

**MAKING IT UP AS THEY GO ALONG-
THE IMAGINATIVE EFFORTS BY COUNTIES TO INCREASE REVENUES
FROM TRANSFER AND RECORDATION TAXES**

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As County governments in Maryland feel the ongoing fiscal pressures of the current real estate recession, many have taken to creative and often dubious interpretations of law to try to boost revenues derived from the Transfer and Recordation Taxes paid upon the recording of real estate transfer and financing documents in the Land Records. Although County officials have vehemently denied taking such actions to try to plug any revenue gap in receipts from recording deeds and mortgages in the Land Records, the protestations of such officials have the same ring as the surprise voiced by Captain Renault upon his “discovery” of the roulette table in Rick’s Café Americain in Casablanca.

The Howard County Department of Law has taken a very aggressive interpretation of the law with respect to the Recordation Tax payable on an Indemnity Deed of Trust (“IDOT”) which is foreclosed upon. Specifically, the Howard County Department of Law has determined that it is entitled to collect the Recordation Tax that was due (but not required to be paid) on the original recording of the IDOT, at the time that a Trustee’s Deed transferring title from the foreclosing Trustee is presented for recordation. As a result, the Recordation Tax of 0.5% of the secured amount of the loan will be required to be paid by one of the parties to the Trustee’s deed (often the foreclosing Lender) and not by the Grantor under the IDOT.

By way of background, an IDOT is not, in and of itself, exempt from the Recordation Tax. If, following a default, the Lender makes demand on the Guarantor that has granted the IDOT, the Recordation Tax becomes due at that time. Based on an Opinion letter of the Attorney General of Maryland dated July 28, 1989, it was previously thought to be settled law that, upon a default under an IDOT, the obligation for the payment of the Recordation Tax is that of the defaulting Grantor under the IDOT and not the obligation of the Lender. The recent assertion by Howard County turns this assumption on its head.

An official of the Howard County Department of Law explained that the County does not believe the facts of the 1989 Opinion are generally applicable to a foreclosure under an IDOT. However, despite repeated requests from members of the Real Property Section of the State Bar Association and others, no distinguishing facts to the analysis in the 1989 Opinion have been provided by the County. The County is merely asserting that the 1989 Opinion does not apply and, as a result, the provisions of Section 3-104(b)(1) of the Real Property Article can be applied, which requires the payment of all “taxes, assessments, and charges due on the property” as a condition to the transfer of real property. The County's analysis therefore requires the payment of the Recordation Tax to the County before a Trustee’s Deed may be recorded. This is a highly flawed reading of

the statute, because, among other reasons, the Recordation Tax is not a tax on the “property,” but rather a tax for the privilege of recording an instrument.

In addition to the foregoing, it is believed that the Clerk’s offices in at least Harford County and Howard County are now closely reviewing Loan Modification documents or other modification documents to an IDOT or Indemnity Mortgage in order to determine whether such documents reflect that a default has occurred under a loan that is (secondarily) secured by an IDOT. For example, if a Loan Modification document or Modification of IDOT makes reference to the fact that a loan was previously in default and is being reinstated in accordance with the Loan Modification Agreement, the Clerk will assess the payment of Recordation Tax on the original IDOT.

Unlike Howard County’s determination that Recordation Tax must be paid upon the recording of Trustee’s deeds arising out of foreclosed IDOT’s, this is a correct exercise of the Clerk’s discretion and care should be taken in documenting a loan workout that will be presented for record, whether in Harford or Howard County or elsewhere. As noted above, the 1989 Attorney General’s opinion held that the Recordation Tax under an IDOT becomes due upon a default in the underlying Promissory Note, whereupon the IDOT becomes primary security for the guaranty of the note. Lenders will need to give loan budget consideration in a workout as to whether the Recordation Tax that was not due on the original recording of the IDOT will need to be paid upon the documentation of a loan workout following default.

Another example of an aggressive interpretation of the law in an effort to collect additional Recordation Taxes relates to a deed of trust or mortgage that secures a Letter of Credit obligation. In connection with land development loan facilities, the Lender often agrees to issue Letters of Credit to governmental authorities to secure the developer’s obligations with respect to public works or other obligations for public improvements. Since the Letters of Credit are not current obligations until they are presented for payment by the government authority following a default by the Developer in completing its public improvement obligations, Recordation Tax is typically not collected upon recording of a Deed of Trust to secure those obligations. Instead, the Recordation Tax is due, in accordance with Section 12-105(f)(2) of the Tax-Property Article, at such time as a draw is made under a Letter of Credit secured by the Deed of Trust. Officials of Howard County have asserted that they will require that the Recordation Tax to be paid in full on the amount of the secured Letters of Credit obligation at the time of recording unless the Lender issuing the Letters of Credit agrees to be primarily liable for the payment of any Recordation Tax as it becomes due upon a draw under a Letter of Credit.

A final example of aggressive interpretation of law is the effort of County Clerks in, at least, Anne Arundel County, to assess Transfer and Recordation Tax on a Deed arising out of a “short sale” based on the amount of the existing debt at the time of transfer, rather than the actual consideration paid by the Buyer. In a “short sale,” a property is transferred by Deed for consideration less than the outstanding amount of the loan secured by a Mortgage on the property. The Lender that is secured by the property consents to a release of its lien upon payment of less than the amount owed by the Seller.

Section 12-104(a) of the Tax Property Article requires only that the consideration payable “including the amount of any mortgage or deed of trust assumed by the grantee” be recited on the deed for purposes of determining the applicable Transfer and Recordation Taxes due. The basis for Anne Arundel County’s assessment of Transfer and Recordation Taxes on a “short sale” deed based on the amount of the then-existing debt is unclear given that the short sale Purchaser does not assume the outstanding mortgage indebtedness. Regardless, Clerks have requested copies of a payoff statement of the loan or a loan statement from the Lender to confirm the amount of the debt in excess of the purchase price for the property.

As real estate development activity slowly increases and Lenders are again willing to provide loans for land development activities, the actions of officials in Howard County, for example, will be an unnecessary drag on lending transactions. Lenders will have to analyze and perhaps include in their loan budgets the potential costs of Recordation and Transfer Taxes, which were previously not imposed on a Lender. The unintended consequences of a push for cash receipts by whatever means possible will not be fully understood until the pace of new real estate development and lending activity quickens.

If you have any questions about these recent developments concerning Recordation Taxes, please contact Barry Greenberg at (410) 727-6600 or bgreenberg@rosenbergmartin.com. If you need any assistance with any of your other real estate needs, please contact Barry or another attorney in our real estate group:

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