfer of Mortgage Interest, Security Interest and Right to Proceeds stated, in pertinent part:

> "NOW THEREFORE, in consideration of $10 and other good and valuable consideration, the adequacy of which is hereby acknowledged, the Assignors [Bankers Trust and Citibank] hereby assign, transfer and set over unto the Assignee [NMPC] all right, title and interest in (i) the Fourth Mortgage, (ii) the Consolidation Agreement, (iii) the Third Mortgage (as defined in the Consolidation Agreement), (iv) the Collateral Agreement (as defined in the Consolidation Agreement) and (v) the NMPC Reimbursement Obligations (as defined in the Fourth Mortgage and Consolidation Agreement) that was originally assigned by the Assignee to the Assignors pursuant to the Assignment Agreement; provided that nothing contained herein shall be deemed to affect any rights of assignors to any of the foregoing under the Amended and Restated Restructuring Credit Agreement dated as of June 27, 1989 between LILCO, the banks party thereto and Citibank, The Chase Manhattan Bank, N.A. and Chemical Bank as Co-Agents for such banks.
>
> "This Assignment and Transfer does not alter in any manner any other relationships which exist between Assignors, Assignee, LILCO or any other party."

On October 26, 1989, NMPC and LILCO entered into a Surrender of Mortgage Interest, Security Interest and Right to Proceeds dated as of October 13, 1989. This instrument was recorded in the Office of the County Clerk of Nassau County on October 26, 1989 in Liber 13253 of Mortgages, Page 232 (the "Surrender").

The Surrender of Mortgage Interest, Security Interest and Right to Proceeds from NMPC to LILCO provided, in part:

> "WHEREAS, Bankers Trust and Citibank have executed and delivered releases which release NMPC from its obligations as guarantor under the

Guaranties; and

"WHEREAS, pursuant to an Assignment and Transfer of Mortgage Interest, Security Interest and Right to Proceeds dated the date hereof which Bankers Trust, Citibank and NMPC have executed, delivered and caused to be recorded, Bankers Trust and Citibank assigned, transferred and set over unto NMPC all of their collective rights, title and interest in (i) the Fourth Mortgage, (ii) the Consolidation Agreement, (iii) the Third Mortgage (as defined in the Consolidation Agreement), (iv) the Collateral Agreement (as defined in the Consolidation Agreement) and (v) the NMPC Reimbursement Obligations (as defined in the fourth Mortgage and Consolidation Agreement).

"NOW, THEREFORE, in consideration of the release by Citibank and Bankers Trust of NMPC's obligations under the Guaranties the receipt and adequacy of which is hereby acknowledged, NMPC and LILCO agree that the NMPC Reimbursement Obligations (as defined in the Fourth Mortgage and Consolidation Agreement) are irrevocably extinguished and NMPC hereby surrenders and releases all of its right, title and interest in (i) the Fourth Mortgage, (ii) the Consolidation Agreement, (iii) the Third Mortgage (as defined in the Consolidation Agreement), (iv) the Collateral Agreement (as defined in the Consolidation Agreement) and (v) the NMPC Reimbursement Obligations (as defined in the Fourth Mortgage and Consolidation Agreement), and, also in consideration of the aforesaid release of NMPC by Citibank and Bankers Trust NMPC hereby releases the Mortgage Agent (as defined in the Third Mortgage and Consolidation Agreement) from any liability under the Third Mortgage, the Fourth Mortgage and the Consolidation Agreement.

"This Surrender concerns only the relationships detailed herein and does not alter in any manner the relationships between LILCO and any other party in any of the above referenced documents or agreements or any other relationship between NMPC and LILCO."

On October 26, 1989, LILCO paid the full amount of the mortgage tax, as calculated on New York State Form MT-15 NYC to the Clerk of Nassau County in the amount of $921,124.00. This amount was paid by a certified check which reflected the notation that this tax was paid under protest.

In addition to the facts set forth in the stipulation, the following facts are found.

In a letter dated June 5, 1991, the Division denied petitioner's application for a refund of mortgage recording tax. The denial was based on the Division's position that "in order to be exempt from mortgage recording tax, the original indebtedness must remain undischarged and the original mortgage lien must be continued in force". The Division concluded that mortgage recording tax was properly imposed because the mortgage in issue replaced and superseded the prior mortgage. This proceeding ensued.

In support of its position, petitioner submitted affidavits from a George Sideris who, from March 1984 until January 1992, served as Vice President-Finance and then as Senior Vice President-Finance of LILCO. Between 1984 and 1990, Mr. Sideris was responsible for all of LILCO's financial and securities transactions and negotiated all of the significant terms.

In his affidavit, Mr. Sideris explained that, in December 1985, NYSERDA agreed to issue on LILCO's behalf $150,000,000.00 of tax-exempt Pollution Control Revenue Bonds ("bonds"). As a condition, NYSERDA required LILCO to obtain letters of credit support in the amount of approximately $163,000,000.00.

Mr. Sideris negotiated with Citibank and Bankers Trust ("Banks") and they agreed to provide LILCO with two letters of credit in the amount of approximately $163,000,000.00 with an expiration date of March 1989. Mr. Sideris explains that because of LILCO's precarious financial condition, the Banks would not issue the letters of credit without additional security. Therefore, NMPC agreed to guarantee the letters of credit through a Guaranty Agreement dated December 1, 1985, as amended as of June 15, 1987, July 15, 1988, February 1, 1989 and August 1, 1989. In exchange for its guarantee, NMPC insisted that LILCO provide a $165,000,000.00 Promissory Note dated December 31, 1985 ("Note") and an $85,000,000.00 Fourth Mortgage dated March 27, 1986 ("Fourth Mortgage") on LILCO properties. NMPC also insisted that LILCO grant NMPC pari passu rights in an outstanding Third Mortgage dated August 22, 1984, which was granted to Citibank and other lending banks.

Mr. Sideris continues that, in early 1989, prior to the March 16, 1989 expiration of the letters of credit, he addressed with the Banks and NMPC the need for an extension of the letters of credit and the NMPC guaranty until March 1991. During these negotiations, NMPC agreed to return a major portion of the fees already paid to it if NMPC was removed as guarantor before March 1990. Beginning in February 1989, Mr. Sideris monitored the transaction to determine when the company could remove NMPC and renegotiate the deal. In June 1989, LILCO commenced discussions with Citibank to remove NMPC.

According to Mr. Sideris, in October 1989, LILCO negotiated with Citibank for new

letters of credit, at a lower cost, to support the Bonds for an additional three years and to substitute for the letters of credit that had been issued by Citibank and Bankers Trust in 1985. Under the new arrangement, Bankers Trust was to be released from its support obligation and NMPC was to be removed as guarantor. In connection with these letters of credit, Citibank required the assignment to it of the Note, which had been initially issued to NMPC. Additionally, Citibank made it a condition of the issuance of its letter of credit that it be provided with the same security that had been provided to NMPC, namely, an $85,000,000.00 mortgage that would be pari passu with LILCO's existing Third Mortgage. Citibank also required LILCO to obtain title insurance to insure that no liens intervened between the time that NMPC was named as mortgagee under the Fourth Mortgage and the time Citibank was named as successor under the new arrangements.

Mr. Sideris explains that, during these negotiations, he informed Citibank that LILCO wanted to minimize any costs associated with this transaction, specifically, that LILCO wanted to avoid a new mortgage tax and title insurance. LILCO's attorneys informed Mr. Sideris that by exchanging a new instrument naming Citibank as mortgagee for the existing Fourth Mortgage and by specifically providing for such exchange in the closing documentation, a new mortgage tax could be avoided. LILCO's attorneys and Citibank's attorneys worked together to structure the transaction so that no new mortgage tax would be required. At the direction of LILCO's attorneys and with Citibank's consent, the documentation was drafted to reflect LILCO's desire to avoid the mortgage tax. Mr. Sideris further explained that in order to continue the lien of the Fourth Mortgage, the instrument naming Citibank as mortgagee would be exchanged and recorded before the existing Fourth Mortgage was satisfied of record. LILCO also agreed to give Citibank a title report evidencing the continuation of the lien without any intervening liens between the new instrument and the existing Fourth Mortgage.

Mr. Sideris avers that Citibank wanted to be protected from any possible tax liability and gave the company several options to close the transaction. Because of the ongoing significant daily costs and the expenses associated with the February 1989 transaction, the company

wanted to close the transaction quickly. According to Mr. Sideris, to eliminate the costs and close the transaction, LILCO consented at Citibank's insistence to the only timely option, namely, to pay the mortgage tax and thereafter to seek a refund. Upon payment of the tax, Mr. Sideris directed LILCO's counsel to file the application for a refund.

Petitioner also presented the affidavit of a Robert S. Lyle, who was a vice president in the Utility Department of Citibank during the periods relevant to the matters herein and between 1980 and 1990 was Citibank's principal representative in negotiations with LILCO on a substantial number of its finance transactions with its banks. To the extent not repetitious of that presented by Mr. Sideris, Mr. Lyle states that during the negotiations for the $165,000,000.00 Promissory Note and the $85,000,000.00 mortgage that would be pari passu with LILCO's existing Third Mortgage, he was keenly aware that LILCO wanted to structure the transaction in such a way that it did not require a new mortgage tax. Mr. Lyle asserts that Citibank's attorneys were directed to assist LILCO's counsel in structuring the transaction so that no additional mortgage tax would be required.

Mr. Lyle explained that to protect Citibank if the structure of this transaction resulted in an additional mortgage tax, he insisted that LILCO either obtain an advisory opinion from the Division that no additional mortgage recording tax was required or pay the mortgage recording tax and seek a refund.

Mr. Lyle maintains that because of the ongoing expense associated with the existing Citibank and Bankers Trust letters of credit and the NMPC guaranty arrangement, and the time required to get an advisory opinion, the parties agreed to close the transaction on the basis that LILCO would exchange a Fourth Mortgage dated October 13, 1989 for the existing Fourth Mortgage in order to provide Citibank with an $85,000,000.00 mortgage lien. Through an Intercreditor Agreement dated October 13, 1989, the new instrument was given the pari passu position with the holders of the Third Mortgage formerly held by NMPC. Additionally, because the cost to LILCO of title insurance would have been prohibitive, Citibank agreed to accept a title report from LILCO evidencing the absence of any lien intervening between the replacement

Fourth Mortgage naming Citibank as mortgagee and the existing Fourth Mortgage naming NMPC as mortgagee.

Mr. Lyle further submits that it was also agreed that the Fourth Mortgage dated October 13, 1989 in favor of Citibank and the Intercreditor Agreement were to be recorded before recording a satisfaction of the existing NMPC Fourth Mortgage; that the mortgage tax would be paid; and that LILCO would file an application for a refund. Although Citibank insisted on LILCO paying a mortgage tax, Citibank indicated that it had no objection if LILCO sought the refund on the ground that no additional mortgage tax was due on the transaction as long as such determination would not affect the validity of the mortgage.

SUMMARY OF THE PARTIES' POSITIONS

Petitioner maintains that an instrument, nominally recorded as a mortgage, which does not evidence a lien securing new or further indebtedness, does not "impose a lien" within the meaning of Tax Law § 250 and is exempt from tax. It is petitioner's position that the Fourth Mortgage is exempt from tax because it does not secure new indebtedness but merely continues an existing lien in connection with an ongoing security interest. According to petitioner, Citibank, as mortgagee under the Fourth Mortgage, has "stepped into the shoes" of NMPC vis-a-vis the remaining creditors who share the lien evidenced by the Third Mortgage.

Petitioner also argues that the Fourth Mortgage does not evidence security for new or further indebtedness. Petitioner submits that no new debt was created by the 1989 transactions and, therefore, the Fourth Mortgage does not "impose a lien" within the meaning of Tax Law §§ 250 and 253. After reviewing the changes which occurred, petitioner concludes that, despite the changes in parties and amendments to LILCO's obligations under the letters of credit, no new lien was created.

Lastly, petitioner argues that the Fourth Mortgage and the Intercreditor Agreement show it was LILCO's intent not to cancel or extinguish the security previously granted but rather to continue and confirm it. Petitioner's brief concludes with the argument that the $85,000,000.00 lien originally held by NMPC is now held by Citibank as evidenced by the Fourth Mortgage. It

is submitted that the lien imposed by the Fourth Mortgage is the same lien previously imposed by that part of the Third Mortgage which represented the lien of the Old Fourth Mortgage and the Fourth Mortgage. Petitioner concludes that the $85,000,000.00 originally imposed in 1986 remains in force and that only the evidence of the lien has changed.

In response to the foregoing, the Division contends that when NMPC, as the sole entity holding an interest in the Fourth Mortgage, surrendered its interest to LILCO, the Old Fourth Mortgage ceased to exist by the doctrine of merger. The Division submits that the Old Fourth Mortgage, extinguished by its surrender to LILCO, could not thereafter be resurrected and modified by LILCO and Citibank. According to the Division, while the property secured by the Old Fourth Mortgage and the amount of indebtedness remained unaltered between the Old Fourth Mortgage and the Fourth Mortgage, the underlying lien was not preserved from the Old Fourth Mortgage, notwithstanding the assignment by the parties of the underlying $165,000,000.00 Promissory Note. This argument continues that it is not enough that the parties intend to preserve the evidence of debt secured by the Old Fourth Mortgage to avoid the imposition of mortgage recording tax. Rather, the original indebtedness must remain undischarged and the original mortgage lien must remain in force. The Division concludes with the argument that while the Note was assigned by NMPC to Citibank, the Old Fourth Mortgage was not assigned to Citibank. Instead, it was surrendered by NMPC to LILCO and extinguished. The Division submits that a "new" Fourth Mortgage was executed by LILCO to Citibank and, as a result, the mortgage in issue was not supplemental to the Old Fourth Mortgage and mortgage recording tax was due.

Petitioner submitted a responding brief which reiterated its position that replacing the 1986 instrument with the 1989 instrument did not create a new lien within the meaning of Article 11 of the Tax Law. Petitioner submits that since it continued an existing lien, there is no need for it to rely upon Tax Law § 255 for an exemption even though it is available to petitioner. Petitioner's brief then proceeds to raise four points: that Tax Law § 255 is not the sole basis under the Tax Law for an exemption from mortgage recording tax; that the

continuation of a lien through an exchange of instruments is not subject to mortgage recording tax; that if properly effected, the form and timing of the transaction will preserve the lien; and that a change of mortgages when the mortgages are exchanged does not result in a taxable lien.

CONCLUSIONS OF LAW

A. Article 11 of the Tax Law imposes a tax on the recording of mortgages on real property located in the State of New York (see, Tax Law § 253[1]). The mortgage recording tax is imposed on the privilege of recording a mortgage rather than the privilege of lending money (Matter of Citibank v. State Tax Commn., 98 AD2d 929, 470 NYS2d 920, 921). The mortgage debt is used as the basis for the computation of the tax (Matter of Citibank v. State Tax Commn., supra; Tax Law § 253[1]).

B. The essence of the dispute between the parties focuses on whether the transactions which occurred in 1989 created a new lien or continued a pre-existing lien. Since the parties have relied on largely the same cases, a review of the these cases is in order.

C. In Matter of Sverdlow v. Bates (283 App Div 487, 129 NYS2d 88), petitioners gave a total of 18 mortgages on 7 parcels of real estate in Potsdam, New York. Initially, separate mortgages had been given to the Savings and Loan Association upon single parcels of property. However, as time went on, the equity of the owners in each mortgaged parcel increased. Thereafter, petitioners borrowed additional sums from the Savings and Loan Association giving as security a blanket mortgage covering the additional equity in the property already mortgaged and an additional parcel or parcels. In order to satisfy criticism from the State Banking Department, it was agreed that the amount of mortgage indebtedness would be reallocated among the parcels and seven new mortgages, each covering a single parcel, would be given. Thereafter, the State Tax Commission concluded that mortgage recording tax was due. The court confirmed this determination stating:

> "We are constrained to uphold the Tax Commission's determination. The old mortgages were all discharged of record and new mortgages were recorded. It is true that the total amount of the new mortgages was identical with the total amount of the discharged mortgages, but this fact does not relieve the petitioners of liability for the mortgage recording tax. A recording tax is payable under Section 253, by reason of the execution and recording of the new mortgages.

* * *

> "Both petitioners joined in all the new mortgages, whereas some of the former mortgages had been given by one of the petitioners alone. As to these mortgages, a tax was clearly payable because a new mortgagor had been added by the transaction [citations omitted]. However, even as to the mortgages which had not resulted in the addition of a new debtor, the mortgage tax was payable merely because of the fact that the old mortgages had been discharged and new mortgages had been given . . ." (Matter of Sverdlow v. Bates, supra, 129 NYS2d at 90).

In Matter of Fifth Avenue & 46th Street Corp. v. Bragalini (4 AD2d 387, 165 NYS2d 312), the petitioner gave a mortgage on July 7, 1953, to Irving Trust Company ("Irving") to secure an indebtedness in the amount of $2,150,000.00 which was evidenced by a mortgage note in that amount. On March 18, 1955, the petitioner borrowed an additional $600,000.00 from Irving. The new debt was consolidated with the earlier mortgage into a single lien securing a total debt of $2,750,000.00. On May 20, 1955, the petitioner entered into a "purchase agreement" with Massachusetts Mutual Life Insurance Company ("Massachusetts Mutual") whereby Massachusetts Mutual agreed to purchase $1,000,000.00 of bonds issued by the petitioner to be secured by a mortgage and also agreed to purchase from Irving the old mortgage notes in the amount of $2,750,000.00. The total indenture was set at $3,750,000.00 and the parties agreed that Massachusetts Mutual was entitled to receive, in exchange for the mortgage notes, bonds under the indenture.

On May 31, 1955, the transaction was closed and, on the same day, Irving became the trustee under the indenture of mortgage. Massachusetts Mutual paid Irving $2,750,000.00 for the two mortgage notes and, thereafter, Irving assigned the notes to Massachusetts Mutual. At the same time, Irving assigned to itself as trustee the existing mortgage in the amount of $2,750,000.00. The indenture of mortgage provided that the lien of the existing mortgage was confirmed and consolidated with the lien of indenture. It also provided that it was to secure both the old mortgage indebtedness as well as bonds issued under the indenture.

Pursuant to the indenture, the petitioner purchased a bond from Massachusetts Mutual in the amount of $1,000,000.00. Massachusetts Mutual surrendered the mortgage notes which it acquired from Irving to the trustee for a new bond under the indenture in the same principal

amount as the sum of the old mortgage notes, $2,750,000.00. Thereafter, Massachusetts Mutual surrendered the new bonds of $1,000,000.00 and $2,750,000.00 and obtained a single bond of $3,750,000.00.

The petitioner offered to pay mortgage recording tax on the $1,000,000.00. However, the Register of New York City, and subsequently the State Tax Commission, concluded that tax was due on the total amount of $3,750,000.00.

In the proceeding which followed, the determination of the State Tax Commission was annulled. Initially, the court noted that it was not the intention of the parties to cancel the old indebtedness but to continue and confirm it (id., 165 NYS2d at 316). The court then pointed out that the exchange of the old mortgage notes for the bonds in a new form did not cancel the indebtedness. It merely exchanged one form of evidence of indebtedness for another (id., 165 NYS2d 316).

After noting that the old indebtedness was not cancelled, the court stated that Tax Law § 253 only imposes tax "to the extent of any new principal debt or obligation" secured thereby (id., 165 NYS2d at 317). The court proceeded to describe the crux of its determination as follows:

> "The essential point is that, in order to be exempt from the mortgage tax, the original indebtedness must remain undischarged and the original mortgage lien must be continued in force. In this case, both the original debt and the original mortgage lien were kept alive. The change of the form of the mortgage from a direct mortgage to a mortgage to a trustee did not impair the lien of the mortgage" (id., 165 NYS2d at 318).

The Court concluded that since the old indebtedness and the old mortgage lien were kept alive, tax was due only on the amount of the new loan.

In Matter of Bay View Towers Apartments v. State Tax Commn. (48 AD2d 86, 367 NYS2d 856, affd 40 NY2d 856, 387 NYS2d 1002), the Village Mall at Bayside, Inc. ("Village Mall") executed to Long Island Savings Bank ("LISB") a promissory note and first mortgage on property in Bayside, New York, on which townhouses and apartment buildings were planned to be built. The mortgage described the entire property as Parcel I and subdivisions of the land as Parcels II and III. The mortgage was recorded on July 27, 1971 and mortgage recording tax was

paid.

On October 29, 1971, Village Mall and LISB executed a "Mortgage Severance and Modification Agreement" which severed the mortgage into two parts. Thereafter, the lien on Parcel II secured $3,220,000.00 of the original debt and the lien on Parcel III secured $930,000.00 of the original debt. The document specifically stated that it secured the original indebtedness and did not secure additional obligations. On November 10, 1971, the instrument was recorded and no tax was paid. Thereafter, Bay View Towers, Inc. ("Bay View") acquired title to Parcel II.

After execution of the "Mortgage Severance and Modification Agreement", Village Mall conveyed Parcel III, subject to the $930,000.00 mortgage, to Briarwood Terrace, Inc. ("Briarwood"). On January 13, 1972, Briarwood and LISB entered into a "Supplemental Mortgage Agreement" that severed Parcel III into 62 parcels. Each parcel served as security for 1/62 of the $930,000.00 first mortgage lien held by LISB. This document was also recorded and no tax was paid.

Both the Division and the former State Tax Commission concluded that mortgage recording tax was due on the "Mortgage Severance Modification Agreement" and the "Supplemental Mortgage Agreement".

In the proceeding which followed, this determination was annulled (id., 367 NYS2d at 856). The court first noted that Tax Law §§ 253 and 255 require only that the mortgage tax be applied to a mortgage on the principal debt or obligation or on a new or further indebtedness. The court then stated that parties may exchange old mortgages for new ones without liability for the tax because it is "merely an exchange of one form of indebtedness for another form. The indebtedness remained the same; only the evidence of it changed" (id., 367 NYS2d at 856, 859, citing Matter of Fifth Avenue & 46th Street Corp. v. Bragalini, supra, 165 NYS2d at 312, 316). The court also pointed out that a new mortgage is not created by the fact that different parties were involved in a subsequent transaction than were on the original mortgage (id., 367 NYS2d at 860). On the basis of the foregoing transactions, the court concluded as follows:

> "Thus the transactions involved in the present case should not incur a mortgage recording tax. The State Tax Commission erred when it ruled that since the original mortgage did not expressly provide for the severance of the mortgage, the filing of the subsequent documents incurred the recording tax. Such is not the appropriate rule. Rather, only the recording of a mortgage securing the principal debt or a new indebtedness is subject to the tax. Subsequent filings that consolidate, perfect, or modify the original mortgage without creating new indebtedness do not incur any tax liability. As long as the parties are careful not to extinguish the original debt so as not to create a new indebtedness, no tax should be incurred . . . [citations omitted]" (id., 367 NYS2d at 860).

On the appeal which followed, the judgment of the Appellate Division was affirmed. The Court of Appeals held that:

> "a mere substitution of one mortgage agreement for another, even in combination with a change of mortgagors, is insufficient to create a new mortgage for purposes of section 253 of the Tax Law (citations omitted)" (40 NY2d 856, 387 NYS2d 1002).

Since a new mortgage was not created, the court considered it unnecessary to consider the statutory exemption for supplemental mortgages (id., 387 NYS2d at 1003).

In Matter of Citibank v. State Tax Commn. (supra), Citibank N.A. ("Citibank") loaned money to Joseph Hirsch Sportswear, Inc. The loan was guaranteed by Mr. and Mrs. Lichtman, the principal stockholders of the corporation. As security for the guarantee, the Lichtmans gave Citibank a second mortgage on their residence. The mortgage was recorded and mortgage recording tax was paid.

In May 1978, the Lichtmans decided to sell their residence and acquire a new one. Thereafter, they and Citibank agreed that Citibank would release its mortgage lien on the first residence and, as a substitute, the Lichtmans would provide a mortgage on their new residence.

On May 8, 1978, a satisfaction piece was recorded certifying that the mortgage was paid and consenting to its discharge of record. Subsequently, the Lichtmans purchased a new residence and, on December 22, 1978, they provided Citibank with a mortgage on the new property in the same principal sum as the prior mortgage. When the new mortgage was recorded, Citibank presented an affidavit for exemption from recording tax. As a result, no tax was paid. Thereafter, the Division, and later the State Tax Commission, determined that mortgage recording tax was due on the recording of the new mortgage. In the subsequent

Article 78 proceeding, the court agreed with the State Tax Commission that:

> "because the 1975 mortgage was no longer in existence when the 1978 mortgage went into effect, the latter did not qualify as an additional mortgage under section 255" (id., 470 NYS2d at 921).

The court further noted that the State Tax Commission's determination conforms with the modern judicial interpretation of Tax Law § 255, citing, among other cases, Matter of Sverdlow v. Bates (supra). Accordingly, the court held that the State Tax Commission correctly found that mortgage recording tax was due.

D. With the foregoing cases as a framework, it is determined that the mortgage recording tax was due on the mortgage between LILCO and Citibank dated October 13, 1989.

E. Initially, it is noted that no issue is being taken with petitioner's position that Tax Law § 255 is not the sole basis under the Tax Law for an exemption from mortgage recording tax. As petitioner contends, a mortgage which does not impose a lien is not subject to mortgage recording tax (see, Matter of Fifth Avenue & 46th Street Corp. v. Bragalini, supra; Miller, Hacking a Path Through the New York State Mortgage Tax Jungle, 43 Alb L Rev 37 [1978]).

F. Petitioner argues that the contemporaneous exchange of one instrument for another is not subject to mortgage recording tax. As presented by petitioner, the pertinent consideration is confused. The central consideration is whether the mortgage secures a new or further indebtedness. Thus, in Matter of Sverdlow v. Bates (supra), mortgage recording tax was due because, as a result of the discharge of the old mortgages, the new mortgages secured a new indebtedness. On the other hand, in Matter of Fifth Avenue & 46th Street Corp. v. Bragalini (supra), tax was due only on the increase in indebtedness because the original debt and the original lien continued (id., 165 NYS2d at 318).

G. In this case, the original debt was kept alive through an assignment. However, the original lien for the benefit of NMPC was extinguished by its surrender to LILCO and a new lien for the benefit of Citibank was imposed in its place. Under these circumstances, a mortgage securing a new lien was presented for recording and mortgage recording tax was due.

H. Petitioner contends that the form and timing of the transaction will preserve the lien.

Petitioner submits that, unlike Matter of Citibank v. State Tax Commn. (supra), there is no dispute that the LILCO mortgage exchange was simultaneous; that no change in the mortgaged property occurred; and that the discharge occurred after the new mortgage was in place.

I. Petitioner's argument confuses different points. When the question presented is whether an instrument which changes collateral constitutes a supplemental mortgage within the meaning of Tax Law § 255, an important consideration is whether the new collateral is added before the old collateral is released (see, e.g., Matter of City of New York v. Tully, 55 NY2d 960, 449 NYS2d 181, affg 75 AD2d 246, 429 NYS2d 276; Matter of Citibank v. State Tax Commn., supra). Here, petitioner's sur-reply brief makes it clear that petitioner is not relying on Tax Law § 255. The timing in this instance has no bearing on the point that the transactions in 1989 resulted in the release of one lien and the creation of a new lien.

J. Petitioner's last argument is that changing mortgagors when the mortgages are exchanged does not create a taxable lien. This argument is also rejected under the facts presented herein. There may be an instance where the debt and the mortgage lien were both assigned by the mortgagor without incurring a liability for mortgage recording tax. However, this is not the situation presented here. Here, as noted, the lien imposed by the Old Fourth Mortgage was extinguished by the surrender of the mortgage and a new mortgage was executed. Having chosen the course presented herein, petitioner is liable for the tax (see, Matter of Sverdlow v. Bates, supra).

K. In concluding, it is noted that petitioner has not shown how the decision of the secretary of the PSC (Finding of Fact "17") has any bearing on whether mortgage recording tax is due.

L. The petition of Long Island Lighting Company is denied.

DATED: Troy, New York
June 9, 1994

/s/ Arthur S. Bray
ADMINISTRATIVE LAW JUDGE