

**Department of Legislative Services**  
Maryland General Assembly  
2015 Session

**FISCAL AND POLICY NOTE**

Senate Bill 565

(Senator Gladden)

Judicial Proceedings

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**Real Property - Redeemable Ground Rents**

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This bill requires a redeemable ground rent on a residential property to be redeemed when the property is transferred for arm's length consideration, or when the tenant obtains or refinances a loan secured by a mortgage or deed of trust on the property, whichever occurs earlier. If a past-due ground rent is subject to a collection or enforcement procedure, that default must be cured before the ground rent is redeemed. The bill does not apply to (1) a transfer by foreclosure sale as specified; (2) a transfer to a lender by deed in lieu of foreclosure; (3) a transfer by a fiduciary as part of the administration of an estate or trust; (4) a transfer to a spouse or former spouse in an action for divorce or annulment; or (5) a loan secured by a home equity line of credit.

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**Fiscal Summary**

**State Effect:** The bill does not materially impact State operations or finances.

**Local Effect:** Baltimore City expenditures may increase, potentially significantly, due to the bill's requirement that the ground rent be redeemed when the property is transferred. If the property is transferred to the city as the result of a settlement in lieu of condemnation, Baltimore City may be required to redeem the ground rent, significantly increasing the cost of each transaction.

**Small Business Effect:** Potential meaningful impact on small businesses that are holders of ground leases who may see an increase in redemptions of ground rents due to the requirements of the bill.

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## Analysis

### Current Law/Background:

#### *Ground Leases, Generally*

As of February 2015, there were 88,422 ground leases registered with the State Department of Assessments and Taxation (SDAT). According to the registry maintained by SDAT, ground leases are concentrated mostly in Baltimore City (59,955), with some properties located in Anne Arundel (3,539), Baltimore (24,506), Carroll (10), Charles (1), Harford (171), Howard (58), Montgomery (3), Prince George's (36), and Worcester (143) 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*

*State v. Goldberg, et al.*, 437 Md. 191 (2014), 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. 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.

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## **Additional Information**

**Prior Introductions:** None.

**Cross File:** HB 637 (Delegates Holmes and Beidle) - Environment and Transportation.

**Information Source(s):** Anne Arundel, Baltimore, Charles, Carroll, Harford, Howard, Prince George's, Talbot, and Worcester counties; Baltimore City; State Department of Assessments and Taxation; Judiciary (Administrative Office of the Courts); Department of Legislative Services

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