

Department of Legislative Services
Maryland General Assembly
2007 Session

FISCAL AND POLICY NOTE
Revised

House Bill 502 (Delegate Stein and the Speaker, *et al.*) (By Request – Administration)
Environmental Matters Judicial Proceedings

Ground Rents - Notices Regarding Ground Leases on Residential Property

This Administration bill requires a ground lease holder to mail a bill for the payment due to the tenant's last known address no later than 60 days before a yearly or half-yearly installment payment of a ground rent is due. The bill must include a notice containing specified information about the property subject to the ground rent, contact information for the ground lease holder, consequences for failing to pay the ground rent, and the right to redeem the ground lease. The bill requires a contract for the sale of real property subject to a ground lease to include a similar notice. The bill also requires a leasehold tenant to notify a ground lease holder of a change of address, including specified information, within 30 days after the change.

The provisions governing billing for ground rent and notice by the tenant apply to residential property used, intended to be used, or authorized to be used for four or fewer dwelling units. The provisions do not apply to property leased for other specified uses.

The bill takes effect July 1, 2007.

Fiscal Summary

State Effect: The bill would not materially affect State finances or operations.

Local Effect: Baltimore City could experience minor savings on properties it owns subject to ground rent.

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

Current Law: Within 30 days of any transfer of improvements located on property subject to a ground rent, the transferor must notify the holder of the reversionary interest (the landlord) of the transfer, including the name and address of the transferee, and the date of transfer. The notice must be given by certified mail, return receipt requested, to the landlord's last known address.

A contract for the sale of real property subject to a ground must contain: (1) notice of the existence of the ground rent; and (2) notice that if the ground rent is not paid in a timely fashion, the effect may be that the landlord may bring an action for possession and, as a result, the landlord may own the property in fee, discharged from the lease.

A ground rent established on or after April 9, 1884 may be redeemed by the tenant. The tenant must give the ground rent holder one month's notice and pay:

- an amount equal to the annual rent multiplied by:
 - 25, which is capitalization at 4%, if the lease was executed from April 8, 1884 to April 5, 1888;
 - 8.33, which is capitalization at 12%, if the lease was executed after July 1, 1982; or
 - 16.66, which is capitalization at 6%, if the lease was executed at any other time;
- a lesser sum, if specified in the lease; or
- a sum to which the parties may agree at the time of redemption.

If the lease was executed after July 1, 1982, the reversion is redeemable five years after the date of the lease. If the lease was entered before that time, it may be redeemed at any time.

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 or landlord) 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 the State Department of Assessments and Taxation (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. Of the properties transferred with a ground rent, 67,861 were residential properties with one to four dwelling units.

Local Fiscal Effect: Baltimore City advises that it pays approximately \$36,275 annually in ground rent on 722 properties in a database maintained by its housing department. The city has expressed concern that it may be liable for ground rent on an additional 1,800 properties for which it has not received a bill. To the extent the bill encourages the timely notice of ground rent due, the city could experience savings related to litigation on the 1,800 properties. Any such savings is likely to be minimal.

Additional Information

Prior Introductions: None.

Cross File: SB 398 (Senator Gladden, *et al.*) – Judicial Proceedings, although it is not designated as an Administration bill.

Information Source(s): Judiciary (Administrative Office of the Courts), State Department of Assessments and Taxation, Baltimore City, Department of Legislative Services

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