STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petitions	:	
of	:	
MIDDLE ISLAND ASSOCIATES	:	DETERMINATION DTA NOS. 810677
for Revision of Determinations or for Refund of Tax on Gains Derived from Certain Real Property Transfers under Article 31-B of the Tax Law.	:	AND 811113

Petitioner, Middle Island Associates, c/o Seymour Katchen, 1800 Walt Whitman Road, Melville, New York 11747, filed petitions[1] for revision of determinations or for refund of tax on gains derived from certain real property transfers under Article 31-B of the Tax Law.

On December 1, 1993 and December 3, 1993, respectively, petitioner by its duly authorized representative, Stuart J. Stein, Esq., and the Division of Taxation by William F. Collins, Esq. (Paul A. Lefebvre, Esq., of counsel) consented to have the controversy determined on submission without hearing. All documentary evidence and briefs were due by March 18, 1994. The Division of Taxation submitted documents on January 11, 1994. Petitioner submitted a brief on February 1, 1994. The Division of Taxation submitted a responding brief on March 16, 1994.[2] Petitioner submitted a reply

[1]A second petition was filed as a result of the Division of Taxation's May 29, 1992 denial of petitioner's September 27, 1991 claim for refund. Petitioner requested that this petition be consolidated with the prior action involving the same issues (DTA No. 810677).

[2]The briefing schedule was revised at the Law Bureau's representative's request because the parties had inadvertently attached the wrong mortgage note to the stipulation. The revised schedule follows: Division's brief was due March 16, 1994; and petitioner's reply brief was due March 30, 1994.

brief on April 1, 1994.[3] After due consideration of the entire record, Winifred M. Maloney, Administrative Law Judge, renders the following determination.

ISSUE

Whether the "additional interest" under the Second Mortgage, as modified, and whether the "fees" under the First Mortgage, as consolidated, constitute allowable costs or whether the Division of Taxation was correct in disallowing the same.[4]

FINDINGS OF FACT

The Division of Taxation ("Division") and petitioner, Middle Island Associates, agreed to a stipulation of facts which has been incorporated into the following Findings of Fact.

Petitioner is a New York general partnership.

In 1986, petitioner purchased "The Shores at Lake Pointe", Lake Pointe Circle, Middle Island, New York, acquiring 360 apartments, 92 of which were aggregated and sold as cooperative apartments.

The 1986 purchase was subject to an existing first mortgage (the "First Mortgage") held by Barclays Bank and further subject to a purchase

money second mortgage (the "Second Mortgage") given by Greater New York Savings Bank ("Greater").

The Second Mortgage and the note which it secures, in addition to provisions for mortgagor's payment of interest, events of default and other customary matters, also provided for permitted sale of condominium units on certain payment terms, as they are sold to individual buyers.

Subsequently, the First Mortgage, initially held by Barclays Bank, was assigned to and

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[3]Petitioner's representative requested additional time in which to file its reply brief. Assistant Chief Administrative Law Judge Daniel J. Ranalli granted an extension until April 1, 1994.

[4]The Division of Taxation and petitioner agreed to stipulated issue(s) on December 2, 1993.

consolidated with an additional first mortgage given by Home Savings Association of Kansas City, F.A. ("Home").[5] This consolidated First Mortgage, in addition to providing for customary terms such as payment of interest, taxes, insurance and other usual matters, also required payments ("fees") to be made on the sale of cooperative units in the aggregate amount of $95,000.00. These payments were not to be applied in reduction of the principal amount of the Second Mortgage,[6] as consolidated.[7]

The transfer to the cooperative housing corporation took place on February 8, 1988.

The Second Mortgage and note were modified in 1989 to provide for permitted sales under a cooperative offering plan, rather than as condominium sales. Under the Second Mortgage and the note, as modified,

Greater was to receive, for each unit sold, (i) a "Release Consideration" which was to be applied in reduction of the principal balance of the Second Mortgage, and (ii) a payment designated as "additional interest" of $10,000.00 for each unit sold. This additional interest was not to be applied in reduction of the Second Mortgage.[8]

The $95,000.00 fee under the First Mortgage, as consolidated, and the $920,000.00

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[5]The "Consolidated and Extension Agreement and Restatement of Mortgage Security Agreement, Assignment of Rents and Financing Statement" between petitioner and Home was executed on July 7, 1987.

[6]The stipulated facts incorrectly reference the Second Mortgage. The correct reference is to the First Mortgage.

[7]Section 16.03 of the Consolidation and Extension Agreement, executed on July 7, 1987, is set forth in Appendix A.

[8]Paragraphs 23 and 24 of the Middle Island Associates to Greater New York Savings Bank Mortgage Note, dated August 14, 1989, is set forth in Appendix D. Appendices B and C contain pertinent excerpts of the Middle Island Associates to Greater New York Savings Bank Mortgage Note, dated December 17, 1986; Mortgage and Security Agreement, dated December 17, 1986; and Mortgage Modification Agreement, dated July 7, 1987.

"additional interest" under the Second Mortgage, as modified, were paid.

On June 6, 1990, petitioner filed a Claim for Refund of Real Property Transfer Gains Tax, as well as finalized Forms DTF-700, 701 and 703 (gains tax questionnaire and schedules). Petitioner requested a refund of $121,397.00 in gains tax based on the updating of Forms DTF-700, 701 and 703 to reflect the sellout of the cooperative project. Petitioner's original Forms DTF-700, 701 and 703 contained only estimates.

In response to petitioner's claim for refund, the Division issued to petitioner a Notice of Determination (L-002151093-7), dated November 5, 1990, asserting real property transfer gains tax due of $20,827.87, plus interest of $3,614.62 and penalties of $7,289.65. The notice contained the following recalculation of tax:

"Consideration

Cash Sales		$ 6,318,000.00
Mortgage Indebtedness		4,800,000.00
Less: Reserve Fund		(10,000.00)
Working Capital Fund		(10,000.00)
Rebates	$815,481.00	
Less: Disallowed (Note 1)	(9,411.00)	(806,070.00)
Adj. Consideration		10,291,930.00
Brokerage Fees Claimed		$ 331,426.00
Less: Disallowed for Advertising		(78,706.00)
Adj. Brokerage		252,720.00
Original Purchase Price Claimed		$ 7,262,865.00
Disallowed:		
(1) Other Acquisition Costs (Note 2)		(219,548.00)
(2) Personal Property		
(a) Lawn Furniture		(8,168.00)
(b) Custom Blinds		(540.00)
(3) Operating Expenses - Office Expense		(3,376.00)
(4) Bank Conversion Fees		
(a) Home Savings Bank (Note 3)		(95,000.00)
(b) Greater N.Y. Savings Bank (Note 4)		(920,000.00)
Adj. O.P.P.		6,016,233.00
Gain Subject to Tax		4,022,977.00
Tax Due		402,297.70
Tax Paid (Note 5)		381,469.83
Balance Due (penalty and interest will be computed from 5/18/89, the date the last unit was transferred)."		$ 20,827.87

Note 2, Note 3 and Note 4, which were referenced in the calculation and accompanied it, contain the rationale for disallowance of certain claimed deductions. The reasons given for these disallowances were:

> "(Note 2) - For other acquisition costs, you claimed $382,693.00, which had been allocated from a total amount of $1,500,759.00. Of the $1,500,759.00, costs of $639,786.00 were incurred as a result of the acquisition in December 1986. The remaining $860,973.00 were costs incurred in July 1987 to re-finance a previous mortgage. Since the $860,973.00 were not costs incurred in acquiring the real property, these costs are being disallowed. Of the $860,973.00, the amount allocated to this project was $219,548.00.
>
> "(Note 3) - The $95,000.00 claimed was a cost also incurred in July 1987 to re-finance the previous mortgage. Since this re-financed mortgage was not obtained to acquire the real property the cost of $95,000.00 is being disallowed.
>
> "(Note 4) - Claimed as part of your costs were payments made to the Greater New York Savings Bank (Bank), which totaled $920,000.00. The payments were made pursuant to the provisions of an agreement dated September 29, 1986, between you and the Bank for a second mortgage to be used in acquiring the real property. The agreement provided for a 'Release Fee' of $10,000.00 to be paid for each unit as it was sold. These release fees were not to be applied in reducing the principle [sic] balance of the loan.
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> "Black's Law Dictionary defines the term 'interest', in part, as payments a borrower pays a lender for the use of the money. Interest is the compensation allowed by law or fixed by the parties for the use or forbearance or detention of money.
>
> "Based on a review of the agreement, we consider the 'Release Fee' to be a form of interest paid on the mortgage with the Bank. Since Section 590.15(c) of the Gains Tax Regulations provides, in part, that interest paid on loans where the proceeds of such loan were used to acquire the real property are not allowable, we are disallowing the $920,000.00 fees as interest incurred as a result of the acquisition loan."

On November 20, 1990, petitioner by its authorized representative, Seymour Z. Katchen, submitted a timely request for a conciliation conference with the Bureau of Conciliation and Mediation Services ("BCMS").

Petitioner submitted a second Claim for Refund of Real Property Transfer Gains Tax in which it requested a refund of $128,708.00 because it had failed to deduct construction interest "on Forms DTF 700, 701 and 702."[9] Petitioner included the following calculation of how the

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[9]In response to an issue involving construction period interest that was first discussed at the conciliation conference on September 23, 1991, and at the Commissioner's recommendation, petitioner filed the second (amended) claim for refund.

construction loan was determined:

1st Mortgage Barclay Bank		$13,500,000.00
2nd Mortgage Greater NY Bank for Savings		9,500,000.00
		$23,000,000.00
Cost of land & building		22,724,683.00
Balance		$ 275,317.00
Add Back		
Downpayment	$150,000.00	
½ commitment fee 1st mortgage	67,500.00	
½ commitment fee 2nd mortgage	95,000.00	312,500.00
Construction loan proceeds		$ 587,817.00
Average prime rate 10/1/86 - 12/31/87	7.75	
Points over prime	2.00	
Interest	9.75	
15 months		$ 73,110.00
10% tax		$ 7,311.00

A BCMS conference was held on September 23, 1991. Petitioner appeared by Seymour Z. Katchen, CPA. Pursuant to the conference, a Conciliation Order (CMS No. 109830), dated January 3, 1992, was issued with the following recomputation of the statutory notice (L002151093):

Determination	$11,678.57
Penalty	Computed at Applicable Rate
Interest	Computed at Applicable Rate

Petitioner filed a petition dated March 27, 1993, which requested a revision of the determination of additional real property transfer gains tax and further requested the amount requested in the refund claim. Petitioner alleged that the Division erred in determining that petitioner's original purchase price for the property was $6,019,609.00 rather than the $7,335,975.00 figure determined by petitioner. Petitioner asserted that the Commissioner based his determination:

> "upon the disallowance of (i) other acquisition costs in the amount of $219,548, (ii) acquisition costs for personal property in the aggregate amount of $8,708, (iii) bank conversion fees in the amount of $95,000 and $920,000, and (iv) construction

period interest in the amount of $73,110."[10]

The Division filed an answer, dated May 15, 1992, denying petitioner's allegations in the petition and stating that the burden of proof is upon petitioner to establish that the determination of the Division is erroneous and/or improper.

In response to petitioner's September 27, 1991 refund claim, the Division issued a refund denial letter dated May 29, 1992. The Division denied the refund in its entirety for the following reason(s):

> "Pursuant to Section 590.16(d) of the Gains Tax Regulations, interest paid during the construction period on loans where the proceeds of such loans were used to make capital improvements may not be included in the original purchase price for real property not undergoing the activities necessary to prepare it for its use. As it appears that only minor improvements and general maintenance was done to this property after its purchase no construction period was established. Therefore construction period interest is not being allowed."

Petitioner filed a petition dated August 13, 1992, which requested a refund of real property transfer gains tax. Petitioner also requested that this action be consolidated with the prior action, filed in March 1992, which involved the same issues. Petitioner alleged that the Division erred in determining that petitioner's original purchase price for the property was $6,019,609.00 rather than the $7,335,975.00 figure determined by petitioner. Petitioner asserted that the Commissioner based his determination:

> "upon the disallowance of (i) other acquisition costs in the amount of $219,548, (ii) acquisition costs for personal property
>
> in the aggregate amount of $8,708, (iii) bank conversion fees in the amount of $95,000 and $920,000, and (iv) construction period interest in the amount of $73,110."

These are the same allegations raised in petitioner's prior petition.

The Division filed an answer dated December 17, 1992. Subsequently, an amended answer was filed on January 6, 1993 due to an error in the original answer. The Division's amended answer denied petitioner's allegations and stated that the burden of proof was upon

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[10] Petitioner's allegation that the construction period interest was disallowed was premature. The issue of construction period interest was not raised in petitioner's June 5, 1990 claim for refund.

petitioner to establish that the determination of the Division was erroneous and/or improper.

The stipulation which petitioner and the Division entered into on December 2, 1993 pertained to the "additional interest" under the Second Mortgage and the "fees" under the First Mortgage, as consolidated.

SUMMARY OF THE PARTIES' POSITIONS

Petitioner argues that the fees under the First Mortgage and under the Second Mortgage are analogous to the points paid to a lender which, under 20 NYCRR 590.39, are allowable costs of co-oping. Petitioner contends that:

> "The fees payable under the First Mortgage amount to almost exactly 2% of the mortgage burden allocated to the co-op project, and the fees under the First Mortgage and under the Second Mortgage become due only upon the happening of an event (sale of co-op units) and not otherwise, they are fixed in amount and they do not increase or decrease depending on the amount of time that the loan is outstanding."

Petitioner also argues that these fees under the First and Second Mortgages "are frequently referred to as 'equity kickers'." It maintains that these equity kickers "were reasonable and necessary expenses to create ownership in cooperative form." Petitioner further maintains that "the fees under the First and Second Mortgages costs were costs incurred in connection with modifying mortgage debt so that a Cooperative Offering Plan would [be] acceptable for filing" with the Attorney General of the State of New York, "a pre-requisite to and an integral part of creating ownership interests in the cooperative form."

Petitioner asserts that the Division, in its Notice of Determination dated November 5, 1990, incorrectly classified the payments as interest. Petitioner argues that the payments are distinguishable from interest payments. Petitioner contends:

> "Interest payments are calculated at a certain rate multiplied by outstanding principal balance of the loan based on the time the loan was outstanding. Interest accrues absolutely, whether or not units are sold, and accrued unpaid interest is due at the maturity of the mortgage. The payments here in question did not have to be calculated, the amount was fixed and the period for which the loan was outstanding as irrelevant."

The Division contends that it properly disallowed the two sets of fees as items of original purchase price.

The Division asserts that the release fees are not fees paid for allowable professional services and "do not qualify as selling expenses." The Division also asserts that these fees are neither "necessary" costs of a cooperative conversion nor are they "customary" costs of a conversion. Rather, these fees are non-allowable selling expenses -- expenses incurred after the conversion of the property to cooperative form.

The Division contends that the release fees "are really pre-payment penalties which the sponsor is incurring as a result of pre-paying a mortgage." The Division argues that:

> "Since 'no release fee payment shall be applied in reduction of the principal balance of the loan' but, instead, is to offset the prepayment premium it is clear that the release fees are no more than a system which allows the mortgagor to pay the prepayment penalty in installments as the units are sold."

Petitioner, in its reply brief, argues that the Division has incorrectly described the release fees as prepayment penalties. Petitioner contends the payments were additional consideration, an equity kicker, paid to the lenders, the timing of which was simultaneous with release of units. Petitioner analogizes these fixed amount equity kickers to the "points paid to lender" allowed under 20 NYCRR 590.39. It maintains that "the only difference between the payments here in question and such points is that the date on which the payment would be due was not fixed."

Petitioner further argues that the equity kickers are an allowable cost which should be taken into account when determining the original purchase price.

CONCLUSIONS OF LAW

A. Tax Law § 1441 imposes a tax on gains derived from the transfer of real property at the rate of 10% of the gain. For purposes of computing the tax, a cooperative conversion is treated as a single transfer; however, the payment of tax is due upon the transfer of shares to individual purchasers pursuant to a cooperative plan (Tax Law § 1442[b]; see, Matter of Mayblum v. Chu, 67 NY2d 1008, 503 NYS2d 316). In computing the amount of tax due as each share is sold, an apportionment of the original purchase price of the real property and total consideration anticipated under such cooperative plan shall be made for each share (Tax Law § 1442[b]).

B. Tax Law § 1440(former [5][a]) defines original purchase price as follows:

"'Original purchase price' means the consideration paid or required to be paid by the transferor; (i) to acquire the interest in real property, and (ii) for any capital improvements made or required to be made to such real property, including solely those costs which are customary, reasonable, and necessary, as determined under rules and regulations prescribed by the tax commission, incurred for the construction of such improvements. Original purchase price shall also include the amounts paid by the transferor for any customary, reasonable and necessary legal, engineering and architectural fees incurred to sell the property and those customary, reasonable and necessary expenses incurred to create ownership interests in property in cooperative or condominium form, as such fees and expenses are determined under rules and regulations prescribed by the tax commission."

C. 20 NYCRR 590.39 states as follows:

"Question: What are the allowable costs of co-oping (or converting property to condominium form) if paid or required to be paid by realty transferor?

"Answer: The following list illustrates costs that are includible in original purchase price as costs to convert property to cooperative or condominium form:

- legal, accounting and engineering fees incurred directly as a result of cooperative or condominium formation and transfer of title to the cooperative corporation
- filing and recording fees
- costs of printing offering plan
- title insurance
- New York City Real Property Transfer Tax paid as a result of conveyance of title to the cooperative corporation
- New York State Real Estate Transfer Tax paid as a result of conveyance to the cooperative corporation
- appraisal fees
- mortgage recording tax on mortgages created as a result of conveyance of title to the cooperative corporation
- mortgage commitment fees
- points paid to lender
- the cost of 'buying down' the interest rate on co-op loans to purchasers
- the cost of 'buying out' nonpurchasing tenants
- amounts paid to relocate nonpurchasing tenants"

D. Original purchase price includes those "customary, reasonable and necessary expenses incurred to create ownership interests in property in cooperative form" (Tax Law § 1440[5][a]). 20 NYCRR 590.39 contains an illustrative list of cooperative or condominium conversion costs includible in the original purchase price. In Matter of 415 C.P.W. Co. (Tax Appeals Tribunal, March 2, 1989), the Tribunal discussed the meaning of various terms in Tax Law § 1440(5)(a). The Tribunal defined "expenses" as "something expended to secure a benefit or bring about a result" (Matter of 415 C.P.W. Co., supra).

E. Petitioner argues that the fees under the First Mortgage and the Second Mortgage costs were incurred in modifying the mortgage debt so that a cooperative offering plan would be acceptable for filing, a prerequisite to the creation of a cooperative form of ownership. It further argues that the First Mortgage fees of $95,000.00 and the Second Mortgage costs ("additional interest") of $920,000.00 represent costs which were necessary for the creation of the cooperative form, "not carrying the ownership of the cooperative form." Petitioner has also described these fees as "equity kickers", extra profit, paid to the lenders for the modification of the loans in order to permit conversion to cooperative ownership. Petitioner contends these payments are identical to "points paid to lender" which is allowed under 20 NYCRR 590.39. The only difference, petitioner argues, is that the due date of these payments is not fixed.

The Division contends that both the First Mortgage fees and the Second Mortgage costs ("additional interest"/"release fees") are expenses incurred after the conversion of the property to cooperative form (i.e., selling expenses) and as such are not allowable expenses. The Division also argues that the "additional interest"/"release fees" are prepayment penalties which were payable even if the buildings were not converted to cooperative form. Furthermore, the Division maintains that both sets of fees are products of petitioner's personal financing and are not necessary and customary costs of converting the property to cooperative form.

F. I find that the First Mortgage fees of $95,000.00 are allowable cooperative conversion costs. While these fees may not have been customary or ordinary, they were necessary to effectuate the cooperative conversion. Section 16.03 of the First Mortgage, as refinanced on July 7, 1987, entitled "Transfer to Cooperative Corporation", contains language pertaining to these payments in subsection K. In order to gain the lender's approval for the transfer to the cooperative corporation, petitioner/borrower had to comply with all of the provisions of Section 16.03. Although the fees were payable at the time each co-op unit was sold rather than at the time of the transfer to the cooperative corporation, these payments do not become nonallowable selling expenses. The First Mortgage fees of $95,000.00 were necessary to create ownership interests in property in cooperative form.

G. Petitioner's argument that the Second Mortgage fees are costs of a cooperative conversion is without merit. The Division is correct that these fees ("additional interest") are pre-payment penalties. Review of the pertinent paragraphs of the Greater mortgage and mortgage note contained in Appendices B, C and D indicate that petitioner/borrower was required to pay a premium (pre-payment penalty) if the mortgage was pre-paid regardless of whether the property was converted to condominium or cooperative form. The pre-payment penalty due from the borrower would be reduced by any payment of release fees/additional interest.[11] These fees were not to be applied to reduce the principal balance. These fees were neither incurred to acquire the property nor were they expenses to create an ownership interest in cooperative form. Rather, they were an expense of borrowing funds.

The Division argues that the mortgage pre-payment penalty is similar to interest and should be treated the same way. The Division is correct that the fees are similar to interest. It is clear that Greater considered these payments as additional interest. The provisions of the August 14, 1989 mortgage note reclassified the release fees as additional interest. For

gains tax purposes, acquisition interest and similar items are not allowable expenses for determining the original purchase price of a property (see, 20 NYCRR 590.15[c]; Matter of Mattone v. Dept. of Taxation & Fin., 144 AD2d 150, 534 NYS2d 478; Matter of 645 East 11th Street Assoc., Tax Appeals Tribunal, January 21, 1993).

It should be noted that petitioner's classification of the release fee payments as equity kickers and its reliance on Matter of V & V Properties (Tax Appeals Tribunal, July 16, 1992) is misplaced. The release fees/additional interest payments are not equity kickers. These fees are pre-payment penalties which are paid to the lender, who does not have an ownership interest in the property.

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[11]See, Greater Mortgage Note, dated December 17, 1986, paragraph 25; Greater Mortgage and Security Agreement, dated December 17, 1986, paragraph 35; Greater Mortgage Note, dated August 14, 1989, paragraph 24.

The $920,000.00 in additional interest under the Second Mortgage does not constitute an allowable cost. The Division correctly disallowed this cost.

H. The petitions of Middle Island Associates are granted to the extent indicated in Conclusion of Law "F"; the Notice of Determination and disallowance of the claim for refund are to be modified in accordance therewith; and, in all other respects, the petitions are denied.

DATED: Troy, New York
September 22, 1994

/s/ Winifred M. Maloney
ADMINISTRATIVE LAW JUDGE

APPENDIX A

"Consolidation and Extension Agreement and Amendment and Restatement of Mortgage, Security Agreement, Assignment of Rents and Financing Statement executed July 7, 1987 by Middle Island Associates, mortgagor, and Home Savings Association of Kansas City, mortgagee ('First Mortgage').

"ARTICLE XVI

Transfer of Mortgaged Property

* * *

"Section 16.03 Transfer to the Cooperative Corporation

"Borrower's right to transfer its interest to the Cooperative Corporation pursuant to Section 16.02(b) hereof shall be subject to prior receipt and approval by Lender in the exercise of its reasonable discretion of the following:

* * *

"(K) an assumption agreement duly executed by the Cooperative Corporation evidencing its assumption of all of the obligations of Borrower hereunder and under the Note and Loan Documents, granting Lender a prior perfected Lien and security interest in the proceeds from the sale of the stock of the Cooperative Corporation and the proprietary leases, and Borrower's agreement to pay Lender a fee as shares in the Cooperative Corporation are sold from time to time, such fee to be paid in installments upon the sale of each unit owned by the Cooperative Corporation and calculated by multiplying $95,000 times a fraction, the numerator of which is

one (1) and the denominator of which is the number of units in the cooperative . . . ."

APPENDIX B

"Middle Island Associates to The Greater New York Savings Bank Mortgage Note, dated December 17, 1986 ('Second Mortgage').

* * *

"24. It is agreed that the ownership, control, management and operation of the Premises covered by the Mortgage securing this Note by Maker of which Edward Lapidus and/or David Glaser are the controlling partners, ('The Principals') is a material inducement to the Payee to make the Loan evidenced by this Note and secured by the Mortgage and that the control, management and operation of the Premises by others, who or which does not in the Payee's sole opinion possess the business or managerial acumen and experience of the Principals will seriously endanger the security represented by the Mortgage. Accordingly, the whole debt evidenced by this Note and secured by the Mortgage shall immediately become due and payable at the option of the Payee at any time title to, control, management or operation of the Premises or any part thereof is transfereed [sic] to any entity not controlled, owned or operated by Principals. Notwithstanding the foregoing, if a valid condominium plan is declared effective for the Premises, Maker may convert the Premises into condominium ownership and the Payee will release from the lien of the Mortgage pro rata, each condominium unit sold upon said sale provided Maker is not in default of the Lien Instruments and provided the Payee receives as consideration for the release of each Unit from the lien of the Mortgage, the following: (i) an amount equal to the product obtained by multiplying (x) the percentage of common interest allocated to the unit, as calculated in accordance with all declarations of condominium to be filed for the Premises, being released by, (y) $9,500,000.00 by (z) 110% ('Release Consideration'); and (ii) $10,000.00 ('Release Fee'). All payments of Release Consideration shall be applied in reduction of the Principal balance of the loan evidenced hereby, however, no

Release Fee payment shall be applied in reduction of the principal balance of the Loan. At the time of each such release the Payee's Attorneys shall be paid a legal fee of $100.00 for each such release prepared plus an attendance fee, if an attendance is required. The lien of the Mortgage shall continue to encumber all condominium units which have not been released, until the principal balance of the loan evidenced hereby has been repaid in full, together with all interest accrued thereon, and payment of all sums and fees due to the Payee under the Lien Instruments have been received, including payment of Release Fees totalling $3,600,000.00, notwithstanding whether the Principal balance of the loan has been repaid in full.

"Notwithstanding the foregoing, provided the Maker is not in default of the Note, the Mortgage or the Lien Instruments and provided a valid declaration of condominium is filed for the Premises, Payee shall release from the lien of the Mortgage the clubhouse, swimming pool, tennis courts and other homeowner association properties, without the payment of any Release Consideration or Release Fee provided the lien of the Mortgage is spread to cover the percentage interest in the common areas appurtenant to each condominium unit.

"25. Maker may prepay the entire Principal balance of this Note on any payment date provided Maker additionally pays as a premium for the privilege of so prepaying $3,600,000.00 less any Release Fees paid by Maker and received by Payee.

* * *

"Mortgage and Security Agreement dated December 17, 1986 between Middle Island Associates and The Greater New York Savings Bank

* * *

"Rider #1

Rider to Mortgage

* * *

"33. It is agreed that the ownership, control, management and operation of the Premises covered by this Mortgage securing the Note by Mortgagor of which Edward Lapidus and/or David Glaser are the controlling partners, ('The Principals') is a material inducement to the Mortgagee to make the Loan evidenced by the Note and secured by this Mortgage and that the control, management and operation of the Premises by others, who or which does not in the Mortgagee's sole opinion possess the business or managerial acumen and experience of the Principals will seriously endanger the security represented by this Mortgage. Accordingly, the whole debt evidenced by the Note and secured by this Mortgage shall immediately become due and payable at the option of the Mortgagee at any time title to, control, management or operation of the Premises or any part thereof is transferred to any entity not controlled, owned or operated by Principals. Notwithstanding the foregoing, if a valid condominium plan is declared effective for the Premises and the declaration of condominium is filed, Mortgagor may convert the Premises into condominium ownership and the Mortgagee will release from the lien of this Mortgage pro rata, each condominium unit sold upon said sale provided Mortgagor is not in default of the Lien Instruments and provided the Mortgagee receive as consideration for the release of each Unit from the lien of this Mortgage, the following: (i) an amount equal to the product obtained by multiplying (x) the percent of common interest allocated to the unit, as calculated in accordance with all declarations of condominium to be filed for the Premises, being released by, (y) $9,500,000.00 by (z) 110% ('Release Consideration'); and as additional consideration (ii) $10,000.00 ('Release Fee'). The lien of this Mortgage shall continue to encumber all units which have not been released, until this principal balance of the Loan has been repaid in full, together with all interest accrued thereon, and payment of all sums and fees

due to the Mortgagor under the Lien Instruments have been received, including payment of Release Fees totalling $3,600,000.00, notwithstanding whether the principal balance of the Loan has been repaid in full. All payments of Release Consideration shall be applied in reduction of the principal balance of the loan evidenced by the Note and secured by this Mortgage ('Loan'). At the time of each such release the Mortgagee's Attorneys shall be paid a legal fee of $100.00 for each release prepared plus an attendance fee, if an attendance is required. All payments of Release Fees shall be paid to Mortgagee and retained by it as a fee and not in reduction of the Principal balance or payment of interest. Notwithstanding the foregoing, provided the Mortgagor is not in default of the Note, this Mortgage or the Lien Instruments and provided a valid declaration of condominium is filed for the Premises, Mortgagee shall release from the lien of this Mortgage the clubhouse, swimming pool, tennis courts and other homeowner association properties, without the payment of any Release Consideration or Release Fee provided the lien of this Mortgage is spread to cover the percentage interest in the common areas appurtenant to each condominium unit.

* * *

"35. Mortgagor may prepay the entire Principal of the loan evidenced by the Note and secured hereby on any payment date provided that additionally Mortgagor pays, as a premium for the privilege of so prepaying, $3,600,000.00 less the aggregate of the Release Fees paid by Mortgagor and received by Mortgagee."

APPENDIX C

"Mortgage Modification Agreement dated July 7, 1987 between Middle Island Associates and The Greater New York Savings Bank

* * *

"4. Upon execution of the Splitter, the Coop Premises and the swimming pool clubhouse, tennis courst [sic] and any other property conveyed to the homeowner's association shall be released form [sic] the mortgage lien encumbering the Coop Premises and in substitution thereof Obligor shall grant Obligee a security interest in all proprietary leases and shares of stock issued by the Coop ('Coop Collateral'). The individual proprietary leases and the appurtenant shares of the Coop constituting the Coop Collateral shall be released from the lien on and security interest granted in the Coop Collateral upon the sale of the respective units appurtenant thereto upon the payment of the Release Fees, Release Consideration and attorney fees in the manner and as calculated as provided in paragraph 24 of the Note and paragraph 33 of the Mortgage as amended hereby.

"5. Paragraph 33 of the Mortgage is amended to read:

"It is agreed that the ownership, control, management and operation of the Premises covered by this Mortgage securing the Note by Mortgagor of which Edward Lapidus and/or David Glaser are the controlling partners, ('The Principals') is a material inducement to the Mortgagee to make the Loan evidenced by the Note and secured by this Mortgage and that the control, management and operation of the Premises by others, who or which does not in the Mortgagee's sole opinion possess the business or managerial acumen and experience of the Principals will seriously endanger the security represented by this Mortgage. Accordingly, the

whole debt evidenced by the Note and secured by this Mortgage shall immediately become due and payable at the option of the Mortgagee at any time title to, control, management or operation of the Premises or any part thereof is transferred to any entity not controlled, owned or operated by Principals. Notwithstanding the foregoing, if a valid condominium plan or cooperative offering plan is declared effective for the Premises and the declaration of condominium is filed, Mortgagor may convert the Premises into condominium or cooperative ownership and the Mortgagee will release from the lien of this Mortgage pro rata, each condominium unit or cooperative unit sold upon said sale provided Mortgagor is not in default of the Lien Instruments and provided the Mortgagee receive as consideration for the release of each Unit from the lien of this Mortgage, the following: A: for a condominium: (i) an amount equal to the product obtained by multiplying (x) the percentage of common interest allocated to the unit being released by, (y) the lien of this Mortgage, as split, encumbering the portion of the Premises not conveyed to the Coop by (z) 110% ('Release Consideration'); and as additional consideration (ii) $10,000.00 ('Release Fee'); B: for the Coop: (i) an amount equal [to] the product obtained by multiplying (x) the ratio the numerator of which is the number of shares allocated to the unit being released and the denominator is the total number of Coop shares by (y) the lien of the Mortgage, as split, securing the Coop Collateral, by (z) 110% ('Release Consideration'); and as additional consideration (ii) $10,000.00 ('Release Fee'). The lien of this Mortgage shall continue to encumber all units which have not been released, until this principal balance of the loan secured hereby ('Loan') has been repaid in full, together with all interest accrued thereon, and payment of all sums and fees due to the Mortgagor under the Lien Instruments have been received, including payment of Release Fees totalling $3,600,000.00, notwithstanding whether the principal balance of the Loan has been repaid in full. All payments of Release Consideration shall be applied in reduction of the principal balance of the loan evidenced by the Note and secured by this Mortgage ('Loan'). At the time of each such release the Mortgagee's Attorneys shall be paid a legal fee of $100.00 for each release prepared plus an attendance fee, if an attendance is required. All payments of Release Fees shall be paid to

Mortgagee and retained by it as a fee and not in reduction of the Principal balance or payment of interest. Notwithstanding the foregoing, provided the Mortgagor is not in default of the Note, this Mortgage or the Lien Instruments and provided a valid declaration of condominium is filled [sic] for the Premises, Mortgagee shall release from the lien of this Mortgage the clubhouse, swimming pool, tennis courts and other homeowner association properties, without the payment of any Release Consideration or Release Fee provided the lien of this Mortgage is spread to cover the percentage interest in the common areas appurtenant to each condominium unit.

* * *

"7. Paragraph 24 of the Note is amended to read as follows:

"It is agreed that the ownership, control, management and operation of the Premises covered by the Mortgage securing this Note by Maker of which Edward Lapidus and/or David Glaser are the controlling partners, ('The Principals') is a material inducement to the Payee to make the Loan evidenced by this Note and secured by the Mortgage and that the control, management and operation of the Premises by others, who or which does not in the Payee's sole opinion possess the business or managerial acumen and experience of the Principals will seriously endanger the security represented by the Mortgage. Accordingly, the whole debt evidenced by this Note and secured by the Mortgage shall immediately become due and payable at the option of the Payee at any time title to, control, management or operation of the Premises or any part thereof is transfereed [sic] to any entity not controlled, owned or operated by Principals. Notwithstanding the foregoing, if a valid condominium plan or cooperatvie [sic] offering plan is declared effective for the Premises, Maker may convert the Premises into condominium ownership or cooperatvie [sic] ownership and the Payee will release from the lien of the Mortgage pro rata, each condominium unit sold or cooperative unit upon said sale provided Maker is not in default of the Lien Instruments and provided the Payee receives as

consideration for the release of each Unit from the lien of the Mortgage, the following: A for a condiminium [sic]: (i) an amount equal to the product obtained by multiplying (x) the percentage of common interest allocated to the unit being released by, (y) the lien of the Mortgage, as split, encumbering that portion of the Premises not conveyed to the Coop by (z) 110% ('Release Consideration'); and (ii) $10,000.00 ('Release Fee'); B for the Coop: (i) an amount equal [to] the product obtained by multiplying (x) the ratio the numerator of which is the number of shares allocated to the unit being released and the denominator is the total number of Coop shares, by (y) the lien of the Mortgage, as split, encumbering the Coop Collateral, by (z) 110% ('Release Consideration'); and as additional consideration (ii) $10,000.00 ('Release Fee'). All payments of Release Consideration shall be applied in reduction of the Principal balance of the loan evidenced hereby, however no Release Fee payment shall be applied in reduction of the principal balance of the Loan. At the time of each such release the Payee's Attorneys shall be paid a legal fee of $100.00 for each such release prepared plus an attendance fee, if an attendance is required. The lien of the Mortgage shall continue to encumber all condominium units or cooperative units which have not been released, until the principal balance of the loan evidenced hereby ('Loan') has been repaid in full, together with all interest accrued thereon, and payment of all sums and fees due to the Payee under the Lien Instruments have been received, including payment of Release Fees totalling $3,600,000.00, notwithstanding whether the Principal balance of the loan has been repaid in full. Notwithstanding the foregoing, provided the Maker is not in default of the note, the Mortgage or the Lien Instruments and provided a valid declaration of condominium is filed for the Premises, Payee shall release from the lien of the Mortgage the clubhouse, swimming pool, tennis courts and other homeowner association properties, without the payment of any Release Consideration or Release Fee provided the lien of the Mortgage is spread to cover the percentage interest in the common areas appurtenant to each condominium unit."

APPENDIX D

"Middle Island Associates to The Greater New York Savings Bank Mortgage Note, dated August 14, 1989

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"23. It is agreed that the ownership, control, management and operation of the Premises covered by the Mortgage securing this Note by Maker of which Edward Lapidus and/or David Glaser are the controlling partners, ('The Controlling Principals') is a material inducement to the Payee to make the Loan evidenced by this Note and secured by the Mortgage and that the control, management and operation of the Premises by others, who or which does not in the Payee's sole opinion possess the business or managerial acumen and experience of The Controlling Principals will seriously endanger the security represented by the Mortgage. Accordingly, the whole debt evidenced by this Note and secured by the Mortgage shall immediately become due and payable at the option of the Payee at any time title to, control, management or operation of the Premises or any part thereof is transfered to any entity not controlled, owned or operated by The Controlling Principals. Notwithstanding the foregoing, provided Maker is not in default of the Mortgage securing this Note, this Note or under the Lien Instruments, upon the approval of a cooperative offering plan for the Premises by the Bank, which approval shall not be unreasonably withheld, and such plan is declared effective for the Premises, Maker may convert the Premises to cooperative ownership and the Payee will release from the lien of the Mortgage securing this Note the Premises secured hereby including any property conveyed to a Home Owners Association in conjunction with said offering plan, provided Maker pledges and grants a security interest in each of the 268 cooperative units and the proprietary leases and shares of stock in the cooperative corporation to be formed appurtenant thereto. In connection therewith, Maker shall execute such instruments as are

required in the opinion of Payee's counsel to perfect Payee's security interest in such collateral including but not limited to a substitute note, security agreement, assignment of leases, stock powers and U.C.C. financing statements. In addition, Payee shall possess all proprietary leases and shares of stock in the cooperative corporation until the Release Consideration and Additional Interest, as hereinafter deined, for the appurtenant unit is received by Payee. Thereafter, Payee shall deliver a release for each cooperative apartment and the proprietary lease and shares of stock in the cooperative corporation appurtenant thereto upon receipt of payment from Maker of the following: (i) an amount equal to the product obtained by multiplying (x) a fraction the numerator of which is the number of shares allocated to each unit to be released and the denominator of which is the total number of shares for all 268 units consisting the cooperative corporation by (y) $8,172,776.84 by (z) 1.25% ('Release Consideration'); and (ii) $10,000.00 ('Additional Interest'). All payments of Release Consideration shall be applied in reduction of the Principal balance of the loan evidenced hereby, however no Additional Interest payment shall be applied in reduction of the Principal balance of this Note. At the time of each such release the Payee's Attorneys shall be paid a legal fee of $50.00 for each such release prepared plus an attendance fee, if an attendance is required. The lien of the Security Agreement to be executed in substitution hereof upon release of the Premises as described hereinabove shall continue to encumber all cooperative units which have not been released, until the Principal balance of this Note has been repaid in full, together with all interest accrued thereon, and payment of all sums and fees together with all interest accrued thereon, and payement [sic] of all sums and fees due to the Payee under the Lien Instruments or any instruments executed in substitution hereof have been received, including payment of Additional Interest totalling $2,680,000.00, notwithstanding whether the Principal balance of this Note has been repaid in full.

"24. Maker may prepay the entire the [sic] Principal balance of this Note on any payment date provided Maker additionally pays as a premium for the privilege of so prepaying $2,680,000.00

less any payments of Additional Interest paid by Maker and received by Payee."