

Department of Legislative Services
 Maryland General Assembly
 2007 Session

FISCAL AND POLICY NOTE
Revised

House Bill 580 (Delegate McIntosh and the Speaker, *et al.*)
 (By Request – Administration)

Environmental Matters

Judicial Proceedings

Ground Rents - Registry of Properties Subject to Ground Leases

This Administration bill establishes a registry of ground leases in the State Department of Assessments and Taxation (SDAT).

The bill applies to residential property used, intended to be used, or authorized to be used for four or fewer dwelling units. The bill does not apply to property leased for other specified uses.

Fiscal Summary

State Effect: Special fund expenditures could increase by approximately \$193,100 in FY 2008 to register ground rents. Special fund revenues could increase by approximately \$154,400 in FY 2008. Out-years reflect annualization, inflation, and the period during which ground lease holders may register.

(in dollars)	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012
SF Revenue	\$154,400	\$178,800	\$203,100	\$15,600	\$0
SF Expenditure	193,100	125,600	128,700	72,900	76,400
Net Effect	(\$38,700)	\$53,200	\$74,400	(\$57,300)	(\$76,400)

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect

Local Effect: The bill would not materially affect the finances or operations of Baltimore City.

Small Business Effect: A small business impact statement was not provided by the Administration in time for inclusion in this fiscal note. A revised fiscal note will be issued when the Administration's assessment becomes available.

Analysis

Bill Summary: SDAT is required to maintain an online registry of landlords and properties subject to ground leases. A ground lease holder must register a ground lease by submitting a registration form containing specified information. The fee for registration per ground lease holder is \$10 for the first ground lease and for each additional ground lease, \$3 if registered before October 1, 2008, \$4 if registered between October 1, 2008 and September 30, 2009, and \$5 on or after October 1, 2009.

SDAT must register a ground lease when it receives a registration form and the fee for each ground lease.

After registration, the ground lease holder must promptly notify SDAT of • specified name and address changes; • a redemption of the ground lease; and • any other information required by SDAT. A landlord must pay a \$5 fee for each notification.

A ground lease holder must register a ground lease by September 30, 2010. If the ground lease holder is under a legal disability at the expiration of this period, the ground lease holder has two years after its removal to apply to register. If SDAT is unable to register a ground lease for which a form and fee have been submitted, it must notify the ground lease holder, within 30 days of processing the registration form, of any information needed by SDAT to complete the registration. The ground lease holder has up to 30 days to supply the needed information.

If the ground lease holder fails to register within the time requirements, the ground lease holder's reversionary interest is extinguished and ground rent is no longer payable. SDAT is then required to issue a ground lease extinguishment certificate to the tenant. The extinguishment conclusively vests a fee simple title in the leasehold tenant, free and clear of any and all right, title, or interest of the ground rent holder, the ground rent holder's lienholders, and any person claiming by, through, or under the ground rent holder when the certificate is accepted for recording in the land records.

To the extent that a ground lease's extinguishment creates income for the leasehold tenant, that income may not be considered in the calculation of information for the purposes of determining eligibility for any State or local program.

If a ground lease holder's legal disability is removed after a ground lease is extinguished because the ground lease holder failed to register the ground lease:

- if the ground lease extinguishment certificate has been recorded, the ground lease holder is entitled to receive the redemption value from the former leasehold tenant and has no claim on the property; and
- if the certificate has not been recorded, the ground lease holder may reinstate the ground lease by registering it with SDAT within two years after the legal disability has been removed but is not entitled to ground rent for the period of the legal disability.

If a ground lease has been extinguished under these provisions and a ground lease extinguishment certificate has not been recorded, the buyer of the property may apply to SDAT for a certificate and may file the certificate in the land records. Once the ground lease extinguishment certificate has been filed, the buyer may not be required to pay any security or amount into an escrow account for the extinguished ground lease.

SDAT must work with the State Archives to coordinate the recordation, indexing, and linking of ground leases under the bill.

SDAT is required to credit all fees collected under the bill to its expedited processing fund and must adopt regulations to carry out the bill's registration requirements. The fees must help defray the costs of the registry established by the bill.

SDAT must publish notice of the bill's registration requirements at least annually in specified advertising in newspapers of general circulation in Baltimore City and each county in which ground rents are located through September 30, 2010.

SDAT is required to report to the General Assembly by December 31, 2007 and by December 31, 2008 on the bill's implementation, including recommendations on the provision of notification to ground lease holders about the registration requirements by electronic and other means.

The Comptroller is required to report to the General Assembly by December 31, 2007 on recommendations regarding the provision of notification by the Comptroller to ground lease holders about registration requirements with SDAT established under the bill, including providing notification in the yearly State income tax instruction booklet.

Current Law: There is no central registry of ground leases.

SDAT charges an additional fee for the expedited processing of documents. Revenue from these fees is deposited into a fund, which is used to help pay costs associated with SDAT's charter document processing unit.

Background: While ground rents are recognized in other states, Maryland's system is unique. In Maryland, a ground rent creates a leasehold estate in the grantee. The leasehold estate is personal – not real – property. The grantor retains a reversion in the ground rent property and the fee simple title to the land. Ground rents generally have a 99-year term and renew perpetually. Ground rent is paid to the grantor (the ground rent holder) for the use of the property for the term of the lease in annual or semi-annual installments. Under a typical ground rent contract, the tenant agreed to pay all fees, taxes, and other costs associated with ownership of the property.

Ground rents have been a form of property holding in Maryland since colonial times, with some of the earliest known leases dating to 1750. The purpose of these ground rents was to produce income for their grantors. Most ground rents in colonial times required the tenant to erect improvements on the property. Maryland's unique system of ground rents can be traced to wording in its colonial charter from Charles I that prohibited certain feudal tenures, specifically those that would reserve a rent in a grantor who has transferred fee simple title. The 99-year lease was devised to reserve a ground rent without violating Maryland's colonial charter.

Prior to 1884, a ground rent could be redeemable or irredeemable by the terms of the lease. A redeemable ground rent would state the terms under which the tenant could redeem the lease and take fee simple ownership of the property. Generally, a tenant cannot take fee simple ownership of an irredeemable ground rent. When the General Assembly prohibited the creation of irredeemable ground rents beginning April 9, 1884, the General Assembly also established a method of calculating the redemption value.

Chapter 464 of 2003 established an alternative method for redeeming a ground rent if the tenant is unable to locate the ground rent holder, which had become a problem with some of the older ground rents. Under this method, the tenant must submit specified documentation and pay associated fees to SDAT.

In the 20th Century, developers used ground rents as part of their overall business strategy. Properties subject to ground rent could reduce the purchase price to a homebuyer, who might then be better able to afford a mortgage. In the earlier part of the century, a developer would sell houses in a development and retain the ground rent as a steady long-term income source. Later in the century, developers began securitizing and selling the ground rents to finance further developments. Many of these ground rents were held by institutional investors who saw them as long-term, low-risk investments.

When a tenant fails to pay rent, the ground rent holder may bring an action for the past-due rent or for possession of the premises. In either case, the ground rent holder is limited by statute to three years' past-due rent. Because the tenant has a leasehold estate, a tenant whose property is seized in an ejectment action (an action to retake the premises) receives no other compensation. The ground rent holder is then free to release the property under the ground rent or sell the property in fee simple.

Chapter 80 of 2003 established limits on the amounts that ground rent holders could receive as reimbursement for expenses received for actions to collect past due rent and for an ejectment action. A holder of a ground rent that is at least six months past due is entitled to reimbursement for actual expenses of up to \$500 to collect the past-due amount. In an ejectment action, the ground rent holder is entitled to filing fees and court costs, costs related to process service or other notice, title searches up to \$300, attorney's fees up to \$700, and taxes paid.

Recent newspaper accounts noted a sharp increase in the number of ejectment actions filed in the Circuit Court for Baltimore City during the last five years.

According to estimates from Baltimore City and SDAT, properties subject to ground rents are concentrated mostly in Baltimore City (74,085), with some properties located in Anne Arundel (5,000), Baltimore (35,705), Harford (1,500), Howard (200), Talbot (10), and Worcester (250) counties. SDAT advises that new ground rents have recently been created.

Baltimore City has identified 234,943 separate properties in the city, of which 214,604 have been transferred since 1982. City records indicate that 74,085 of the properties transferred have a ground rent.

State Revenues: According to the estimates from Baltimore City and SDAT, there are approximately 116,750 properties subject to a ground rent in the State. Under the bill, the ground lease holders of these ground leases would be able to apply to register over four fiscal years, beginning in fiscal 2008. SDAT estimates that approximately 100,000 of the State's approximately 117,000 ground leases would be registered under the bill by approximately 25,000 different ground lease holders. It is estimated that 32,500 ground leases would be registered in each of the first three years of the program by 8,125 different ground lease holders and that 2,500 ground leases would be registered in the final year in which to register by 625 different ground lease holders. Based on these estimates and the amounts charged per ground lease, special fund revenues would increase by \$154,375 in fiscal 2008, \$178,750 in fiscal 2009, \$203,125 in fiscal 2010, and \$15,625 in fiscal 2011.

State Expenditures: Special fund expenditures could increase by an estimated \$193,087 in fiscal 2008, which accounts for the bill's October 1, 2007 effective date. This estimate reflects the cost of hiring one charter specialist to process registrations under the bill and to purchase newspaper advertising. It includes a salary, fringe benefits, the cost to hire a contractor to create and maintain the database, other one-time start-up costs, and other ongoing operating expenses.

Salary and Fringe Benefits	\$39,629
Database Creation and Maintenance	89,000
Newspaper Advertising	59,750
Other Operating Expenses	<u>4,708</u>
Total FY 2008 State Expenditures	\$193,087
Positions	1

Future year expenditures reflect: (1) full salary with 4.5% annual increase and 3% employee turnover; (2) database maintenance and fee collection; (3) newspaper advertising in fiscal 2009 and 2010; and (4) 1% annual increases in ongoing operating expenses.

Additional Information

Prior Introductions: None.

Cross File: SB 622 (Senator Gladden) – Judicial Proceedings, although it is not designated as an Administration bill.

Information Source(s): No Agency Contacted, Department of Legislative Services
State Department of Assessments and Taxation, Baltimore City, Department of
Legislative Services

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