

One Minute Memo[®]



District of Columbia Issues Notice Regarding Tax Treatment of Mortgage Refinancings and Modifications

On January 6, 2012, the District of Columbia Office of Tax and Revenue issued an official notice relating to the recent controversy over the recordation tax treatment of refinancings and modifications of security interest instruments. Based on the notice, the Recorder of Deeds shall tax any instrument evidencing a security interest in real property, and reflecting a refinance or modification, on the difference between the face amount of such instrument and the outstanding principal amount of existing debt under the prior security interest instrument, provided, of course, that the full amount of any tax due on the prior instrument was paid or the prior instrument was exempt from taxation. The Recorder of Deeds has established a process for taxpayers to substantiate and claim credits for those taxes previously paid on any security interest instruments relating to a refinancing or modification.

The Recorder of Deeds generally deems a refinance to consist of a new loan that is used to pay off and extinguish an existing loan (whether with the original or a new lender) and is secured by the same property (and additional property) as in the original loan. The sale or assignment of a security interest instrument from one lender to another on the secondary market, where there are no changes in the terms or conditions provided in the instrument and the borrower has taken no steps to refinance, is not considered a refinance by the Recorder of Deeds. The Recorder of Deeds deems a modification to have occurred when the terms of a pre-existing security interest instrument are changed in some manner, but the obligation imposed by the preexisting instrument is preserved and the loan secured by that instrument it is not paid off, extinguished or retired. Pursuant to District of Columbia law, a supplemental instrument that modifies a prior recorded instrument without additional consideration is not taxed. However, if a modification increases the total amount of the debt secured, tax is imposed on the increase in the face amount of the modification over the face amount of the pre-existing instrument, provided that any tax due with respect to the pre-existing instrument was paid or the pre-existing instrument was exempt. Any transaction concerning residential real property containing five (5) dwelling units or less, and for which a proper Security Affidavit is on file, is exempt from tax under District of Columbia law.

The Council of the District of Columbia is currently considering legislation to address the recordation tax treatment of transactions discussed in the notice, and the enactment of such legislation may affect the taxation of the transactions addressed by the notice. As currently drafted, the proposed legislation provides, as does the notice, that the Recorder of Deeds shall tax any instrument with respect to a refinancing or modification on the difference between the face amount of such instrument and the outstanding principal amount of existing debt under the prior security interest instrument. At a first hearing on the proposed legislation, the Attorney General of the District of Columbia testified that it was the position of the Mayor under current law that the full balance of any refinancing should be taxed at recordation. The proposed legislation has not been moved out of the District of Columbia Council Committee on Finance and Revenue, but is expected to be taken up early in 2012.

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