March 23, 2021

The Honorable Andrew M. Cuomo
Governor of New York State
NYS Capitol Building
Albany, NY 12224

The Honorable Robert Ortt
Senate Republican Leader
Legislative Office Building, Room 315
Albany, NY 12247

The Honorable Carl E. Heastie
Speaker
New York State Assembly
Legislative Office Building, Room 932
Albany, NY 12248

The Honorable William A. Barclay
Minority Leader
New York State Assembly
Legislative Office Building, Room 933
Albany, NY 12248

The Honorable Andrea Stewart-Cousins
Temporary President & Majority Leader
New York State Senate
Legislative Office Building, Room 907
Albany, NY 12247

Re: Proposed Tax and Recording of Mezzanine Debt and Preferred Equity Investments

Dear Governor Cuomo, Speaker Heastie, Majority Leader Stewart-Cousins, Leader Barclay, and Leader Ortt:

The undersigned organizations are writing to you to oppose companion mezzanine debt tax and preferred equity tax legislation included in Senate and Assembly budget proposals.[1] We believe the enactment of these taxes would exacerbate the affordable housing challenges in New York and effectively increase rents on low to middle-income New York families and small businesses, at a time when they can least bear that increase.

Together, our groups represent commercial and multifamily real estate owners, a broad range of lenders that make loans to finance commercial and multifamily properties, and other stakeholders. The commercial/multifamily real estate finance market is an essential and integral part of the economy of the State of New York that provides the financing for properties that enables the state's many small businesses to operate and supports the multifamily rental housing that 2.2 million New York households call home.

The mezzanine debt and preferred equity proposed tax provisions would require that such investments (not secured by land) be recorded in county land records along with any related mortgage and would require the payment of a recording tax.

The tax will increase the cost of credit.

Mezzanine debt and preferred equity expand the availability of credit for all types of properties, including hotels, retail, office, apartments, manufactured housing. Mezzanine and preferred equity capital availability is critical to many of New York's owners and developers, both large and small, who rely on this type of financing to build and operate their properties. Increasing the cost and availability of mezzanine and preferred equity capital will directly impact the development of both affordable and market-rate apartments. Owners of other commercial real estate categories such as office and hotel will also be deprived of critical financing capital over and above what "conventional" lenders make available, which might lead to additional stress in the commercial real estate industry at a time when the average owner (and tenant) are already suffering.

A traditional mortgage is secured by a lien on the property itself. The mezzanine or preferred equity holder is able to step into the shoes of the original borrower if the original borrower becomes financially unsound. By doing so, the mezzanine/preferred equity lenders will typically provide critical capital to "rescue" the previously ailing property from disrepair which is clearly beneficial to the tenants. This is different from a senior mortgage lender who would usually foreclose and sell the property in the event of a default. Like all large commercial loans, these transactions are between sophisticated lenders and borrowers who understand the risks and rewards of the ownership structures and related financings.

Credit availability will be crucial in the months and years ahead as New York businesses and buildings attempt to emerge from the pandemic. New York building owners have seen catastrophic drops in revenue and will need cash to cover expenses and upgrade properties in a post-COVID world. When funding is unavailable from other sources, mezzanine and preferred equity lenders step up to help finance buildings. The proposed tax only makes borrowing more expensive and will put even more pressure on building owners as they recover.

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[1] See NY Assembly Bill A3009 – B, part VV, and NY Senate Bill S2509 – B, part SS (March 13, 2021).

The new tax burden will fall on hard-hit building owners, renters, and small businesses.

This provision is estimated to impose approximately $171 million in new taxes. While those taxes will be paid directly by building owners, the cost of those additional taxes will be effectively distributed throughout the economy, including:

- **Building owners** will bear some of that $171 million tax. This will be a substantial burden as many building owners have already suffered millions of dollars in lost rental income from families and small business tenants that have been unable to fully pay their rent and may be continuing to experience rent shortfalls. Furthermore, building owners have also faced increased costs in order to maintain a healthy environment during the pandemic. This dual impact has been exacerbated by eviction moratoriums.

- **Tenants and small businesses** will also bear a substantial portion of the $171 million tax. The proposed new tax will increase the cost of owning and operating buildings. For building owners to stay afloat, much of that increased costs will necessarily be passed down to the tenants in the form of higher rents. In the midst of a pandemic and housing affordability crisis, this tax will make housing more expensive.

  Many of the renting families and small businesses that will bear the burden of the tax-driven increase in rents are already struggling to pay even current rents because of the impacts of the pandemic. Increasing costs on renters will make it even harder for renters and small businesses to recover.

In sum, the mezzanine debt and preferred equity tax provisions will impose a $171 million burden on building owners, renting families, and small businesses – just at the time they and the economy will be working toward recovery.

The potential tax revenue does not justify the burdens it imposes on those already hit hard by the pandemic.

We recognize that many states are struggling with declining revenue amid the pandemic. However, the changing fiscal scenario and increased federal aid to states reduce the need for a punitive tax on renters and small businesses. The State of New York is receiving substantial federal assistance under the American Rescue Plan. We encourage the State to first analyze the funds it will receive and how those funds may be used to backfill lost revenue during the pandemic, while also helping the State to balance its budget. In addition, according to the monthly State Cash Report by New York State Comptroller Thomas P. DiNapoli, tax collections through February were $758.4 million higher than forecasted. In fiscal year 2021, state tax revenues totaled $75 billion at the end of February. Moreover, it was widely reported earlier this week that, following meetings with legislative staff, the Director of the Division of the Budget said that they have identified over $5 billion in resources available that would negate the need for "any significant level in tax increases."

As a result, there is no fiscal need sufficient to justify this new tax burden on a sector acutely affected by the pandemic. Accordingly, we strongly recommend that these provisions be struck from the budget bills.

The potential unintended impacts of the new tax have not been vetted and considered.

The mezzanine debt and preferred equity tax provisions are unprecedented and could have far-reaching unintended consequences. Given that this policy proposal has been introduced in stand-alone legislation in previous years without the benefit of a public hearing, we believe that, at a minimum, the Legislature should hold hearings to evaluate these provisions and consider potential unintended impacts.

Indeed, it is disheartening to see the Senate and the Assembly hastily attempting to implement a tax proposal of this magnitude without evaluating the potential effects on the macro economy, small businesses, and consumers, in particular. Such a review is essential given the economic upheaval caused by the current health crisis, which has hit renters and businesses especially hard. Now is not the time to increase costs on renters and owners by inhibiting the real estate finance industry's ability to serve as a vital economic engine in the recovery of New York's economy.

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We appreciate your consideration of our views. A tax on mezzanine debt and preferred equity is a tax on renters and small businesses. We urge the State's leadership to reconsider raising costs for those recovering from the pandemic.

Respectfully,

Mortgage Bankers Association

American Council of Life Insurers

Building & Construction Trades Council of Greater New York

CRE Finance Council

Empire State Mortgage Bankers Association

International Council of Shopping Centers

Life Insurance Council of New York, Inc.

Mortgage Bankers Association of New York, Inc.

Real Estate Board of New York

New York Mortgage Bankers Association

New York State Association of Realtors, Inc.

The Business Council of New York

The Real Estate Roundtable