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To: The Honorable Kumar Barve
Chair, Environment and Transportation Committee

From: Kira Wilpone-Welborn, Assistant Attorney General
Consumer Protection Division

Re: House Bill 1076 – Real Property - Residential Leases - Fee in Lieu of Security Deposit
(OPPOSE)

The Consumer Protection Division of the Office of the Attorney General (the “Division”) **opposes** House Bill 1076 sponsored by Delegate Wells. House Bill 1076 purports to provide consumers a reasonable alternative to paying a security deposit or obtaining a surety bond by allowing them to pay a “fee in lieu of a security deposit,” which their landlord would use to purchase insurance coverage for unpaid monies and damage to the unit. However, the “fee in lieu of a security deposit” provides few benefits to tenants and could result in some tenants paying significantly more than they would have if they had paid a security deposit. For example, House Bill 1076 would permit the landlord to charge a fee in any amount, payable at any interval, that is wholly nonrefundable, would permit a landlord to contract with an insurance provider that is not licensed by the Maryland Insurance Commission, and would encourage insurance providers to seek subrogation (financial compensation) from tenants for claims paid to their former landlords. Thus, House Bill 1076 would make it easier for landlords to engage in unfair, abusive, or deceptive practices by either misleading or failing to advise prospective tenants of the consequences of choosing to pay a “fee in lieu of security deposit” and ultimately fails to provide any meaningful benefit to tenants.

Maryland's Security Deposit Law

Maryland's Security Deposit Law defines “security deposit” to mean “any payment of money, including payment of the last month's rent in advance of the time it is due, given to a landlord by a tenant in order to protect the landlord against nonpayment of rent, damage due to breach of lease, or damage to the leased premises, common areas, major appliances, and furnishings.” Md. Code Ann., Real Prop. §8-203(a)(3). Maryland's Security Deposit law affords consumers who lease residential properties in Maryland important protections from unscrupulous landlords. For

example, a landlord may not require a tenant to pay a security deposit that exceeds the equivalent of two months' rent per dwelling unit, regardless of the number of tenants. Md. Code Ann., Real Prop. §8-203(b). A landlord must maintain security deposits in an account that is devoted exclusively to security deposits and bears interest. Md. Code Ann., Real Prop. §8-203(d). A landlord may only withhold a security deposit for unpaid rent, damage due to breach of lease, or for damage caused by the tenant beyond "ordinary wear and tear to the leased premises, common areas, major appliances, and furnishings owned by the landlord" and must provide a tenant a written list of the damages claimed together with a statement of the costs actually incurred. Md. Code Ann., §§8-203(f)(1) and (g)(1). A security deposit is not liquidated damages and may not be forfeited to the landlord for breach of the rental agreement, except in the amount that the landlord is actually damaged by the breach. Md. Code Ann., Real Prop. §8-203(f)(2).

Alternatively, a tenant can purchase a surety bond to protect the landlord against nonpayment of rent, damage due to breach of lease, or damage to the leased premises, common areas, major appliances, and furnishings. As with a traditional security deposit under section 8-203, the amount of the surety bond purchased and any security deposit paid may not exceed the equivalent of two month's rent per dwelling unit. Md. Code Ann., Real Prop. §8-203(i)(3). Importantly, it is the tenant who purchases the bond rather than the landlord and the tenant must be advised in writing of all the tenant's rights prior to the purchase of the security bond. Md. Code Ann., Real Prop., §8-203(i)(5). Additionally, before making a claim against the surety bond, a landlord must provide written notice to the tenant that includes a list of damages to be claimed and costs actually incurred; and a tenant has the right to pay any damages directly to the landlord and has the right to dispute a landlord's claim. Md. Code Ann., Real Prop. §8-203(i)(7), (8), and (9).

House Bill 1076 Would Harm Consumers

House Bill 1076 does not include many of the protections afforded by the provisions in the Real Property Article related to security deposits and surety bonds. While the proposed "fee in lieu of security deposit" may appear to benefit and open housing opportunities for low-income households, in fact, House Bill 1076 would likely harm consumers in several ways.

First, House Bill 1076 could result in higher out-of-pocket costs paid by consumers over their lease term. Unlike the provisions related to the payment of a security deposit or purchase of a surety bond, House Bill 1076 does not cap the total amount a landlord would be permitted to charge as a "fee in lieu of security deposit." Thus, the total fees paid over the course of a multiple year lease could easily exceed the equivalent of two months' rent. Additionally, unlike a security deposit, which must be returned to a tenant with interest minus any authorized damages within 45 days of the end of a tenancy, House Bill 1076 permits a landlord to deem a "fee in lieu of security deposit" wholly nonrefundable.

Second, House Bill 1076 does not require a landlord who has purchased insurance to disclose to consumers the landlord's actual costs to obtain the insurance or require that the fee charged to consumers be the actual cost of the insurance. Further, the bill does not require a landlord to first apply the portion of the fee charged which is over and above the costs to obtain the insurance towards any claimed losses as a result of nonpayment of rent, damage due to breach of lease, or

damage to the leased premises before making a claim on the insurance. As a result, House Bill 1076 would permit landlords to charge tenants fees that exceed their costs to obtain insurance and unfairly profit from a tenant's election to pay the "fee in lieu of security deposit" instead of the lump-sum security deposit.

Third, because consumers would not be parties to the insurance contract, consumers would not be able to make claims to the insurer, appropriately challenge an insurer's decision to deny a claim, or dispute an insurer's decision to pay a claim until after another party initiates collection activity against the tenant. Moreover, if an insurer sought subrogation against a tenant for a claim paid to a landlord or transfers a paid claim to a third-party as permitted in House Bill 1076, a tenant may not have sufficient information to defend the claim or understand a demand for payment of the claim. As a result, the tenant would pay both a monthly fee and the claim at the conclusion of a tenancy. Thus, the "fee in lieu of security deposit" would ultimately provide no material financial benefit to the consumer.

As such, a "fee in lieu of security deposit" is not a reasonable alternative to a security deposit, which is limited in amount, is refundable, and provides consumers protections under section 8-203 of the Real Property Article. Likewise, a "fee in lieu of security deposit" is not a reasonable alternative to a surety bond, which allows a consumer to avoid an upfront security deposit payment by paying a small monthly fee, and provides consumers protections as a party to the insurance contract and the financial cap protections under section 8-203 of the Real Property Article.

For these reasons, the Division encourages an unfavorable report from the Environment and Transportation Committee on House Bill 1076.

cc: The Honorable Melissa Wells
Members, Environment and Transportation Committee