

Department of Legislative Services
Maryland General Assembly
2012 Session

FISCAL AND POLICY NOTE

Senate Bill 194 (Senator Young, *et al.*)
Judicial Proceedings

Real Property - Residential Leases - Interest on Security Deposits

This bill alters the amount of interest a landlord must pay a tenant upon return of the tenant's security deposit from 3% per annum to the greater of the daily U.S. Treasury yield curve rate for one year on the first business day of each year or 1.5%. If a landlord has held a security deposit for less than the full year, the landlord must prorate the amount returned to a tenant according to the number of months the deposit was held as specified in the bill. The Department of Housing and Community Development's website must include a list of daily U.S. Treasury yield curve rates for one year, as of the first business day of the year, to be used in calculating the interest on a security deposit.

The bill takes effect January 1, 2013. The bill applies prospectively and may not be applied or interpreted to have any effect on or application to any residential leases entered into before the January 1, 2013 effective date of the bill.

Fiscal Summary

State Effect: The bill's requirements can be handled with existing resources. Revenues are not affected.

Local Effect: None.

Small Business Effect: Potential meaningful.

Analysis

Current Law: "Security deposit" is defined as any payment of money to a landlord by a tenant for the purposes of protecting the landlord against nonpayment of rent, damages

due to a breach of the lease, or damages to the leased premises, common areas, major appliances, and furnishings. A security deposit may include advance payment of the last month's rent.

A security deposit may not be greater than the equivalent of two month's rent per dwelling unit. The landlord must provide the tenant with a receipt notifying the tenant of his or her rights regarding the security deposit. Additionally, the landlord must hold all security deposits in specified federally insured financial institutions doing business in the State. The accounts must be devoted exclusively to the security deposits and bear interest. The landlord must deposit the security deposit into this account within 30 days of receipt. The interest must accrue at six-month intervals from the day the tenant gives the landlord the security deposit.

Within 45 days after the contractual end of a tenancy, the landlord must return the security deposit to the tenant, less any damages rightfully withheld. In addition to the principal of the security deposit, the landlord must return simple interest that has accrued in the amount of 3% per annum. If the landlord fails to return this amount within the specified time without a reasonable basis, the tenant may bring an action for up to three times the withheld amount and reasonable attorney's fees.

If a tenant has been ejected or evicted or has abandoned the property prior to the termination of the tenancy, the landlord is not required to return the security deposit unless the tenant provides written notice to the landlord demanding return of the security deposit. This notice must be sent by first-class mail within 45 days of being evicted or ejected or of abandoning the premises. The landlord, within 45 days of receipt of this demand, must send, by first-class mail, a list of any damages and return the security deposit, less any damages rightfully withheld. If the landlord fails to send the list of damages as required, the landlord forfeits the right to withhold any part of the security deposit for damages. In addition to the principal of the security deposit, the landlord must return simple interest that has accrued in the amount of 3% per annum. If the landlord fails to return this amount within the specified time, the tenant may bring an action for up to three times the withheld amount and reasonable attorney's fees.

Background: Chapter 2 of 1973 imposed the duty on a landlord to pay interest on a tenant's security deposit at 3% simple interest, accruing at six-month intervals. Chapter 536 of 1980 increased the interest rate that must be paid on a security deposit from 3% to 4%. Chapter 369 of 2004 lowered the required interest rate to be paid on a tenant's security deposit to 3%.

Several neighboring states have statutes regarding the return of accrued interest on a security deposit. For example, security deposits in the Commonwealth of Virginia must accrue interest at a rate equal to four percentage points below the current year's Federal

Reserve Board's discount rate. However, no accrued interest is returned unless the landlord has held the deposit for a period exceeding 13 months after the effective date of the rental agreement. Over the past three years in Virginia, security deposits have accrued no interest due to a low Federal Reserve discount rate. New Jersey law requires landlords who rent more than 10 apartments to place the deposit in either an insured money market fund or a federally insured bank account. The rate of interest must equal the average rate the bank pays on a money market fund. Landlords who rent fewer than 10 apartments must place the security deposit in an account that pays at least the regular rate of interest. Landlords are required to pay tenants, or subtract from the rent, the interest earned on the deposit each year.

The U.S. Treasury's yield curve rates, commonly referred to as "Constant Maturity Treasury" rates or "CMTs," are based on yields that are interpolated by the Treasury from the daily yield curve. This curve, which relates the yield on a security to its time to maturity, is based on the closing market bid yields on actively traded Treasury securities in the over-the-counter market. These market yields are calculated from composites of quotations obtained by the Federal Reserve Bank of New York. The yield values are read from the yield curve at fixed maturities, currently 1, 3, and 6 months and 1, 2, 3, 5, 7, 10, 20, and 30 years. As shown in **Exhibit 1**, the U.S. Treasury's yield curve rates for one year, as of the first business day of the year, have ranged from as high as 5% in 2007 to as low as 0.12% in 2012 over the past 10 years.

Exhibit 1
2003-2012 U.S. Treasury Yield Curve Rates for One Year

<u>Date</u>	<u>Rate</u>
1/3/2012	0.12%
1/3/2011	0.29%
1/4/2010	0.45%
1/2/2009	0.40%
1/2/2008	3.17%
1/2/2007	5.00%
1/3/2006	4.38%
1/3/2005	2.79%
1/2/2004	1.31%
1/2/2003	1.42%

Source: U.S. Department of the Treasury

Small Business Effect: This bill has a potentially meaningful effect on landlords. Under current law, landlords must return each security deposit with an additional 3% simple interest per annum even if the security deposits are accruing less than 3% simple interest per annum from a financial institution. Given the difficult economic climate, it is extremely difficult to find a brick and mortar financial institution that pays interest on deposits at 1% or 2%, let alone 3%. Thus, landlords are required to use other funds, which may include rental profits, loans, or personal savings, to supply the equivalent of an additional 3% simple interest per annum for each returned security deposit.

Under this bill, if the yield curve rate remains at 1.5% or less, landlords are required to return the equivalent of an additional 1.5% simple interest per annum for each returned security deposit. As a result, landlords could realize meaningful savings from the lower interest rate threshold required by the bill. The magnitude of savings would depend on the number of properties rented, the amount of collected security deposits, and the turnover rates of rental properties.

It should be noted, however, that despite the potential savings for landlords due to recent low yield curve rates, in the future, landlords may be required to return an amount of interest greater than 3% per annum to the extent that yield curve rates exceed 3%.

Additional Information

Prior Introductions: HB 917 of 2011, as amended, passed the House and was heard by the Senate Judicial Proceedings Committee but received no further action.

Cross File: Although not designated as a cross file, HB 22 (Delegate McMillan – Environmental Matters) is identical except for the purpose paragraph. Likewise, its cross file, SB 361 (Senator Shank – Judicial Proceedings), is identical except for the purpose paragraph.

Information Source(s): Office of the Attorney General (Consumer Protection Division), Department of Housing and Community Development, Judiciary (Administrative Office of the Courts), New Jersey Code, Virginia Code, U.S. Department of the Treasury, Department of Legislative Services

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