

Department of Legislative Services
Maryland General Assembly
2014 Session

FISCAL AND POLICY NOTE

House Bill 1529 (Delegates McIntosh and Niemann)
Environmental Matters

Real Property - Ground Rents

This emergency bill repeals a provision of law that makes the establishment of a lien the remedy for nonpayment of a ground rent on residential property and reinstates, with modifications, an action for possession of the property (an ejectment action) as the remedy, similar to the posture of the law before 2007. In addition, in an ejectment action, the bill specifies and places limits on the expenses for which a ground lease holder may be reimbursed, and it adds new requirements for service of process on a leasehold tenant.

Fiscal Summary

State Effect: Changing the nature of the remedy available for failure to pay ground rent does not materially affect the finances or operations of the Judiciary.

Local Effect: Changing the nature of the remedy available for failure to pay ground rent does not materially affect the finances or operations of the circuit courts or those local governments that hold ground rents.

Small Business Effect: Minimal.

Analysis

Bill Summary: In addition to up to three years of back rent, a landlord under a residential ground lease or sublease may not receive reimbursement for any additional costs or expenses related to collection of back rent in an action for past-due rent or possession of the property, except as provided in provisions described below establishing certain notice requirements and limitations on expenses.

Action for Possession

The bill expands the action for possession remedy to residential property subject to a ground lease that is or was used, intended to be used, or authorized to be used for four or fewer dwelling units.

When a leasehold tenant under a ground lease fails to pay rent, the ground lease holder, or landlord, may bring an action for possession of the property no less than 45 days after sending a bill for the ground rent due by certified mail, return receipt requested, to the leasehold tenant's last known address if (1) at least six months ground rent is in arrears and (2) the landlord has the right to reenter for nonpayment of the rent under the ground lease. The landlord must also send a copy of the bill by first-class mail to the title agent or attorney listed on the deed to the property or intake sheet recorded with the deed.

The bill repeals an exception to the notice requirement that allowed service in an action for possession to be made by posting notice as prescribed under the Maryland Rules if the tenant cannot be personally served or there is no tenant in actual possession of the property. In addition, the bill stipulates that service of process must be made by (1) personal delivery of the papers to the leasehold tenant or (2) leaving the papers with a resident of suitable age and discretion at the leasehold tenant's dwelling house or usual place of abode.

Before entry of a judgment, the landlord must also give written notice of the pending entry to each mortgagee of the lease, or any part of the lease, who before entry of the judgment has recorded a timely request for a notice of judgment in the land records. The landlord must mail the notice by certified mail, return receipt requested, to the mortgagee at the address stated in the recorded request for notice of judgment.

Generally, property subject to a judgment for possession is discharged from its ground lease, and the rights of all persons claiming under the lease are foreclosed unless, within six months after execution of the judgment, the tenant or other person claiming under the lease (1) pays the ground rent, arrears, and all costs awarded against that person and (2) commences a proceeding to obtain relief from the judgment.

Reimbursement of Costs and Expenses

Generally, a landlord may not receive reimbursement for any additional costs or expenses related to collection of the back rent unless all notice requirements are met.

If authorized under the residential lease or sublease, the holder of a ground rent under a residential lease or sublease in effect on or after July 1, 2007, that is at least six months in arrears is also entitled to reimbursement for actual expenses of up to \$300 incurred to

collect the past-due amount and comply with notice requirements, including title abstract and examination fees, judgment report fees, photocopying and postage fees, and attorney's fees.

If authorized under the residential lease or sublease, upon filing an ejectment action, the plaintiff or ground lease holder is entitled to reimbursement for reasonable expenses incurred in the preparation and filing of the action, including filing fees and court costs; costs related to service of process or otherwise providing notice; additional title abstract and examination fees up to \$150; reasonable attorney's fees up to \$450; and taxes, including interest and penalties, paid by the plaintiff or ground lease holder.

To to be eligible for reimbursement, the holder must give notice to the tenant of the amount of the past-due ground rent. The notice must be sent by first-class mail to the tenant's last known address as shown in the State Department of Assessments and Taxation's (SDAT) records at least 30 days before taking any action, and it must state that the holder will take action to repossess the property and the tenant will be liable for fees and expenses if the past-due ground rent is not paid within 30 days.

Except as specified above, the plaintiff or holder of a ground rent under a residential lease or sublease in effect on or after July 1, 2007, is not entitled to reimbursement for any other expenses incurred in the collection of a ground rent.

Additional Notice Requirements

The bill expands the content of notices required to be included in ground rent bills and contracts for the sale of residential property subject to a ground lease. The notices must include specified information stating that (1) if a ground lease holder files an action in court to collect past-due ground rent, the leasehold tenant may be required to pay the ground lease holder for fees and costs associated with the collection of the past-due ground rent; (2) the ground lease holder may file an action in court to take possession of the property, which may result in the leasehold tenant being responsible for additional fees and costs; and (3) there are limits on how much a ground lease holder may be reimbursed for fees and costs.

Current Law/Background: The bill is in response to the Maryland Court of Appeals decision in *State v. Goldberg, et al.*, No. 8 (September Term, 2013), which held that provisions of Chapter 286 of 2007 eliminating ejectment as a remedy for nonpayment of ground rent and replacing it with a process to create and foreclose on a lien were unconstitutional. This bill substantially restores the ejectment remedy available for ground rent lease holders of residential property available prior to 2007.

Ground Leases, Generally

As of February 2014, there were 86,557 ground leases registered with SDAT. Ground leases are concentrated mostly in Baltimore City (58,433), with some properties located in Anne Arundel (3,517), Baltimore (24,275), Carroll (10), Charles (1), Harford (82), Howard (58), Montgomery (3), Talbot (10), Prince George's (36), and Worcester (142) counties.

History of Ground Leases in Maryland: Ground leases have been a form of property holding in Maryland since colonial times. A ground lease creates a leasehold estate in the grantee that is personal – not real – property. The grantor retains a reversion in the ground lease property and fee simple title to the land. Ground leases generally have a 99-year term and are renewable perpetually. Ground rent is paid to the grantor (the ground lease holder) for the use of the property for the term of the lease in annual or semi-annual installments. Under a typical ground lease contract, the tenant agrees to pay all fees, taxes, and other costs associated with ownership of the property. Prior to 2007, when a tenant failed to pay rent, the ground lease holder could bring an action for the past-due rent or for possession of the premises. Because the tenant had a leasehold estate, a tenant whose property was seized in an ejectment action received no other compensation.

2007 Ground Lease Legislation: In December 2006, a series of articles in the *Baltimore Sun* described an apparently dysfunctional ground rent system in which residential property was being seized over missed ground rent payments and homeowners were being charged exorbitant fees. Often, because of the age of the ground rent, it was reported that the occupant of the property did not know of the existence of the ground rent until facing ejectment or other legal action.

Several measures in the 2007 session addressed the ground rent system. Chapter 1 of 2007 prohibited the creation of new residential ground rents on or after January 22, 2007. The other measures dealt with existing ground leases on residential property.

To eliminate the possibility that a leasehold tenant could lose the tenant's home and all of the equity in it for failure to pay a ground rent, Chapter 286 of 2007 repealed the ability of a ground lease holder to bring an action of ejectment for failure to pay ground rent and instead provided for the creation of a lien.

Chapter 290 of 2007 facilitated the timely payment of ground rents by requiring SDAT to establish an online registry of properties subject to a ground rent. The bill required ground lease holders to register their properties by September 30, 2010. If a ground lease holder failed to register by that date, the ground lease holder's reversionary interest would be extinguished and the ground rent was no longer payable.

Chapters 288 and 289 of 2007 required a ground lease holder to mail a bill to the leasehold tenant's last known address no later than 60 days before an installment payment is due. The bill must include specified information about the property, contact information for the ground lease holder, consequences for failing to pay the ground rent, and the right to redeem the ground rent. A contract for the sale of real property subject to a ground rent must include similar information.

Finally, Chapters 287 and 291 of 2007 encouraged leasehold tenants to redeem ground rents and gain fee simple title to the land underneath their homes. Chapter 287 provided for the conversion of irredeemable ground rents (that is, those executed before April 9, 1884) to redeemable ground rents. An irredeemable ground rent became converted to a redeemable ground rent unless a notice of intention to preserve irredeemability was recorded in the land records by December 31, 2010. If notice was filed, then the irredeemability continues through 2020 unless another 10-year notice is filed. Once a notice lapses, the ground rent becomes redeemable. Chapter 291 eliminated the statutory waiting period before a leasehold tenant may redeem a ground rent and established notice requirements about the right to redeem when a ground rent is transferred to a third party.

Constitutionality of Chapter 290 of 2007

In 2011, the Maryland Court of Appeals held that the retrospective extinguishment and transfer provisions of Chapter 290 violated the due process and takings provisions under Maryland's Declaration of Rights and Constitution and were, therefore, unconstitutional. *Muskin v. State Dept. of Assessments and Taxation*, 422 Md. 544 (2011). However, the court held that the registration requirement was valid. The court suggested that alternative statutory approaches might include one where failure to register a ground lease triggers an interim consequence, such as restrictions on collecting ground rents prospectively or a denial of access to the courts for collection of unregistered ground rents. 442 Md. at 550.

In response to the holding in *Muskin*, Chapters 464 and 465 of 2012 require a holder of a ground lease to comply with the existing requirement to register with SDAT before the holder may (1) collect any ground rent payments due under the ground lease; (2) bring a civil action against the leasehold tenant to enforce any rights the ground lease holder may have under the ground lease; or (3) obtain a lien on the property. The measures do not prohibit a ground lease holder who registers a ground lease from collecting up to three years of back ground rent payments or taking any other enforcement actions after the ground lease is registered. Before a holder can collect any yearly or half-yearly ground rent installment payment or obtain a lien, the holder must mail, at least 60 days before the payment is due, a bill for the amount owed to the leasehold tenant's last known address and the address of the property subject to the ground lease.

The measures also repealed provisions relating to the extinguishment of a ground lease not registered with SDAT prior to September 30, 2010, and voided any extinguishment certificates issued by SDAT for failure to register. On request of the ground lease holder or the leasehold tenant, SDAT is required to file a notice in the county land records where an extinguishment certificate was filed stating that the certificate is void and the underlying leasehold interest is in full effect unless otherwise redeemed.

Constitutionality of Chapter 286 of 2007

In *Goldberg*, the plaintiffs claimed that the retroactive elimination of the remedy of ejectment amounts to a taking of private property without just compensation. The Maryland Court of Appeals, citing *Muskin* as governing the outcome, agreed with the plaintiffs that the provisions of Chapter 286 were unconstitutional under the Maryland Declaration of Rights and the Maryland Constitution.

The court reasoned that within a statement in the *Muskin* opinion – that “[a] ground lease creates a bundle of vested rights for the ground rent owner, [1] a contractual right to receive ground rents and [2] the reversionary interest to re-enter the property in the event of a default or if the leaseholder fails to renew” – the “reversionary interest” actually collectively includes two distinct, intertwined rights: the reversion and the right to re-entry. *Goldberg* at 18, quoting *Muskin* at 559. According to the court, the right of re-entry is the right to pursue a provided remedy, such as ejectment, to terminate the leasehold interest and recover rents due prior to the termination, and the foreclosure-and-lien remedy is not an adequate replacement. *Goldberg* at 22 and 23. The court further explained that “[d]ue to the unique nature of the property rights invested in ground rent leases, where the ground leaseholder’s rights are bundled, the right of re-entry is vested.” *Goldberg* at 26. Thus, the court, stating that “the ejectment remedy ... is essential for the right of re-entry,” ruled that Chapter 286’s impingement of the vested right is unconstitutional. *Goldberg* at 25 and 26.

Additional Information

Prior Introductions: None.

Cross File: SB 1095 (Senator Frosh) - Judicial Proceedings.

Information Source(s): Baltimore, Carroll, Charles, Harford, Montgomery, Talbot, and Worcester counties; Baltimore City; State Department of Assessments and Taxation; Office of the Attorney General; Judiciary (Administrative Office of the Courts); *The Baltimore Sun*; Department of Legislative Services

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