

Department of Legislative Services
Maryland General Assembly
2007 Session

FISCAL AND POLICY NOTE
Revised

House Bill 489

(Delegate Glenn and the Speaker, *et al.*)
(By Request – Administration)

Environmental Matters

Judicial Proceedings

Ground Rents - Redemption

This Administration bill repeals the provision that establishes a waiting period before a ground rent may be redeemed.

The bill also establishes notice requirements for when a ground lease is transferred to a third party and when a loan secured by property subject to ground rent is settled.

The bill takes effect July 1, 2007.

Fiscal Summary

State Effect: The required study could be handled with the existing budgeted resources of the Department of Housing and Community Development (DHCD). The bill's other provisions would not directly affect governmental finances or operations.

Local Effect: The bill would not affect local government finances or operations.

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: Within 30 days after any transfer of a ground lease, the transferee must notify the leasehold tenant of the transfer. The notification is required to include the

name and address of the new ground lease holder and the transfer date. If the property is subject to a redeemable ground rent, the notification has to also include a specified notice about the right to redeem the ground rent. These provisions 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.

Before the settlement of a loan secured by a mortgage or deed of trust on residential real property improved by four or fewer single-family units that is subject to a redeemable ground rent, the settlement agent must notify the borrower that: • the borrower has a right to redeem the ground rent; • the redemption amount is fixed by law but may be negotiated for a different amount; • it may be possible to include the amount of the redemption in the loan; and • the borrower should contact the ground lease holder for information on redeeming the ground rent and the lender or credit grantor making the loan for information on including the redemption amount in the loan. These requirements do not apply to a home equity line of credit, a loan secured by an indemnity deed of trust, or a commercial loan.

Current Law: 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.

If the tenant is unable to locate the ground rent holder, the ground rent may be redeemed through an alternative method. Under this method, the tenant must submit specified documentation and pay associated fees, along with the redemption amount and up to three years' back rent, to SDAT.

A contract for the sale of real property subject to a ground rent 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 reversionary owner (ground rent holder) may bring an action for possession and, as a result, the reversionary owner may own the property in fee, discharged from the lease.

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. Of the properties transferred with a ground rent, 67,861 were residential properties with one to four dwelling units.

Additional Information

Prior Introductions: None.

Cross File: SB 623 (Senator Gladden) – Judicial Proceedings, although it is not designated as an Administration bill.

Information Source(s): Department of Housing and Community Development, State Department of Assessments and Taxation, Baltimore City, Department of Legislative Services

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