

Welcome fellow Real Estate Professionals ...

**MYLESTITLE'S 3RD QUARTER 2012
ADVISORY COUNCIL BREAKFAST & SEMINAR**

Solutions to Key Maryland Real Estate Issues

**BREAKING MARYLAND REAL ESTATE NEWS:
MARYLAND IDOTS - PAST, PRESENT & FUTURE.
DISCOVER VALUABLE PRACTICAL TIPS FROM LEADERS
IN MARYLAND'S LEGAL REAL ESTATE COMMUNITY**

- ❖ **ATTORNEYS & LENDERS:** Discover the impact and nuances of how recent IDOT legislation and AG and county memoranda both raise and answer questions about Maryland real estate transactions.
- ❖ **INVESTORS & DEVELOPERS:** Learn about immediate opportunities and hurdles that exist when dealing with the IDOT issue in Maryland.

OUR LEGAL PANEL

EDWARD S. "TED" EVANS, III, ESQ.

Venable LLP, Partner

BARRY C. GREENBERG, ESQ.

Rosenberg / Martin | Greenberg LLP, Partner

EDWARD J. LEVIN, ESQ.

Gordon Feinblatt LLC, Partner

RICHARD E. LEVINE, ESQ.

DLA Piper LLP, Partner

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Hayfields Country Club
September, 13, 2012

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Myles Title September 13, 2012 Advisory Council Breakfast Seminar:

Outline, Time-Line & Panel Member Parts

I. Myles Intro [Myles Lichtenberg] AC Intro, Intro of Panelists & Moderator and Q&A

II. What is an IDOT? [Ed Levin]

- a. IDOT Background

III. The "New" Law [Ed Levin]

- A. Basic Mechanics
- B. Cost, Per transaction
- C. Overall projected dollar impact?
- D. SDAT working group

IV. WHAT ARE THE PROMULGATED EXEMPTIONS? [Ed Levin]

- A. New law does not apply to the extent recordation tax is paid on another instrument of writing that secures payment of the guaranteed loan.
- B. The new law does not alter the provisions of Section 12-105(f) of the Tax-Property Article of the Annotated Code of Maryland ("TPA"), which allow, with respect to a construction loan over \$100,000 where the total amount of the debt secured has not been incurred at the time of recording, recordation taxes to be paid only on the principal amount of the debt incurred at that time.
 - C. The new law also appears to leave intact the exemption from recordation taxes set forth in Section 12-108(e) of the TPA for "supplemental instruments of writing."
 - D. Under \$1,000,000.00 loans.

V. QUESTIONS AND ANSWERS AND PRACTICE POINTERS ABOUT IDOTS

A. Will other exemptions survive? [Panel Discussion, lead by: Rich Levine]

1. Would the bill apply to existing IDOTs? [Rich Levine]
2. What happens if you have a \$950,000 loan in which an IDOT is recorded and the IDOT is amended of record to reflect that the loan is increased by \$100,000? [Rich Levine]
3. Single loan of \$1 million or more, by recording multiple IDOTs, all of which are under \$1 million? [Rich Levine]
4. How will they know whether this is a taxable IDOT? (Refer to AG Memo) [Rich Levine]

5. **[Ted Evans] [Panel Discussion, lead by: Ted Evans]** What if an IDOT that secures \$1,000,000 or more that was recorded before July 1, 2012 is amended on or after that date? Are there any 'amendments' that would or should not trigger the tax, i.e. Substitution of Trustee?
6. What about an IDOT for more than \$1 million that is secured by real property located in Maryland and by property located in another state. If the amount of the loan that is allocated to Maryland property is under \$1 million, does the IDOT still get taxed? *[Ted Evans]*
7. What can be done to minimize the need to record an amendment to an IDOT after July 1, 2012? *[Ted Evans]*
 - a. Change in maturity date.
 - b. Omit the amount secured. Pros and Cons.
 - c. The law imposing a tax on IDOTs amended only TP §12-105(f)
8. What if two loans involving IDOTs each secure \$750,000 and are recorded at or about the same time – will they be taxable? How are IDOTs treated in Prince George's County? *[Ted Evans]*
9. Documentation of Loan Transactions to avoid/reduce the payment of Recordation Taxes **[Panel Discussion, lead by: Barry Greenberg]**
 - a. Purchase within 30 days – Purchase Money Exemption.
 - b. Refinance where taxes have already been paid – How to structure the transaction.
 - c. Language requiring lender to sell the loan to subsequent lender upon borrower's request.
 - i. It will be interesting to see whether a practice develops in Maryland refinance situations whereby existing IDOTs are preserved, transferred among lenders and then modified to suit the new lender's requirements (similar to New York).
 - ii. Sample/uniform language for loan documents hopefully to become generally accepted by lenders and borrowers, and their respective counsel
 - (a.) Requirements of Lender
 - (b.) Requirements of Borrower
 - (c.) What if loan documents unavailable/lost
 - (d.) Why IDOTs, i.e. why not Deeds of Trust?
 - iii. Payment of rec tax with the initial IDOT/DOT filing – is the tax later recouped wholly? In part?

III. Q & A [Entire Panel]

Myles Title Advisory Council September 13, 2012 Breakfast Seminar

List of Exhibits

1. Daily Record Article on IDOTs by Edward J. Levin May 21, 2012
2. How Certain Counties Came to Issue Rules on Recordation Tax Collection by Edward J. Levin
3. House Bill 792, Chapter 639, 2000 Regular Session of the Maryland Legislature
4. Senate Bill 1302 – State and Local Revenue Financing Act of 2012
5. A Discussion of IDOTS and Questions and Answers about Senate Bill 1302
6. Memorandum and Order dated August 28, 2012 in the Maryland Tax Court, *Atapco Howard Square I Business Trust, et al vs. Howard County Department of Finance* Case No. 11-RC-OO-0805 through 0811
7. Summaries of Officials' Memoranda Regarding IDOTS under Senate Bill 1302 by Edward J. Levin
8. Assistant Attorney General Stuart Cordish Memorandum to Clerks of Court and Land Records Department dated June 15, 2012
9. Howard County memorandum entitled Recordation Tax -- Indemnity Deeds of Trust
10. Howard County Affidavit for Indemnity Deed of Trust (not for recording)
11. Montgomery County Memorandum from James Babb entitled New Law Concerning Indemnity Deeds of Trust dated June 15, 2012
12. Montgomery County Supplemental Memorandum from James Babb entitled New Law Concerning Indemnity Deeds of Trust dated July 18, 2012
13. Montgomery County Affidavit for Indemnity Deed of Trust (not for recording)
14. Baltimore County Letter dated June 25, 2012 by Keith Dorsey, Director Office of Budget and Finance
15. Assistant Attorney General Bruce L. Benshoof April 1, 2005 Memorandum to Clerks of Court and Land Records Supervisors entitled Recordation Tax on Supplements to Mortgages or Deeds of Trust
16. Sample Language re: Loan Assignments (2)

1.

THE DAILY RECORD

Date: Monday, May 21, 2012
Location: BALTIMORE, MD
Circulation (DMA): 9,187 (24)
Type (Frequency): Newspaper (D)
Page: 8
Keyword: Edward J. Levin

The end of the road for IDOTs?

Buried in one of the budget bills that was enacted during the recent Special Session of the Maryland General Assembly is a measure of significant importance to real estate developers, borrowers and lenders.

The State and Local Revenue and Financing Act of 2012 (SLRFA) amends Section 12-105(f) of the Tax-Property Article of the Maryland Code ("TP") to impose a recordation tax on an indemnity mortgage or indemnity deed of trust (an IDOT) that is given in connection with a guaranteed loan that is in the amount of \$1 million or more. The new law will apply to IDOTs that are recorded on or after July 1.

The new law provides an exception if the recordation tax is paid on another instrument. This is consistent with TP §12-108(e) which provides that no recordation tax is payable on a supplemental instrument of writing.

The Special Session Material, Report on The Budget Reconciliation and Financing Act and State and Local Revenue and Financing Act (dated May 14, 2012) notes that the change in the law affecting IDOTs will generate local revenues of \$36.7 million in fiscal 2013.

IDOT bills, past and present

The bills adopted in the special session were Senate Bill 1302 and House Bill 1302. The IDOT language also was in the two budget bills filed during the regular session, HB 87 and SB 152. Under the regular-session bills, the new IDOT provisions would have applied to all instruments of record on July 1, 2012, and would have presented a substantial issue because of the retroactive effect of the bill.

On the Senate side, the IDOT language was removed from SB 152 and added to SB 523.

Senate Bill 523 passed both houses of the General Assembly, but in different forms. A conference committee was appointed to work out the differences, but the exact language of SB 523

was not agreed to and passed before *sine die* on April 9.

In the special session, the IDOT provisions of SLRFA were the same as those in SB 523.

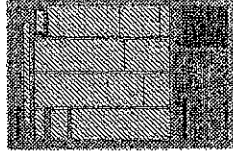
Prior to this year, bills were introduced in the General Assembly to tax IDOTs in every year from 2004 to 2011, other than 2010.[1] The General Assembly rejected each of these bills.

Background

IDOTs have been used as financing devices in Maryland for more than six decades. In general, an IDOT transaction involves a loan made by a lender to a person or an entity (the borrower) and the guaranty of that loan by a different person or entity (the guarantor). In order to secure the guaranty, the guarantor grants to the lender a mortgage or deed of trust (the IDOT) on property that it owns. Importantly for the IDOT structure, the guarantor is not primarily liable on the loan from the lender to the borrower when the IDOT is recorded. In other words, the guaranty is contingent on the occurrence of an event when the IDOT is recorded, such as a default under the loan to the borrower.

IDOTs have been the subject of a number of opinions of the Maryland attorney general, including three formal published opinions dating from 1944, 1973 and 1989.[2]

These opinions provide that no recordation tax is due upon the recording of an IDOT because as to the guarantor, which is the owner of the property encumbered by the IDOT, the "secured debt has not been incurred at the time of recording or filing the instrument of writing." See TP §12-105(f)(1). When the guarantor becomes primarily liable because the borrower defaults (usually when the borrower defaults under the loan), the guarantor then becomes liable for payment of the recordation tax. TP §12-105(f)(2).



Continued use of IDOTs

Under SLRFA, IDOTs may be employed in two situations after July 1. One is for loans of less than \$1 million. This provision (part of SLRFA, House Bill 87, Senate Bill 152, and House Bill 623) was included because many advocates of small business argued that the high recordation taxes in Maryland[3] significantly hurt small business owners. Many small businesses borrow money, and their owners guaranty the loans and secure the guaranty with IDOTs on property they own, including personal residences.

Over the years, the case for small business owners was a primary reason why bills that would have ended the use of IDOTs were defeated in Annapolis. By setting a ceiling of \$1 million before IDOTs are taxable, transactions that secure relatively small amounts will not be subject to recordation tax.

Also, IDOTs may still be used in non-loan situations where one party (the indemnitor) may become liable to another (the indemnitee), and the indemnitee wants to obtain a security interest in the property of the indemnitor should the indemnitor's liability become fixed and noncontingent.

An example of when an IDOT could still be recorded without payment of a recordation tax is described in the 1944 opinion of the attorney general that discussed IDOTs. Under the facts recited, the mortgagors acted as agents and distributors of the mortgagee's petroleum products and executed a mortgage (the IDOT) to secure any amount that they may have owed after a final accounting between the parties was conducted. The attorney general opined that the mortgage presented for recording was not subject to a recordation tax under the predecessor of TP§12-105(f) because, at the time the instrument at issue was to be recorded, "the mortgagors were not actually indebted to the mortgagee in any sum whatsoever." 29 Op. Atty. Gen. Md. at 204.

Alternatives to IDOTs

Without the ability to use IDOTs in

real estate financing transactions, lenders and borrowers will now look for other exemptions to the recordation tax statute to enable instruments to be recorded without payment of recordation taxes or to reduce the amount of recordation taxes that would otherwise be payable.

If the borrower is purchasing the subject property within 30 days of when the loan is made, the parties may use the purchase money mortgage exemption under TP §12-108(f).

If the borrower is refinancing a mortgage or deed of trust on which recordation taxes have previously been paid, the parties may use the supplemental instrument exemption set forth in TP §12-105(e)(2) and pay recordation tax on the amount by which the debt is increased from a prior mortgage to a new one. If the lender does not own the debt secured by the prior mortgage, it can first purchase the debt from the previous lender and then amend and restate the loan documents.

Individuals who refinance their principal residences (or trustees or settlors of trusts in comparable situations) may use the refinancing instrument exception of TP §12-105(g) even if the original mortgages are paid off. However, a commercial landowner must be sure that the mortgage or deed of trust it is refinancing is kept alive to use the supplemental instrument exception.

Workgroup on IDOTs

SLRFA directs the State Department of Assessments and Taxation to create a workgroup consisting of representatives of constituent groups of stakeholders to review the impact of the change in the tax on IDOTs on local government revenues and on commercial and residential real estate transactions. The workgroup is to report its findings and recommendations about the tax to the governor and the General Assembly by Dec. 31. If the members of the workgroup make a compelling case for them, perhaps IDOTs will make a comeback.

Edward J. Levin is a member of Gordon Feinblatt LLC in Baltimore. The author wishes to thank Cheri Wyron Levin for her advice and editorial suggestions on this article. Copyright © Edward J. Levin 2012. All rights reserved.

Endnotes

1. These bills were: in 2004, House Bill 1490; in 2005, House Bill 665; in 2006, House Bill 454; in 2007, House Bill 409; in 2008, House Bill 260 and Senate Bill 559; in 2009 House Bill 824 (would have been applicable to Montgomery County only); and in 2011, House Bill 420.
2. 74 Op. Atty Gen. Md. 281 (1989); 58 Op. Atty Gen. 792 (1973); and 29 Op. Atty Gen. 203 (1944).

3. Recordation tax rates vary by county or Baltimore City. They range generally from one-half percent to one percent of the amount secured by a mortgage or deed of trust.

IDOT

Indemnity Deed Of Trust



Following is information about how certain of the individual counties came to be able to issue rules about how recordation taxes are collected. As of last year, the jurisdictions that issued their own interpretations were Baltimore City and the following counties: Anne Arundel, Baltimore, Carroll, Frederick, Montgomery, and Prince George's. Cecil County may have been recently added to this list. This material is adapted from a pleading in the recordation tax case that I am involved with in the Maryland Tax Court.

Before the year 2000, in Baltimore City and in every county in the State of Maryland, except Prince George's County, recordation taxes were paid to the Clerk of the Circuit Court for the applicable county, who acted as an agent for the State. A number of counties lobbied for years for the right to collect these taxes because they were concerned that the State took too long to remit the counties' portion of the taxes, and the State charged a fee to cover its expenses. Bills were introduced and passed by the General Assembly in 1997, 1998, and 1999 to address this delay, but each of these bills was vetoed by the Governor. Finally, in 2000 House Bill 792 was enacted and signed into law as Chapter 639 of the Laws of Maryland of 2000. A copy is attached. That bill amended TP \$12-109 to provide that recordation taxes could be paid to either the Clerk of the Court or to a county official as determined by the governing body of the county. Each of the bills mentioned in this paragraph was introduced for the sole purposes of having the money paid by persons recording instruments in the land records to the State instead paid to the local jurisdiction, thus giving the counties faster access to these funds, and eliminating the fee that the State charged to administer the collection and disbursement of the taxes.[1] Although in no way was House Bill 792 (or any of the predecessor bills) intended to affect the manner in which the State recordation tax statutes were to be interpreted, or the office that issues the interpretations of the statutes, Howard County has used (and now, with SB 1302, other counties are using) House Bill 792 as a vehicle to have the county Office of Law render legal advice about when and how the county should collect recordation taxes on documents presented to be recorded among the land records.

[1] The file containing the 2000 Legislative history for House Bill 792 contains five letters lobbying about the bill, all in support of it and all focused on counties receiving tax funds more promptly and on not paying a fee to the State.

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Unofficial Copy

Q6

HB 709/99 - W&M

2000 Regular Session
01r2024

By: Delegates Marriott and Bozman

Introduced and read first time: February 10, 2000

Assigned to: Ways and Means

Committee Report: Favorable

House action: Adopted

Read second time: March 15, 2000

CHAPTER _____

1 AN ACT concerning

2 **Recordation Tax - Payment and Collection**

3 FOR the purpose of providing for collection of the recordation tax by certain county
4 officers instead of by the clerks of the circuit court under certain circumstances;
5 requiring certain county officers to deduct from the recordation tax and remit to
6 the Comptroller a certain percentage for a certain fiscal year; and generally
7 relating to the payment and collection of the recordation tax imposed on certain
8 instruments.

9 BY repealing and reenacting, without amendments,

10 Article - Tax - Property

11 Section 1-101(e)

12 Annotated Code of Maryland

13 (1994 Replacement Volume and 1999 Supplement)

14 BY repealing and reenacting, with amendments,

15 Article - Tax - Property

16 Section 12-109(b) and 12-110(a) and (b)(1)

17 Annotated Code of Maryland

18 (1994 Replacement Volume and 1999 Supplement)

19 SECTION 1. BE IT ENACTED BY THE GENERAL ASSEMBLY OF

20 MARYLAND, That the Laws of Maryland read as follows:

Article - Tax - Property

1
2 1-101.

3 (e) "Collector" includes an officer of a county or municipal corporation who has
4 a duty to collect or remit taxes.

5 12-109.

6 (b) (1) Except as provided in paragraph (2) of this subsection, the
7 recordation tax on an instrument of writing or a security agreement recorded under
8 subsection (a)(1) of this section in any county shall be paid to the COLLECTOR OR THE
9 clerk of the circuit court for the county, AS DESIGNATED BY THE GOVERNING BODY OF
10 THE COUNTY.

11 (2) In Prince George's County, the recordation tax on an instrument of
12 writing or a security agreement recorded under subsection (a)(1) of this section shall
13 be paid to the Director of Finance of Prince George's County.

14 (3) The recordation tax on a security agreement, articles of transfer,
15 articles of merger, articles of consolidation or other documents which evidence a
16 merger or consolidation of foreign corporations, foreign partnerships, foreign limited
17 liability companies, or foreign limited partnerships filed with the Department shall
18 be paid to the Department.

19 12-110.

20 (a) (1) Except as provided in subsections (c) through (e) of this section, in
21 any county except Prince George's, the recordation tax collected by the COLLECTOR
22 OR THE clerk of the circuit court shall be paid to the governing body of the county in
23 which the recordation tax was collected.

24 (2) In Prince George's County the recordation tax is both paid to and
25 collected by the Director of Finance of Prince George's County.

26 (b) (1) A person who offers for recordation an instrument of writing for
27 property located in 2 or more counties shall submit to the COLLECTOR OR THE clerk of
28 the circuit court for each county a certificate showing the apportionment of the total
29 value of the property between each of the counties.

30 SECTION 2. AND BE IT FURTHER ENACTED, That, for any county other
31 than Prince George's County, for fiscal year 2001 only, if the recordation tax under
32 Title 12 of the Tax - Property Article is not collected by the clerk of the circuit court
33 for the county, the officer of the county who collects the recordation tax shall deduct
34 from the recordation tax collected and remit to the Comptroller the percentage that a
35 clerk of the court is authorized to deduct under § 2-213 of the Courts and Judicial
36 Proceedings Article.

37 SECTION 3. AND BE IT FURTHER ENACTED, That this Act shall take effect
38 July 1, 2000.

Chapter 2

(Senate Bill 1302)

AN ACT concerning

State and Local Revenue and Financing Act of 2012

FOR the purpose of altering the State income tax rate on certain income of individuals; altering the amount allowed as a deduction for certain exemptions under the Maryland income tax under certain circumstances; modifying a fiduciary's adjusted gross income to add back that portion of an electing small business trust consisting of stock of one or more S corporations that is subject to special taxing rules under certain provisions of the Internal Revenue Code; altering certain tax rates for certain cigars and certain tobacco products; providing that, for purposes of the recordation tax, secured debt with respect to certain mortgages, deeds of trust, and other security interests in real property securing a guarantee of repayment of a loan for a certain amount is deemed to be incurred as debt is incurred on the guaranteed loan and, with respect to those mortgages, deeds of trust, and other security interests, the recordation tax applies in a certain manner; altering the amount of certain fees; repealing a certain exemption to the sales and use tax for certain sales in the form of a demurrage charge; repealing a certain modification for purposes of determining Maryland taxable income for certain public utilities; repealing a certain credit against the State income tax for certain public utilities; requiring the Comptroller to waive certain interest and penalties for a certain calendar year to a certain extent; authorizing the Comptroller to provide an alternative method of assessing and collecting a certain additional tax; requiring certain revenue to be remitted to the Comptroller by a certain date; repealing an obsolete provision; requiring the State Department of Assessments and Taxation to establish a certain workgroup; providing for the duties, composition, and chair of the workgroup; requiring the workgroup to submit a certain report to the Governor and the General Assembly by a certain date; defining certain terms; providing for the application of certain provisions of this Act; and generally relating to State and local revenues and finances.

BY repealing and reenacting, with amendments,

Article – Tax – General
 Section 10–105(a), 10–211(b), and 12–105(b)
 Annotated Code of Maryland
 (2010 Replacement Volume and 2011 Supplement)

BY repealing and reenacting, without amendments,

Article – Tax – General
 Section 10–204(a) and 10–211(a)

Annotated Code of Maryland
(2010 Replacement Volume and 2011 Supplement)

BY adding to

Article – Tax – General
Section 10–204(k)
Annotated Code of Maryland
(2010 Replacement Volume and 2011 Supplement)

BY adding to

Article – Tax – Property
Section 12–105(f)(7)
Annotated Code of Maryland
(2007 Replacement Volume and 2011 Supplement)

BY repealing and reenacting, with amendments,

Article – Health – General
Section 4–217(c)(1)
Annotated Code of Maryland
(2009 Replacement Volume and 2011 Supplement)

BY repealing and reenacting, with amendments,

Article – State Government
Section 9–1604(b)(1)(vi)
Annotated Code of Maryland
(2009 Replacement Volume and 2011 Supplement)

BY repealing

Article – Tax – General
Section 10–306(c), 10–708, and 11–202
Annotated Code of Maryland
(2010 Replacement Volume and 2011 Supplement)

SECTION 1. BE IT ENACTED BY THE GENERAL ASSEMBLY OF MARYLAND, That the Laws of Maryland read as follows:

Article – Tax – General

10–105.

(a) (1) [Except as provided in paragraph (3) of this subsection, for] FOR an individual other than an individual described in paragraph (2) of this subsection, the State income tax rate is:

- (i) 2% of Maryland taxable income of \$1 through \$1,000;

- (ii) 3% of Maryland taxable income of \$1,001 through \$2,000;
- (iii) 4% of Maryland taxable income of \$2,001 through \$3,000;
- (iv) 4.75% of Maryland taxable income of \$3,001 through **[\$150,000] \$100,000**;
- (v) 5% of Maryland taxable income of **[\$150,001] \$100,001** through **[\$300,000] \$125,000**;
- (vi) 5.25% of Maryland taxable income of **[\$300,001] \$125,001** through **[\$500,000] \$150,000**; [and]
- (vii) 5.5% of Maryland taxable income [in excess of \$500,000] OF **\$150,001 THROUGH \$250,000**; AND
- (VIII) **5.75% OF MARYLAND TAXABLE INCOME IN EXCESS OF \$250,000.**

(2) [Except as provided in paragraph (3) of this subsection, for] FOR spouses filing a joint return or for a surviving spouse or head of household as defined in § 2 of the Internal Revenue Code, the State income tax rate is:

- (i) 2% of Maryland taxable income of \$1 through \$1,000;
- (ii) 3% of Maryland taxable income of \$1,001 through \$2,000;
- (iii) 4% of Maryland taxable income of \$2,001 through \$3,000;
- (iv) 4.75% of Maryland taxable income of \$3,001 through **[\$200,000] \$150,000**;
- (v) 5% of Maryland taxable income of **[\$200,001] \$150,001** through **[\$350,000] \$175,000**;
- (vi) 5.25% of Maryland taxable income of **[\$350,001] \$175,001** through **[\$500,000] \$225,000**; [and]
- (vii) 5.5% of Maryland taxable income [in excess of \$500,000] OF **\$225,001 THROUGH \$300,000**; AND
- (VIII) **5.75% OF MARYLAND TAXABLE INCOME IN EXCESS OF \$300,000.**

[(3) For a taxable year beginning after December 31, 2007, but before January 1, 2011, the State income tax for an individual, including spouses filing a joint return or a surviving spouse or head of household as defined in § 2 of the Internal Revenue Code, is:

(i) for Maryland taxable income up to \$500,000, the rate specified in paragraph (1)(i) through (vi) or (2)(i) through (vi) of this subsection; and

(ii) for Maryland taxable income in excess of \$500,000:

1. 5.5% of Maryland taxable income of \$500,001 through \$1,000,000; and

2. 6.25% of Maryland taxable income in excess of \$1,000,000.]

10-204.

(a) To the extent excluded from federal adjusted gross income, the amounts under this section are added to the federal adjusted gross income of a resident to determine Maryland adjusted gross income.

(K) FOR A TAXABLE YEAR BEGINNING AFTER DECEMBER 31, 2012, THE ADDITION UNDER SUBSECTION (A) OF THIS SECTION INCLUDES THE AMOUNT OF INCOME OF AN ELECTING SMALL BUSINESS TRUST, AS DEFINED UNDER § 1361(E)(1) OF THE INTERNAL REVENUE CODE, THAT IS SUBJECT TO THE SPECIAL TAXING RULES UNDER § 641(C) OF THE INTERNAL REVENUE CODE.

10-211.

(a) Except as provided in subsection (b) of this section, whether or not a federal return is filed, to determine Maryland taxable income, an individual other than a fiduciary may deduct as an exemption:

(1) \$3,200 for each exemption that the individual may deduct in the taxable year to determine federal taxable income under § 151 of the Internal Revenue Code;

(2) an additional \$3,200 for each dependent, as defined in § 152 of the Internal Revenue Code, who is at least 65 years old on the last day of the taxable year;

(3) an additional \$1,000 if the individual, on the last day of the taxable year, is at least 65 years old; and

(4) an additional \$1,000 if the individual, on the last day of the taxable year, is a blind individual, as described in § 10-208(c) of this subtitle.

(b) (1) If an individual other than one described in paragraph (2) of this subsection has federal adjusted gross income for the taxable year greater than \$100,000, the amount allowed for each exemption under subsection (a)(1) or (2) of this section is limited to:

(i) **[\$2,400] \$1,600** if federal adjusted gross income for the taxable year does not exceed \$125,000;

(ii) **[\$1,800] \$800** if federal adjusted gross income for the taxable year is greater than \$125,000 but not greater than \$150,000; **AND**

(iii) **[\$1,200] \$0** if federal adjusted gross income for the taxable year is greater than \$150,000 [but not greater than \$200,000; and

(iv) \$600 if federal adjusted gross income for the taxable year is greater than \$200,000].

(2) If a married couple filing a joint return or an individual described in § 2 of the Internal Revenue Code as a head of household or as a surviving spouse has federal adjusted gross income for the taxable year greater than \$150,000, the amount allowed for each exemption under subsection (a)(1) or (2) of this section is limited to:

(i) **[\$2,400] \$1,600** if federal adjusted gross income for the taxable year does not exceed \$175,000;

(ii) **[\$1,800] \$800** if federal adjusted gross income for the taxable year is greater than \$175,000 but not greater than \$200,000; **AND**

(iii) **[\$1,200] \$0** if federal adjusted gross income for the taxable year is greater than \$200,000 [but not greater than \$250,000; and

(iv) \$600 if federal adjusted gross income for the taxable year is greater than \$250,000].

SECTION 2. AND BE IT FURTHER ENACTED, That the Laws of Maryland read as follows:

Article – Tax – General

12-105.

(b) (1) [The] EXCEPT AS PROVIDED IN PARAGRAPH (2) OF THIS SUBSECTION, THE tobacco tax rate for other tobacco products is [15%] 30% of the wholesale price of the tobacco products.

(2) (I) IN THIS PARAGRAPH, "PREMIUM CIGARS" HAS THE MEANING STATED IN § 16.5-101 OF THE BUSINESS REGULATION ARTICLE.

(II) EXCEPT AS PROVIDED IN SUBPARAGRAPH (III) OF THIS PARAGRAPH, THE TOBACCO TAX RATE FOR CIGARS IS 70% OF THE WHOLESALE PRICE OF THE CIGARS.

(III) THE TOBACCO TAX RATE FOR PREMIUM CIGARS IS 15% OF THE WHOLESALE PRICE OF THE PREMIUM CIGARS.

SECTION 3. AND BE IT FURTHER ENACTED, That the Laws of Maryland read as follows:

Article – Tax – Property

12-105.

(f) (7) (I) IN THIS PARAGRAPH, "INDEMNITY MORTGAGE" INCLUDES ANY MORTGAGE, DEED OF TRUST, OR OTHER SECURITY INTEREST IN REAL PROPERTY THAT SECURES A GUARANTEE OF REPAYMENT OF A LOAN FOR WHICH THE GUARANTOR IS NOT PRIMARILY LIABLE.

(II) EXCEPT AS PROVIDED IN SUBPARAGRAPH (III) OF THIS PARAGRAPH:

1. SECURED DEBT WITH RESPECT TO AN INDEMNITY MORTGAGE IS DEEMED TO BE INCURRED FOR PURPOSES OF THIS SUBSECTION WHEN AND TO THE SAME EXTENT AS DEBT IS INCURRED ON THE GUARANTEED LOAN; AND

2. THE RECORDATION TAX APPLIES UNDER THIS SUBSECTION IN THE SAME MANNER AS IF THE GUARANTOR WERE PRIMARILY LIABLE FOR THE GUARANTEED LOAN.

(III) THIS PARAGRAPH DOES NOT APPLY:

1. TO THE EXTENT THAT RECORDATION TAX IS PAID ON ANOTHER INSTRUMENT OF WRITING THAT SECURES PAYMENT OF THE GUARANTEED LOAN; OR

2. TO AN INDEMNITY MORTGAGE THAT SECURES A GUARANTEE OF REPAYMENT OF A LOAN FOR LESS THAN \$1,000,000.

SECTION 4. AND BE IT FURTHER ENACTED, That the Laws of Maryland read as follows:

Article – Health – General

4-217.

- (c) (1) Except as otherwise provided by law:
 - (i) The Department shall collect a \$12 fee:
 - 1. For each certified or abridged copy of a [death,] fetal death, marriage, or divorce verification certificate;
 - 2. For a report that a search of the [death,] fetal death, marriage, or divorce verification certificate files was made and the requested record is not on file;
 - 3. For each change to a [death,] fetal death, marriage, or divorce verification certificate made later than one year after the certificate has been registered with the Department; or
 - 4. To process an adoption, foreign adoption, or legitimization; [and]
 - (ii) The Department shall collect a \$24 fee:

- 1. For each certified or abridged copy of a birth certificate;

2. FOR THE FIRST COPY OF A CERTIFIED OR ABRIDGED DEATH CERTIFICATE ISSUED IN A SINGLE TRANSACTION;

- 3. For a report that a search of the birth OR DEATH certificate files was made and the requested record is not on file; or

[3.] 4. For each change to a birth OR DEATH certificate made later than 1 year after the certificate has been registered with the Department;
AND

(III) THE DEPARTMENT SHALL COLLECT A \$12 FEE FOR EACH ADDITIONAL CERTIFIED OR ABRIDGED COPY OF A DEATH CERTIFICATE PROVIDED CONCURRENTLY WITH AN INITIAL REQUESTED DEATH CERTIFICATE.

Article – State Government

9-1604.

(b) (1) The Chief Administrative Law Judge may:

(vi) assess fees to cover administrative expenses as follows:

1. to file an appeal, a fee not exceeding:
 - A. [\$125] \$150 for an appeal of a driver's license suspension or revocation related to a violation of the Maryland Vehicle Law; and
 - B. \$50 for all other types of appeals; and
2. to process a subpoena, a fee not exceeding \$5.

SECTION 5. AND BE IT FURTHER ENACTED, That Section(s) 10-306(c) and 10-708 of Article – Tax – General of the Annotated Code of Maryland be repealed.

SECTION 6. AND BE IT FURTHER ENACTED, That Section(s) 11-202 of Article – Tax – General of the Annotated Code of Maryland be repealed.

SECTION 7. AND BE IT FURTHER ENACTED, That the Comptroller shall waive any interest or penalty imposed on an individual relating to payment of estimated income tax for calendar year 2012 to the extent that the Comptroller determines that the interest or penalty would not have been incurred but for an increase in the income tax rates or reduction in the amount that may be deducted as an exemption for calendar year 2012 under Section 1 of this Act.

SECTION 8. AND BE IT FURTHER ENACTED, That, as provided in § 12-105 of the Tax – General Article, all other tobacco products used, possessed, or held in the State on or after July 1, 2012, by any person for sale or use in the State, shall be subject to the full tax on other tobacco products, as enacted under this Act. The Comptroller may provide an alternative method of assessing and collecting the additional tax. The revenue attributable to this requirement shall be remitted to the Comptroller by October 15, 2012.

SECTION 9. AND BE IT FURTHER ENACTED, That:

(a) The State Department of Assessments and Taxation shall establish a workgroup to study the impacts of imposing the recordation tax on indemnity mortgages and deeds of trust as provided under this Act, including:

- (1) The expected tax revenues to be collected for local governments;
 - (2) The impacts of the tax, if any, on the forms, volume, and value of commercial real estate transactions in urban, suburban, and rural areas of the State and on the overall commercial real estate market in the State; and
 - (3) The impacts of the tax, if any, on residential real estate transactions.
- (b) The workgroup shall include representatives from various stakeholder groups, including, but not limited to, representatives of State agencies, local governments, commercial real estate organizations, business organizations, and the Maryland Bankers Association.
- (c) The Director of Assessments and Taxation, or the Director's designee, shall chair the workgroup and facilitate the activities of the workgroup.
- (d) The workgroup shall submit a report of its findings and recommendations under this section, including a detailed description of the process used and the data relied on by the workgroup, to the Governor and, subject to § 2-1246 of the State Government Article, the General Assembly, on or before December 31, 2012.

SECTION 10. AND BE IT FURTHER ENACTED, That Section 5 of this Act and §§ 10-105(a) and 10-211(b) of Article – Tax – General of the Annotated Code of Maryland as enacted by Section 1 of this Act shall be applicable to all taxable years beginning after December 31, 2011.

SECTION 11. AND BE IT FURTHER ENACTED, That Sections 2 and 6 of this Act shall take effect July 1, 2012.

SECTION 12. AND BE IT FURTHER ENACTED, That Section 3 of this Act shall take effect July 1, 2012, and shall be applicable to all instruments of writing recorded on or after July 1, 2012.

SECTION 13. AND BE IT FURTHER ENACTED, That, except as otherwise provided in this Act, this Act shall take effect June 1, 2012.

Approved by the Governor, May 22, 2012.

A DISCUSSION OF IDOTS AND QUESTIONS AND ANSWERS ABOUT SB 1302

What is an IDOT?

In a conventional loan transaction, the borrower issues a promissory note to the lender to evidence the loan, and grants a deed of trust on real property owned by the borrower to secure repayment of the loan. The borrower is primarily and unconditionally liable for the loan, and therefore the Maryland recordation tax must be paid on the debt when the deed of trust is recorded. If the loan is advanced in stages, the borrower may elect to pay the tax either on the full loan amount when the deed of trust is recorded, or on each loan advance when made.

In an IDOT loan transaction, the borrower also issues a promissory note to the lender to evidence the loan. However, the borrower is not the owner of the real property that is to (indirectly) secure the loan. Instead, the property is owned by a third party, typically an affiliate of the borrower. The third party gives the lender a guaranty of the borrower's obligations under the note and other loan documents, and secures the guaranty—not the note itself—by an indemnity deed of trust on the property. The IDOT secures only the guarantor's liability (not the borrower's), which is only *secondary* and is *conditioned* on, typically, the borrower's default under the note or another loan document. For that reason, the Attorney General of Maryland has opined that, when the IDOT is recorded, the liability secured by the IDOT has not been "incurred" for recordation tax purposes, and therefore no recordation tax is due at that time.

Note that this structure *defers*, but does not necessarily *eliminate*, the duty to pay the recordation tax. If at a later date the borrower defaults on its loan and the guarantor becomes primarily and unconditionally liable under the guaranty, the deferred recordation tax will immediately and automatically become due from the guarantor, a tax obligation that is not eliminated by a subsequent cure of the default. On the other hand, if the loan is repaid without a default, potential liability for the recordation tax is extinguished.

IDOT Background

Indemnity deeds of trust (IDOTs) have been used for decades in Maryland to defer recordation taxes on commercial financing transactions.

During the past several years bills were introduced in the Maryland General Assembly seeking to tax IDOTs when they are recorded among the land records. In the past, such efforts failed. The General Assembly did not pass a budget during the regular legislative session in 2012, and it convened the First Special Session to deal with fiscal matters. The General Assembly enacted Chapter 2 of that special session, Senate Bill 1302, which imposes the recordation tax on IDOTs that secure loans in the amount of \$1,000,000 or more.

What is the dollar impact?

Recordation tax rates vary by county in Maryland, ranging from 0.5 percent to 1.2 percent of the principal amount of the secured debt. In the City of Baltimore the rate is 1 percent, so that a developer who borrows \$20 million for a Baltimore City project, securing the loan with a conventional deed of trust, will pay a \$200,000 recordation tax. Before July 1, 2012, the developer could defer, and possibly avoid, payment of that \$200,000 by using an IDOT instead of a conventional deed of trust.

This will no longer be possible given that the bill taxing IDOTs has passed. (An exemption in the bill, for IDOTs securing loans of less than \$1 million, will benefit few if any commercial transactions.)

Impact: The Department of Legislative Services, Office of Policy Analysis, has estimated that the tax on IDOTs will raise \$39.9 million annually on a statewide basis.

THE NEW LAW

The State and Local Revenue and Financing Act of 2012 (SLRFA) (Senate Bill 1302 and House Bill 1802) amends Section 12-105(f) of the Tax-Property Article of the Maryland Code ("TP") to impose a recordation tax on an indemnity mortgage or indemnity deed of trust (an IDOT) that is given in connection with a guaranteed loan that is in the amount of \$1,000,000 or more. The new law is effective for IDOTs that

are recorded on or after July 1, 2012.

The new law provides an exception if the recordation tax is paid on another instrument. This is consistent with TP §12-108(e) which provides that no recordation tax is payable on a supplemental instrument of writing.

SLRFA directs the State Department of Assessments and Taxation to create a workgroup consisting of representatives of stakeholders to review the impact of the change in the tax on IDOTs on local government revenues and on commercial and residential real estate transactions. The workgroup is to report its findings and recommendations about the tax to the Governor and the General Assembly by December 31, 2012.

WHAT ARE THE EXCEPTIONS?

The bill contains two exceptions.

It does not apply to the extent recordation tax is paid on another instrument of writing that secures payment of the guaranteed loan. For example, if the borrower is merely adding property to enhance the collateral for a loan and had already paid recordation tax on the loan, recordation tax would not be due on a deed of trust encumbering the additional property. Nor does the new law apply to an indemnity mortgage that secures a guarantee of repayment of a loan for less than \$1,000,000.

The new law does not alter the general provisions of TP §12-105(f), which allow the recordation tax to be paid as debt is incurred. *But see* TP §12-105(f)(6), with respect to a construction loan over \$100,000 where the total amount of the debt secured has not been incurred at the time of recording, which requires that lenders pay the recordation taxes on the principal amount of the debt when incurred. Effectively, construction borrowers can still pay the taxes incrementally, within seven days following each advance under the loan.

The new law does not amend the exemption from recordation taxes set forth in TP Section 12-108(e) for “supplemental instruments of writing.” That exemption provides that “a supplemental instrument of writing is not subject to recordation tax except to the extent that: (1) actual consideration is payable on the supplemental instrument of writing; or (2) the amount of debt is increased by the supplemental instrument of writing.” TP Section 12-101(j) defines a “supplemental instrument of writing” as “an instrument of writing that confirms, corrects, modifies, or supplements a previously recorded instrument of writing.” Accordingly, under this exemption if a borrower refinances an existing \$3 million loan, and the original deed of trust is merely modified (rather than replaced with a new security instrument),

under the supplemental instrument exemption there is a tax on the increase in the debt, and not on the pre-existing face amount of the deed of trust. This places a premium on maintaining existing deed of trust and gives lenders under existing deed of trust a competitive advantage over new loans. However, the Attorney General's office and a number of counties have issued memoranda that state that they will not apply the supplemental instrument exemption of TP Section 12-108(e) to IDOTs because no recordation tax was paid when the IDOTs were recorded.

It will be interesting to see whether a practice develops in Maryland refinance situations whereby existing IDOTs are preserved, transferred among lenders and then modified to suit the new lender's requirements.

QUESTIONS AND ANSWERS AND PRACTICE POINTERS ABOUT IDOTs ¹

Will other exemptions survive?

The proposed tax on IDOTs will not affect other exemptions available for commercial development, such as purchasing existing loan documents and amending a deed of trust (not an IDOT) already on record (which in many cases results in a tax only on new money advanced as a part of the transaction).

1. *What happens if you have an IDOT securing \$1,000,000 or more that was executed before July 1, 2012, but is recorded on or after July 1, 2012?* The instrument will be taxable. The operative date is the date of recording.

2. *What happens if you have a \$950,000 loan in which an IDOT is recorded and the IDOT is amended of record to reflect that the loan is increased by \$100,000?* The Attorney General's office and a number of counties have indicated that they will tax an IDOT on the full amount that it secures once the amount secured reaches \$1,000,000. In the example above, the tax would be based on \$1,050,000.

According to the AG: Once the amount of the loan being secured reaches \$1 million, it is subject to the new law. The supplemental instrument is the trigger, but the entire amount of the loan is now taxable. This applies regardless of whether the first IDOT was recorded before or after July 1st. Under TP Section 12-108(e), you normally would not tax a supplemental instrument on the new amount of debt secured. But, in order to claim that exemption, the debt secured by the first instrument must have been subject to the tax.

Single loan of \$1 million or more, by recording multiple IDOTs, all of which are under \$1 million?

- Statute enacted to provide additional revenue for the counties and it will be applied broadly.
- Step-transaction doctrine: *Read v. Supervisor of Assessments*
- Must demonstrate true nature of the transaction
- May be an issue relative to the spacing out of the steps
- Focus of the new statute is on the loan amount, so these IDOTs should not be taxable.

How will they know whether this is a taxable IDOT?

As of July 1, 2012 you will need to know the amount begin secured. Therefore, the following must be present:

- A copy of the promissory note;
- The guaranty agreement;
- The HUD-1 or other closing statement; and
- IDOT affidavit (see attached)

The affidavit will not be recorded, but may be retained by the county office along with a copy of the IDOT, between audit cycles. If an existing IDOT is being amended, they will need to see a copy of the original IDOT and a copy of the original note.

There is an “exception” to this rule (although it is rare). Although the instruments under discussion are called “indemnity” deeds of trust, what you normally see are “guaranty” deeds of trust, where the grantor’s obligation to repay a third party’s debt under the guaranty does not arise until the third party defaults. A true “indemnity” deed of trust secures the grantor’s own obligation, but the obligation is contingent or otherwise indeterminate. There is no debt incurred at the time the IDOT is presented because it has not yet become fixed. These may still be recorded without the payment of tax, regardless of the amount of the indemnification. And they will still be taxable when the contingency occurs.

3. *What if an IDOT that secures \$1,000,000 or more that was recorded before July 1, 2012 is amended on or after that date?* The Attorney General’s office and a number of counties have issued memoranda that indicate that the counties will tax any

substantive amendment to an untaxed IDOT on the full amount that the IDOT secures. And some counties do not care whether the amendment is substantive.

AG: Unless the new instrument is a refinance, you would only tax it on the additional amount of debt secured. If you have doubts about whether the new instrument is a supplemental instrument or a refinance, refer the question to the AG office.

What about an IDOT for \$1 million or more that is secured by real property located in Maryland and by property located in another state. If the amount of the loan that is allocated to Maryland property is under \$1 million, does the IDOT still get taxed?

AG: Yes, once the IDOT reached the \$1 million threshold, it becomes taxable, like any other deed of trust. And like any other deed of trust where the security is real property located both within Maryland and without, it is subject to allocation. You would collect the tax attributable to the Maryland real property. Some counties may only tax the IDOT if the portion of the loan allocated to Maryland is \$1 million or more.

4. *What can be done to minimize the need to record an amendment to an IDOT now that it is after July 1, 2012?* Clearly, certain amendments to IDOTs, such as changes in the property descriptions, will need to be recorded, but others may not. Consider the following:

a. *Change in maturity date.* Deeds of trust and mortgages are frequently amended because of the change of the maturity date of the indebtedness. However, there is no requirement under Maryland law that the maturity date of the indebtedness be stated in a deed of trust or a mortgage. If an IDOT contained a maturity date, the instrument could have been amended by an instrument recorded before July 1, 2012 to delete reference to the maturity date. Then, it would not be necessary to record anything in the land records if, on or after July 1, 2012, the maturity date were changed.

b. *Change in the amount secured.* Section 7-102(a)(1) of the Real Property Article of the Maryland Code ("RP") sets forth the rule that deeds of trust and mortgages must state the amount of the principal sum secured thereby. However, RP §7-102(a)(2) provides that IDOTs are not subject to this rule. Nevertheless, many IDOTs do

contain a statement of the maximum principal amount that they secure. If the amount is stated and it is to be increased, an amendment would have to be recorded. However, before July 1, 2012 the parties could have amended an IDOT by deleting reference to the amount secured. Then, it would not be necessary to record anything in the land records if the maximum amount secured were changed on or after July 1, 2012.

c. *The law imposing a tax on IDOTs amended only TP §12-105(f). It did not amend RP §7-102(a). This poses the question of how a clerk would know the principal amount of the debt secured by an IDOT that is taxable under TP §12-105(f) but does not state the principal amount of the debt secured. We can expect the clerks will require the parties to submit a statement of the principal amount of the debt secured in some form.*

5. *What if two loans involving IDOTs each secure \$750,000 and are recorded at or about the same time – will they be taxable? Under a strict reading of the new law, each IDOT should be examined separately, and because each is for less than \$1,000,000, neither should be taxable. There is the possibility that a county would contend that two loans from the same lender at the same time secured by two IDOTs from the same landowner (and perhaps relating to loans made to the same borrower) should be aggregated, causing the recordation tax to be due. Perhaps a county will claim that the loans should be combined under the step transaction theory. This does not fit the classic construct of a step transaction under federal tax law, pursuant to which courts look at the substance rather than the form of a transaction. However, the step transaction doctrine or a similar theory may be the basis used to aggregate loans.*

6. *How are IDOTs treated in Prince George's County? Prince George's County is the only jurisdiction in Maryland that imposes a transfer tax on deeds of trust and mortgages. Prince George's County does not have an exemption (or a deferral provision) for IDOTs. Therefore, IDOTs have always been subject to the Prince George's County transfer tax, and the new law will not affect that. As indicated above, IDOTs given in loan transactions over \$1,000,000 will now be subject to recordation tax.*

7. *May any IDOTs be recorded after July 1, 2012 without payment of a recordation tax? Under SLRFA, IDOTs will be able to be employed in two situations after July 1, 2012. One is for loans in the amount of less than \$1,000,000. This provision was*

included because many advocates of small business argued that the high recordation taxes in Maryland significantly hurt small business owners. Many small businesses borrow money, and their owners guaranty the loans and secure the guaranty with IDOTs on property they own, including personal residences. Over the years, the case for small business owners was a primary reason why bills that would have ended the use of IDOTs were defeated in Annapolis. By setting a ceiling of \$1,000,000 before IDOTs are taxable, transactions that secure relatively small amounts will not be subject to recordation tax.

Also IDOTs may still be used in non-loan situations where one party (the indemnitor) may become liable to another (the indemnitee), and the indemnitee may want to obtain a security interest in the property of the indemnitor should the indemnitor's liability become fixed and non contingent. An example of when an IDOT could still be recorded without payment of a recordation tax is described in the first published opinion of the Attorney General that discussed IDOTs, which was written in 1944. Under the facts recited, the mortgagors acted as agents and distributors of the mortgagee's petroleum products and executed a mortgage (the IDOT) to secure any amount that they may have owed after a final accounting between the parties was conducted. The Attorney General opined that the mortgage presented for recording was not subject to a recordation tax under the statute that was the predecessor of TP §12-105(f).

8. *What are alternatives to IDOTs in loan transactions?* Without the ability to use IDOTs in real estate financing transactions, lenders and borrowers will now look for other exemptions to the recordation tax statute to enable instruments to be recorded without payment of recordation taxes or to reduce the amount of recordation taxes that would otherwise be payable.

If the borrower is purchasing the subject property within 30 days of when the loan is made, the parties may use the purchase money mortgage exemption under TP §12-108(f) .

If the borrower is refinancing a mortgage or deed of trust on which recordation taxes have previously been paid, the parties may use the supplemental instrument exemption set forth in TP §12-105(e)(2) and pay recordation tax on the amount by which the debt is increased from a prior mortgage to a new one. If the lender does not own the debt secured by the prior mortgage, it can first purchase the debt from the previous lender and then amend and restate the loan documents. This can only

happen, however, if the existing lender agrees to sell its debt or if the existing loan documents require it to do so (unlikely).

Borrowers in new loan transactions may wish to include language in the loan documents that requires the lender to sell the loan to a subsequent lender upon the borrower's request.

Individuals who refinance their principal residences (or trustees or settlors of trusts in comparable situations) may use the refinancing instrument exception of TP §12-105(g) even if the original mortgages are paid off. However, a commercial landowner must be sure that the mortgage or deed of trust it is refinancing is kept alive to use the supplemental instrument exception.

ATAPCO HOWARD SQUARE I
BUSINESS TRUST, et al

*

No. 11-RC-OO-0805
through 0811

*

vs.

IN THE

*

HOWARD COUNTY
DEPARTMENT OF FINANCE

MARYLAND TAX COURT

*

*

MEMORANDUM AND ORDER

Petitioners, Atapco Howard Square I Business Trust, The Columbia Bank, Maple Estates, L.C., Simpson Mill, LLC, Susquehanna Bank and SFH 5, Inc. seek a refund of their payment of recordation tax, together with interest from the Respondent, Howard County Department of Finance. The relevant facts are set forth in the joint stipulation of facts with exhibits.

Petitioners claim Respondent forced the Petitioners as lenders in the transactions to pay recordation taxes on the recordation of deeds from the substitute trustees for properties sold at foreclosure sales. Petitioners contend that they willingly paid the recordation and transfer taxes on the deed that granted title to the property but were forced by Respondent to pay recordation tax on the foreclosed Indemnity Deeds of Trust as a condition of recording the deeds. Petitioners paid the recordation tax under protest with the reservation of its rights and bought these claims for refund of recordation taxes from the Respondent. The Respondent denied Petitioners' claim and Petitioners' have filed this appeal from the Respondent's denial requesting a refund of the recordation tax plus interest at 6% per annum from the date of recordation.

This case concerns a financial structure known as an Indemnity Deed of Trust

(IDOT) transaction. An IDOT transaction involves a loan to a person or entity (the "borrower") and the guaranty of that loan by a different person or entity (the "guarantor"). As security to the loan to the borrower, the guarantor grants to the lender an indemnity deed of trust on property owned by the guarantor. The guarantor under the IDOT structure is not primarily liable on the loan from the lender to the borrower. Under Tax Property Article Section 12-105 (f)(1) "...if the total amount of secured debt has not been incurred at the time of recording...the recordation tax applies only to the principal amount of the debt incurred at that time." Thus, if the guarantor is not primarily liable on the loan, the secured debt on which the recordation tax is based "has not been incurred" by the guarantor.

However, the guarantor becomes primarily liable for payment of the recordation tax when a contingency occurs such as a default under the loan to the borrower. But there is no statutory authority or legal precedent that provides for liability of any other party (i.e., the lender) other than the guarantor on an indemnity deed of trust.

Respondent further contends that Real Property Section 3-104 (b) of the annotated Code of Maryland permits Respondent to require payment of the recordation tax before a subsequent instrument may be recorded. In the present cases, the Respondent contends that it can disallow the recordation of a deed issued after a foreclosure sale if there is an Indemnity Deed of Trust in the chain of title on which recordation tax has not been paid under section 3-104 (b).

The Court finds that Real Property Section 3-104 (b) is only applicable if there are taxes, assessments or charges currently due and owed on the property. [Recordation tax in Maryland is an excise tax on the privilege of recording documents among the land records in Maryland and consequently a recordation tax is a tax on a document, not a tax

on real property. *Dean vs. Pinder*, 312 Md. 154, 159, 538 A.2d 1184 (1988).] Moreover, there is no provision in the Maryland Code in which an unpaid recordation tax constitutes a lien upon any real property merely as a result of the non-payment of that tax.

The Respondent also contends the Tax Property Section 12-105(f)6 is applicable to Indemnity Deeds of Trust. The Court finds no merit or authority supporting Respondent's statutory interpretation of Tax Property Section 12-105(f)6 in the present cases.

The court concludes the recordation tax was not the obligation of the foreclosing lender or the Petitioners and the tax did not become a lien on the respective properties. Accordingly, it is this *28th* day of *August*, 2012 hereby order that the decision of the Respondent in denying the refund claims of the Petitioner is hereby **REVERSED**, and the taxes will be refunded with interest at a rate of 6% per annum from the date the taxes were paid pursuant to Tax Property §14-917 (a).

CC: George F. Ritchie, Esq.
Gary W. Kuc, Esq.

CERTIFIED TRUE COPY

TEST: John T. Hearn, Clerk

NOTICE: You have the right of appeal from the above Order to the Circuit Court of any County or Baltimore City, wherein the property or subject of the assessment may be situated. The Petition for Judicial Review **MUST** be filed in the proper Court within thirty (30) days from the date of the above Order of the Maryland Tax Court. Please refer to Rule 7-200 et seq. of the Maryland Rules of Court, which can be found in most public libraries.

**SUMMARIES OF OFFICIALS' MEMORANDA
REGARDING IDOTS UNDER SB 1302**

Attorney General's Office, Stuart Cordish, June 15, 2012

- do not have to pay tax on IDOT if tax has been paid on another instrument – consistent with TP §12-108(e), supplemental instrument
- if an IDOT secures a loan of \$1 million or more, it is taxable in its entirety
- clerks need to know the amount secured by an IDOT, should review 1. Note, 2. Guaranty, 3. HUD-1 or other Closing Statement, and 4. IDOT Affidavit
- a \$500,000 IDOT increased to \$1.1 million is taxed on \$1.1 million because supplemental instrument exception is applicable only if debt secured by original instrument was subject to tax
- if an IDOT is taxed, then amount secured is increased, just need to tax on amount of increase “unless the new instrument is a refinance”
- ~~an IDOT is taxable if it secures a loan for \$1 million or more even if the Maryland allocation share is less than \$1 million~~
- two separate loans of \$750,000 could exist, but it is unlikely
- multiple IDOTs for a single loan of \$1 million or more should be aggregated

Howard County (undated) (pre – July 1, 2012)

- ~~misstates the law: says that all IDOTs are taxable unless recordation tax was paid on another instrument or IDOT secures a guaranty of repayment of a loan in amount under \$1 million~~
- requires submission of same 4 documents required by AG plus loan agreement
- ~~recordation tax is collectible on total amount secured by IDOT if this is an instrument confirming, correcting, modifying, amending or supplementing a previously recorded IDOT~~
- - except to the extent that tax was previously paid on an IDOT
- county will look at substance and will try to aggregate IDOTs

Baltimore County, from Keith Dorsey, Dir., Office of Budget and Finance, June 25, 2012

- ~~misstates the law~~ by saying that any IDOT in an amount of \$1 million or more will be taxable
- there is no exemption for the first \$1 million
- an amended and restated IDOT that secures \$1 million or more is subject to tax on the full amount
- an amended and restated IDOT is not subject to tax to the extent that recordation tax has been paid
- an amended and restated IDOT with the new amount of less than \$1 million will not be taxable even if the original IDOT (recorded before July 1, 2012) was for \$1 million or more
- ~~if the secured debt is \$1 million or more, IDOT will be taxable even if property is in multiple jurisdictions, but would be subject to allocation~~
- IDOTs may be aggregated
- need to present: (1) original IDOT, if one exists, (2) note, (3) guaranty, (4) loan agreement, (5) HOA-1 settlement sheet, and (6) IDOT affidavit

Montgomery County, from James Babb, Tax Operations Manager, June 15, 2012

- ~~misstates law,~~ says any IDOT in an amount of \$1 million or more will be subject to recordation tax
- says that IDOT will not be taxed if secured debt is for less than \$1 million (the focus of the law is on the loan amount)
- there is no exemption for the first \$1 million of an IDOT
- to the extent recordation tax has been paid on an IDOT, additional recordation tax will only be due on increased amount secured
- IDOTs will be aggregated
- documents to be presented are same as those required by AG plus original IDOT, if one exists

Montgomery County Supplemental Memorandum, July 18, 2012

(same as June 15 memorandum except as noted below)

- an amended and restated IDOT that amends and restates an IDOT recorded before July 1, 2012 that does not modify the amount of secured debt and is not otherwise materially changed or is not a refinance or the original IDOT – will not be subject to tax
- ~~EXAMPLES: no tax for (a) adding or subtracting properties, (b) modifying interest rate (c) changing maturity date, (d) changing trustees or (e) changing lenders~~
- EXAMPLE: changing or adding a debtor would be a material change
- IDOT is taxable to the extent of additional consideration
- EXAMPLE of additional consideration is payment by owner to lender for modifications
- ~~IDOT will be taxable if secured debt is \$1 million or more even if properties are in different jurisdictions, subject to allocation of debt among all jurisdictions of the properties. If secured debt allocated to Montgomery County is less than \$1 million, no tax will be due. [This is inconsistent with the above provisions]. If amount of secured debt allocated to Montgomery County is more than \$1 million, tax will be due on the allocative portion.~~
- ~~an assignment of an IDOT that does not amend and restate the IDOT is not taxable~~

Office of the Attorney General

Courts and Judicial Affairs Division

Phone: (410) 576-7934

Fax: (410) 576-6393

E-Mail: scordish@oag.state.md.us

15 June 2012

TO: All Clerks of Circuit Court
All Land Records Departments

FROM: Stuart Cordish, Courts Unit

SUBJECT: New Legislation – Taxation of IDOTs

Dear Folks:

As you know, Chap. 2 of the 2012 Special Session makes indemnity deeds of trust (IDOTs) taxable if they are for \$1 million or over. The new law affects IDOTs that are recorded on or after July 1, 2012.

A mortgage or deed of trust is generally is subject to the State recordation tax, and the tax is normally imposed when the instrument is presented for recording, based on the amount of the secured debt incurred. Tax-Prop. §§12-102 & 12-104.

With a guaranty (or indemnity) deed of trust, the debt has not been incurred by the grantor of the IDOT at the time the instrument is presented. The lender agrees to make a loan to the borrower if a third party, the grantor of the IDOT, guarantees its repayment. The guarantor/grantor then executes a mortgage creating the lien on its property. But because the debt has not been incurred at the time the IDOT is recorded, no tax is collected. However, if the borrower defaults on the repayment of the loan, the debt is incurred by the grantor, and the tax becomes due. Tax-Prop. §12-105(f); 74 *Op. Atty Gen.* 281 (1989).

This bill changes the landscape for IDOTs of at least \$1 million. The new law provides that for these instruments, the debt is considered to be incurred by both the borrower and the guarantor/ grantor at the same time. Because the debt is deemed incurred, these IDOTs are now taxable when presented.

The bill also provides that the tax doesn't get collected on the IDOT if the tax has already been paid on another instrument that secures the repayment of the same loan. This provision that the tax doesn't get collected on a counterpart mortgage is consistent with our interpretation of Tax-Prop. §12-108(e), which states that you don't tax a supplemental instrument.

There have been a number of questions raised as to the application of the new law, and I hope to address some of them in this memo.

Q: What is the operative date for collecting the tax?

A: The statute applies to IDOTs recorded on or after July 1. In counties where recordings are presented at more than one office, the date of recording is the date that the instrument is stamped for taxes at the first office; the first "stamp" controls.

Q: What if the IDOT is presented prior to July 1 but rejected? If it is presented again after July 1, when do we consider the IDOT to have been recorded?

A: The word has gotten out to the title companies not to wait until the last minute. If they anticipate a question as to the acceptability of the instrument, they should allow time to make corrections. The instrument will be considered recorded when the first collector accepts it and stamps it for taxes.

Q: The tax only applies to IDOTs that guarantee the repayment of loans of at least \$1 million. Even though an IDOT is for over \$1 million, does that mean that the first \$999,999 is exempt?

A: No, the bill was enacted as a revenue-generating measure for the counties and will be applied with that in mind. Once the IDOT crosses the \$1 million threshold, the entire amount is taxable.

Q: How will we know whether this is a taxable IDOT?

A: Before now, IDOTs were not required to state the amount being secured when presented for recording. Because the grantor's liability under the IDOT was contingent, no principal amount of debt had been incurred.

As of July 1, however, you will need to know the amount being secured. Therefore, you should not accept an IDOT for recording unless the following are presented:

1. A copy of the promissory note;
2. The guaranty agreement;
3. The HUD-1 or other closing statement; and
4. An IDOT affidavit (see attached)

The affidavit will not be recorded, but may be retained by your office, along with a copy of the IDOT, between audit cycles. If an existing IDOT is being amended, you will need to see a copy of the original IDOT and a copy of the original note.

There is an exception to this rule, although it is rare. Although they are called "indemnity" deeds of trust, what you normally see are "guaranty" deeds of trust, where the grantor's obligation to repay a third party's debt under the guaranty doesn't arise until the third party defaults.

A true "indemnity" deed of trust secures the grantor's own obligation, but the obligation is contingent or otherwise indeterminate. There is no debt incurred at the time the IDOT is presented, because it has not yet become fixed. These may still be recorded without the payment of tax. And they will still be taxable when the contingency occurs.

Q: Suppose an IDOT for \$500,000 is recorded without the payment of tax, and the IDOT is later amended to reflect that the loan being secured was increased by \$600,000. Do we charge tax, and on what amount?

A: Once the amount of the loan being secured reaches \$1 million, it is subject to the new law. The supplemental instrument is the trigger, but the entire amount of the loan is now taxable. This applies regardless of whether the first IDOT was recorded before or after July 1.

Under Tax-Prop. §12-108(e), you normally would not tax a supplemental instrument except on the new amount of debt secured. But, in order to claim that exemption, the debt secured by the first instrument must have been subject to the tax.

Q: Suppose an IDOT for over \$1 million is taxed and recorded. If an amendment is recorded that increases the secured loan amount, do we tax it based on just the increased debt, or tax it based on the new full amount of the loan?

A: Unless the new instrument is a refinance, you would only tax it on the additional amount of debt secured. If you have doubts about whether the new instrument is a supplemental instrument or a refinance, please refer the question to our office.

Q: What about an IDOT for more than \$1 million that is secured by real property located in Maryland *and* by property located in another state. If the amount of the loan that is allocated to Maryland property is under \$1 million, does the IDOT still get taxed?

A: Yes, once the IDOT crosses the \$1 million threshold, it becomes taxable, like any other deed of trust. And like any other deed of trust where the security is real property located both within Maryland and without, it is subject to allocation. You would collect the tax attributable to the Maryland real property.

- Q: Could you have two separate loans for \$750,000, each involving an IDOT from the same grantor, secured by the same property and presented at or about the same time, and record each IDOT without the payment of the tax?
- A: Possible but unlikely. If the transactions are truly independent of each other, then technically each gets recorded without the payment of recordation tax. Odds are you won't see that very often.
- Q: Tax Avoidance. What happens if the grantor tries to avoid the tax on a single loan of \$1 million or more, by recording multiple IDOTs, all of which are under \$1 million? How would we know this is occurring?
- A: This statute was enacted specifically to provide additional revenue for the counties, and it will be applied as broadly as the law permits. If a single taxable transaction is disguised, by breaking it down into multiple steps to avoid payment of the tax, we will consider "collapsing" those steps back into one taxable transaction. The "step transaction" doctrine, approved by the Court of Appeals in *Read v. Supervisor of Assessments*, 354 Md. 383 (1999), permits the collector to look at the true substance of a transaction and disregard the form.
- Therefore, the party who submits the IDOT for recording must be prepared to demonstrate the true nature of the transaction by presenting the guaranty, the promissory note, and the HUD-1 or closing statement, along with the affidavit as to the total principal amount of the debt being secured.
- If, for example, you see a \$2 million promissory note, but the IDOT secures only \$750,000, that should raise a red flag, and you can be on the lookout for the rest of the "steps." Granted, it is more difficult to apply the doctrine as the steps are spaced farther apart, but if you have doubts about the taxability of an instrument, please contact our office.

I expect additional questions to arise. We'll blow up those bridges as we come to them.

attachment

AFFIDAVIT FOR IDEMUNITY DEED OF TRUST

(to accompany IDOT presented to the Clerk of the Court)

For Clerk's Use Only - NOT FOR RECORDING

By signing below, I hereby certify, affirm, and declare, under penalty of perjury, that the accompanying Indemnity Deed of Trust meets the following requirements for exclusion from Recordation Tax:

- The grantor of the IDOT is a separate and distinct entity from the maker of the note, and is not obligated under the note.
- The grantor of the IDOT has signed a guaranty of the note.
- The IDOT secures only the guaranty.
- The grantor of the IDOT is not primarily liable for the indebtedness.
- The proceeds of the loan have not been used to acquire the property secured by the IDOT.
- The amount of the secured debt of the IDOT or the amended and restated IDOT is _____.
- The parcel identification number is _____.

Signed this _____ day of _____

By _____

Print Name _____

Signer is (please check one choice below):

Lender's Attorney _____

Settlement Attorney _____

Party to the IDOT _____



HOWARD COUNTY DEPARTMENT OF FINANCE

3430 Courthouse Drive ■ Ellicott City, Maryland 21043 ■ 410 -313 -2389

Recordation Tax Office
recordation@howardcountymd.gov

FAX 410-313-3293
TDD 410-313-2323

Recordation Tax – Indemnity Deeds of Trust

Change in Recordation Tax Law:

The State and Local Revenue and Financing Act of 2012 (“Act”) was enacted for the purpose of generating revenue for the counties in Maryland. A provision of the Act makes the recordation tax on Indemnity Mortgages collectible at the time the Indemnity Mortgages are recorded among the land records.

In accordance with Tax Property Article Section 12-105(f)(7), on or after July 1, 2012, recordation tax will be collected on all Indemnity Mortgages presented for recordation among the Land Records of Howard County, Maryland, unless the indemnity mortgage is within one of the following two exceptions:

- (1) To the extent the recordation tax was paid on another instrument of writing that secures payment of the guaranteed loan; or
- (2) The Indemnity Mortgage secures a guarantee of repayment of a loan in an amount less than one million dollars.

The term Indemnity Mortgage is defined in the statute and includes indemnity deeds of trust or IDOTs.

Effective Date:

Recordation tax will not be collected on any Indemnity Mortgage presented to and date stamped by the Recordation Tax Office, with the associated guaranty, promissory note, loan agreement, and closing statement, on or before June 29, 2012. Recordation tax will be assessed on any Indemnity Mortgage rejected by the Recordation Tax Office on or before June 29, 2012 and resubmitted on or after July 1, 2012. Recordation tax will be assessed on any Indemnity Mortgage received by the Recordation Tax Office on or after July 1, 2012.

Implementation:

As of July 1, 2012, all Indemnity Mortgages presented to the Recordation Tax Office must be accompanied with the following documents:

- (1) Guaranty
- (2) Promissory Note
- (3) Loan Agreement
- (4) Closing Statement/HUD 1
- (5) Affidavit For Indemnity Deed of Trust (Recordation Tax Office Form)

Recordation tax will be collected on the total amount secured by the Indemnity Mortgage if any instrument of writing confirming, correcting, modifying, amending, or



HOWARD COUNTY DEPARTMENT OF FINANCE

3430 Courthouse Drive ■ Ellicott City, Maryland 21043 ■ 410 -313 -2389

Recordation Tax Office
recording@howardcountymd.gov

FAX 410-313-3293
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Recordation Tax – Indemnity Deeds of Trust
Page 2

supplementing a previously recorded Indemnity Mortgage is presented for recordation unless one of the two exceptions above applies. For example:

- (1) If a previously recorded IDOT securing an amount of less than one million dollars is amended to secure more than one million dollars, recordation tax will be collected on the total amount secured by the IDOT.
- (2) If a previously recorded IDOT securing an amount of more than one million dollars is amended, corrected, modified, or supplemented, and no recordation tax was previously collected on the IDOT, recordation tax will be collected on the total amount secured by the IDOT.
- (3) If a previously recorded IDOT is amended, corrected, modified or supplemented, and recordation tax was previously collected on the IDOT, then recordation tax will be collected on the difference between the amount in the new instrument of writing and the outstanding principal balance of the original loan.

The Recordation Tax Office will examine the substance and all the surrounding circumstances of the transaction for any Indemnity Mortgage presented for recording in order to determine whether steps have been taken to avoid recordation tax on the Indemnity Mortgage. If, under applicable law, the transaction for the Indemnity Mortgage qualifies for aggregation with any other Indemnity Mortgage, whether previously recorded or also presented for recording, the Recordation Tax Office will collect recordation tax on the aggregate amount of such Indemnity Mortgages. This notice is intended to implement the Act only and to supplement rather than replace other Recordation Tax Office policies with regard to collecting recordation tax on Indemnity Mortgages.

As with all transactions, documents may be previewed by request. Questions should be directed to Leslie Bennett at 410-313-2389 or lbennett@howardcountymd.gov.



HOWARD COUNTY DEPARTMENT OF FINANCE
3430 Courthouse Drive ■ Ellicott City, Maryland 21043 ■ 410-313-2389

Recordation Tax Office
recordation@howardcountymd.gov

FAX 410-313-3293
TDD 410-313-2323

10.

AFFIDAVIT FOR INDEMNITY DEED OF TRUST

*For Recordation Tax Use Only – **NOT FOR RECORDING***

By signing below, I hereby certify, affirm, and declare, under the penalties of perjury, that the following information is true with respect to the Indemnity Deed of Trust (“IDOT”) presented for purposes of computing Recordation Tax in accordance with the laws of the state of

Maryland:

- The amount of the note referenced in the IDOT is \$ _____.
- The amount of the secured debt of the IDOT or the amended and restated IDOT is \$ _____.
- The IDOT is secured by the parcel with tax identification number _____.

Signed this _____ day of _____

By _____

Print Name _____

Name of Company: _____

Company or Individual is the Lender _____, Grantor _____, or Settlement Agent _____.

M E M O R A N D U M

TO: Clients of Montgomery County Transfer/Recordation Tax Office

FROM: James Babb, Tax Operations Manager

DATE: June 15, 2012

SUBJECT: New Law Concerning Indemnity Deeds of Trust

The Transfer Office is hereby notifying you of new legislation which affects calculation of recordation tax on indemnity deeds of trust (IDOT's) presented to us for processing. The General Assembly recently adopted the State and Local Revenue and Financing Act of 2012 (the Act). The Act contains a provision that amends Section 12-105(f) of the Tax-Property Article and states that any IDOT in an amount of \$1,000,000 or more will be subject to recordation tax. The Act takes effect July 1, 2012, and applies to all instruments of writings recorded on or after July 1, 2012.

The following is a description of how Montgomery County will treat new and/or amended and restated IDOT's for purposes of payment of recordation tax. I realize that there may be other questions and issues that arise as the process proceeds and they will need to be handled on a case by case basis as those questions and issues arise.

1. An IDOT presented to the Montgomery County Transfer Office and date stamped by the Transfer Office on or before June 29, 2012, will be treated as recorded before July 1, 2012, and will not be subject to recordation tax. If an IDOT that was submitted to the Transfer Office on or before June 29, 2012 and was rejected by the Transfer Office and then resubmitted on or after July 1, 2012 the new law will apply.
2. An IDOT that is presented to the Transfer Office after July 1, 2012, where the secured debt is less than \$1,000,000, will not be subject to recordation tax.
3. An IDOT that is presented to the Transfer Office on or after July 1, 2012, where the secured debt is \$1,000,000 or more, will be subject to recordation tax on the entire amount of the secured debt. There is no exemption for the first \$1,000,000.

Example: A \$2,000,000 IDOT presented to the Transfer Office will be taxable based on \$2,000,000 of secured debt.

4. An amended and restated IDOT that is presented to the Transfer Office on

or after July 1, 2012, and the amount of the secured debt in the original IDOT is increased to an amount that is \$1,000,000 or more, will be subject to recordation tax on the entire amount of the secured debt.

Example: An IDOT for \$750,000 was recorded prior to July 1, 2012, that is amended and restated and the secured debt is increased to \$2,000,000 will be taxable based on \$2,000,000 of secured debt.

5. An amended and restated IDOT that is presented to the Transfer Office on or after July 1, 2012, where the secured debt on the original IDOT that was recorded on or after July 1, 2012, is \$1,000,000 or more and recordation tax was paid on the entire amount of the original secured debt will be subject to recordation tax on the increased amount of the secured debt as stated in the amended and restated IDOT less the principal balance of the original secured debt.

6. An amended and restated IDOT that is presented to the Transfer Office on or after July 1, 2012, where the secured debt on the original IDOT is \$1,000,000 or more and the original IDOT was recorded prior to July 1, 2012, and the secured debt is reduced to less than \$1,000,000, will not be subject to recordation tax.

Example: An IDOT for \$2,000,000 was recorded prior to July 1, 2012, and is amended and restated and the secured debt is reduced to \$900,000. No recordation tax will be collected.

7. If several IDOT's are submitted either at the same time or close to the same time with the secured debt on some or all of them being less than \$1,000,000, the IDOT's may be aggregated and taxed if the total is \$1,000,000 or more. The Transfer Office will take into account the substance and nature of the transaction and if it is determined that the intent of presenting several IDOT's is to avoid the tax, the IDOT's will be aggregated and taxed accordingly.

8. The following documents will need to be presented with an IDOT or an amended or restated IDOT:

1. The original recorded IDOT, if one exists.
2. A copy of the note or the original or amended promissory note as applicable.
3. The Guarantee Agreement.
4. The HUD-1 settlement sheet.
5. The IDOT Affidavit.

SUPPLEMENTAL MEMORANDUM

TO: Clients of Montgomery County Transfer/Recordation Tax Office

FROM: James Babb, Tax Operations Manager

DATE: July 18, 2012

SUBJECT: New Law Concerning Indemnity Deeds of Trust

The Transfer Office is hereby notifying you of new legislation which affects calculation of recordation tax on indemnity deeds of trust (IDOT's) presented to us for processing. The General Assembly recently adopted the State and Local Revenue and Financing Act of 2012 (the Act). The Act contains a provision that amends Section 12-105(f) of the Tax-Property Article and states that any IDOT in an amount of \$1,000,000 or more will be subject to recordation tax. The Act took effect July 1, 2012, and applies to all instruments of writings recorded on or after July 1, 2012. This memorandum supplements the memorandum previously issued by the Transfer Office on June 15, 2012.

The following is a description of how Montgomery County will treat new and/or amended and restated IDOT's for purposes of payment of recordation tax. I realize that there may be other questions and issues that arise as the process proceeds and they will need to be handled on a case by case basis as those questions and issues arise.

1. An IDOT presented to the Montgomery County Transfer Office and date stamped by the Transfer Office on or before June 29, 2012, will be treated as recorded before July 1, 2012, and will not be subject to recordation tax. If an IDOT that was submitted to the Transfer Office on or before June 29, 2012 and was rejected by the Transfer Office and then resubmitted on or after July 1, 2012 the new law will apply.
2. An IDOT that is presented to the Transfer Office on or after July 1, 2012, where the secured debt is less than \$1,000,000, will not be subject to recordation tax.
3. An IDOT that is presented to the Transfer Office on or after July 1, 2012, where the secured debt is \$1,000,000 or more, will be subject to recordation tax on the entire amount of the secured debt. There is no exemption for the first \$1,000,000.

Example: A \$2,000,000 IDOT presented to the Transfer Office will be taxable based on \$2,000,000 of secured debt.

4. An amended and restated IDOT that is presented to the Transfer Office on or after July 1, 2012, and the amount of the secured debt in the original IDOT is increased to an amount that is \$1,000,000 or more, will be subject to recordation tax on the entire amount of the secured debt.

Example: An IDOT for \$750,000 was recorded prior to July 1, 2012, that is amended and restated and the secured debt is increased to \$2,000,000 will be taxable based on \$2,000,000 of secured debt.

5. An amended and restated IDOT that is presented to the Transfer Office on or after July 1, 2012, that amends and restates an original IDOT that was recorded prior to July 1, 2012, that does not modify the amount of the secured debt and is not otherwise materially changed or is not a refinance of the original IDOT, the amended and restated IDOT will not be subject to recordation tax.

Example: Some examples of modifications that would not trigger the tax on the amended and restated IDOT include: (a) adding or substituting properties as collateral; (b) modifying the loan interest rate; (c) altering the maturity date of the loan; (d) changing the trustees under the IDOT; (e) changing the name of the lender.

After review of the documents, if it is determined that there is a material change to the transaction and/or there is a refinance of the original IDOT, the amended and restated IDOT will be taxable on the full amount of the secured debt.

Example: An example of a material change would include a change or addition of a debtor.

After review, if it is determined that there was additional consideration paid for the amended and restated IDOT and the amended and restated IDOT is not otherwise taxable as being materially changed or refinanced, then recordation tax will be due on the additional consideration which is being paid for the amended and restated IDOT. If it is determined that the amended and restated IDOT is otherwise taxable the additional consideration will be added to the consideration as stated above.

Example: An example of additional consideration would include payment by the owner to the lender for the modifications.

6. An amended and restated IDOT that is presented to the Transfer Office on or after July 1, 2012, where the secured debt on the original IDOT that was recorded on or after July 1, 2012, is \$1,000,000 or more and recordation tax was paid on the entire amount of the original secured debt will be subject to recordation tax on the increased amount of the secured debt as stated in the amended and restated IDOT less the principal balance of the original secured debt.

Example: An IDOT for \$1,500,000 was recorded and recordation tax was

paid on the amount of the original secured debt and the principal balance is \$1,000,000, and the IDOT is increased to \$2,000,000, will be taxable on the difference between \$2,000,000 and the principal balance of \$1,000,000 of the existing IDOT for a total taxable amount of \$1,000,000.

7. An amended and restated IDOT that is presented to the Transfer Office on or after July 1, 2012, where the secured debt on the original IDOT is \$1,000,000 or more and the original IDOT was recorded prior to July 1, 2012, and the secured debt is reduced to less than \$1,000,000, will not be subject to recordation tax.

Example: An IDOT for \$2,000,000 was recorded prior to July 1, 2012, and is amended and restated and the secured debt is reduced to \$900,000. No recordation tax will be collected.

8. If several IDOT's are submitted either at the same time or close to the same time with the secured debt on some or all of them being less than \$1,000,000, the IDOT's may be aggregated and taxed if the total is \$1,000,000 or more. The Transfer Office will take into account the substance and nature of the transaction and if it is determined that the intent of presenting several IDOT's is to avoid the tax, the IDOT's will be aggregated and taxed accordingly.

9. An IDOT or amended and restated IDOT presented to the Transfer Office on or after July 1, 2012, where the secured debt is \$1,000,000 or more, will be subject to tax even if it places a lien on properties in multiple jurisdictions. The IDOT will be subject to allocation of the debt between all of the properties identified in the instrument. If the secured debt allocated to Montgomery County property is less than \$1,000,000, then no tax will be due. If the amount of the secured debt allocated to Montgomery County property is more than \$1,000,000 then tax will be due on the entire amount of the debt allocated to the Montgomery County property.

10. An assignment of an IDOT that does not otherwise amend and restate the IDOT would not be subject to recordation tax under Section 12-108(j) of the Tax-Property Article.

11. The following documents will need to be presented with an IDOT or an amended or restated IDOT:

1. The original recorded IDOT, if one exists.
2. A copy of the note or the original or amended promissory note as applicable.
3. The Guarantee Agreement.
4. The HUD-1 settlement sheet.

5. The IDOT Affidavit.

Montgomery County reserves the right to make appropriate inquiries and ask for appropriate documentation concerning the amount of the secured debt, any material changes to the documents or any other related documents as necessary to determine whether the IDOT is taxable.

AFFIDAVIT FOR IDEMUNITY DEED OF TRUST
(to accompany IDOT presented to Montgomery County Transfer Office)

For Transfer Office Use Only – NOT FOR RECORDING

By signing below, I hereby certify, affirm, and declare, under penalty of perjury, that the accompanying Indemnity Deed of Trust meets the following requirements for exclusion from Recordation Tax:

- The grantor of the IDOT is a separate and distinct entity from the maker of the note, and is not obligated under the note.
- The grantor of the IDOT has signed a guaranty of the note.
- The IDOT secures only the guaranty.
- The grantor of the IDOT is not primarily liable for the indebtedness.
- The proceeds of the loan have not been used to acquire the property secured by the IDOT.
- The amount of the secured debt of the IDOT or the amended and restated IDOT is _____.
- The parcel identification number is _____.

Signed this _____ day of _____

By _____

Print Name _____

Signer is (please check one choice below):

Lender's Attorney _____

Settlement Attorney _____

Party to the IDOT _____



KEVIN KAMENETZ
County Executive

KEITH DORSEY, Director
Office of Budget and Finance

June 25, 2012

Dear Clients of Baltimore County Transfer/Recordation Tax Office:

Re: New Law Concerning Indemnity Deeds of Trust

The Transfer Office is hereby notifying you of new legislation which affects calculation of recordation tax on indemnity deeds of trust (IDOT's) presented to us for processing. The General Assembly recently adopted the State and Local Revenue and Financing Act of 2012 (the "Act"). The Act contains a provision that amends Section 12-105(f) of the Tax-Property Article and states that any IDOT in an amount of \$1,000,000 or more will be subject to recordation tax. The Act takes effect July 1, 2012, and applies to all instruments of writings recorded on or after July 1, 2012.

The following is a description of how Baltimore County will treat new and/or amended and restated IDOT's for purposes of payment of recordation tax. I realize that there may be other questions and issues that arise as the process proceeds and they will need to be handled on a case by case basis as those questions and issues arise.

1. An IDOT presented to the Baltimore County Transfer Office and date stamped by the Transfer Office on or before June 29, 2012, will be treated as recorded before July 1, 2012, and will not be subject to recordation tax. If an IDOT that was submitted to the Transfer Office on or before June 29, 2012 was rejected by the Transfer Office and is then resubmitted on or after July 1, 2012, the new law will apply.
2. An IDOT presented to the Transfer Office after July 1, 2012, where the secured debt is less than \$1,000,000, will not be subject to recordation tax.
3. An IDOT presented to the Transfer Office on or after July 1, 2012, where the secured debt is \$1,000,000 or more, will be subject to recordation tax on the entire amount of the secured debt. There is no exemption for the first \$1,000,000.
Example: A \$2,000,000 IDOT presented to the Transfer Office will be taxable based on \$2,000,000 of secured debt.
4. An amended and restated IDOT presented to the Transfer Office on or after July 1, 2012, where the amount of the secured debt in the original IDOT is increased to an amount that is \$1,000,000 or more, will be subject to recordation tax on the entire amount of the secured debt.

Example: An IDOT for \$750,000 recorded prior to July 1, 2012, that is amended and restated increasing the secured debt to \$2,000,000 will be taxable based on \$2,000,000 of secured debt.

5. An amended and restated IDOT presented to the Transfer Office on or after July 1, 2012, where the secured debt on the original IDOT that was recorded on or after July 1, 2012, is \$1,000,000 or more and on which recordation tax was paid on the entire amount of the original secured debt, will be subject to recordation tax on the increased amount of the secured debt as stated in the amended and restated IDOT.

Example: An IDOT for \$2,000,000 recorded on or after July 1, 2012, on which tax has been paid, that is amended and restated increasing the secured debt to \$2,500,000 will be taxable based on \$500,000 of increased secured debt.

6. An amended and restated IDOT presented to the Transfer Office on or after July 1, 2012, where the secured debt on the original IDOT is \$1,000,000 or more, the original IDOT was recorded prior to July 1, 2012, and the secured debt is being reduced to less than \$1,000,000, will not be subject to recordation tax.

Example: An IDOT for \$2,000,000 was recorded prior to July 1, 2012, and is amended and restated and the secured debt is reduced to \$900,000. No recordation tax will be collected.

7. An IDOT presented to the Transfer Office on or after July 1, 2012, where the secured debt is \$1,000,000 or more will be subject to tax, even if it secures properties in multiple jurisdictions, but would be subject to allocation.

8. If several IDOT's are submitted in a transaction, either at the same time or close to the same time, with the secured debt on each one being less than \$1,000,000, the Transfer Office will take into account the nature of the transaction, and if it is determined that the intent of presenting several IDOT's is to avoid the tax, the IDOT's will be aggregated and taxed accordingly.

8. The following documents will need to be presented with an IDOT or an amended or restated IDOT:

1. The original recorded IDOT, if one exists.
2. A copy of the original or amended promissory note as applicable.
3. The Guaranty Agreement.
4. The Loan Agreement.

5. The HUD-1 settlement sheet.
6. The IDOT Affidavit.

The County reserves the right to make inquiries, as it deems appropriate, into the amount of the secured debt, and to require additional documentation, as necessary.

Sincerely,



Keith Dorsey
Director

Office of the Attorney General
Courts and Judicial Affairs Division
200 St. Paul Place
Baltimore, Maryland 21202

Phone: (410) 576-7292
Fax: (410) 576-6393
E-Mail: bbenshoof@oag.state.md.us

DATE: 1 April 2005

To: All Clerks of the Circuit Courts
cc: All Land Records Supervisors

From: Bruce L. Benshoof,
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Re: Recordation Tax on Supplements to Mortgages or Deeds of Trust

After careful review of the relevant legislative history and cases, I have concluded that the advice which Julia Freit provided to you in memoranda dated May 24, 1990 and April 16, 1990 (copies of which are attached) was, unfortunately, incorrect. Therefore, such memoranda of advice are hereby withdrawn and replaced with the following advice.

It is important to remember that there are two different "amounts" of debt with respect to each mortgage or deed of trust: (1) the "secured amount" (or "amount secured," "full face amount," or "maximum outstanding principal sum"), and (2) the "amount incurred."¹ At the time of recording, the "secured amount" and the "amount incurred" may be the same (e.g., a mortgage

¹ This distinction is also found in the Real Property Article. For example, Real Prop. § 7-102 provides that, unless the obligation "secured" is contingent (i.e. a guaranty or indemnity mortgage or deed of trust for which there is not yet a "direct" debt secured or incurred), a mortgage or deed of trust must state the "aggregate principal sum" to be secured by it, but then the mortgage or deed of trust secures up to that amount with priority as of its recording, regardless of when the debt is actually advanced or re-advanced.

For example, assume First Lender records a mortgage for \$100,000, but only advances \$10,000. Then Second Lender records a mortgage for another \$100,000 and advances that whole sum. Next First Lender advances another \$10,000 under its mortgage. If the lenders were to then foreclose on the property, under Maryland law, First Lender would have first position for all \$20,000 it has advanced, because First Lender would have priority for up to \$100,000. So if the foreclosure proceeds were only \$110,000, First Lender would get the first \$20,000, and Second Lender would get only the remaining \$90,000.

This is quite different from the rule in some other states (such as Illinois) in which First Lender would have first position only for the \$10,000 advanced first, next Second Lender would have priority for the next \$100,000, and then First Lender would have priority for the \$10,000 advanced after Second Lender's advance. So if the foreclosure proceeds were only \$110,000, First Lender would get the first \$10,000, but then Second Lender would get the next \$100,000 - leaving nothing for First Lender's second \$10,000.

secures a maximum of \$100,000 and the lender has initially advanced, and thus the debtor has "incurred," all \$100,000), or they may be very different (e.g., a "credit line" deed of trust "secures" a maximum of \$100,000, but only \$10,000 has been advanced by the lender, and thus "incurred" by the debtor).

If recordation tax was paid on the maximum amount secured by the original mortgage or deed of trust – regardless of whether paid on such original mortgage or deed of trust because the amount of debt then incurred equaled the maximum amount secured or because recordation tax was paid on the "maximum outstanding principal sum," in accordance with Tax-Prop. § 12-105(f)(4), even though "the total amount of secured debt has not been incurred" – then recordation tax is due on a supplement only to the extent that the secured amount (i.e. the "face amount" or "maximum outstanding principal sum") is increased.

Furthermore, if the secured amount is increased, but not all of such increase is then incurred, the debtor may choose to pay recordation tax on the supplement computed on either (A) the amount of debt incurred in excess of the prior maximum secured amount (in accordance with Tax-Prop. § 12-105(f)(1) through (3)), or (B) the total amount of the increase to the "secured debt."

If recordation tax was paid on the amount initially incurred (and such "amount incurred" was less than the "amount secured"), then the debtor may choose to pay recordation tax on the supplement computed on either (A) the amount of debt by which the debt incurred exceeds the amount on which recordation tax has been paid on the original instrument (whether initially, in accordance with Tax-Prop. § 12-105(f)(1), or thereafter, in accordance with Tax-Prop. § 12-105(f)(2)), or (B) the new maximum amount of debt secured, less the amount on which recordation tax has been paid on the original instrument (whether initially, in accordance with Tax-Prop. § 12-105(f)(1), or thereafter, in accordance with Tax-Prop. § 12-105(f)(2)).

Please note that in either situation, another exemption may reduce the amount of recordation tax that would otherwise be due. For example, the refinance exemption under Tax-Prop. § 12-108(g) may exempt an increase to one loan to the extent that the proceeds of such increase are used to refinance another loan secured by the property.

EXAMPLES

- (1) Debtor grants a mortgage in the face amount of \$100,000. All \$100,000 is advanced and incurred as debt at the time of recording, and so recordation tax is computed and paid on all \$100,000. Later, Lender and Debtor execute a

supplement to the mortgage increasing its maximum face amount to \$150,000. Immediately prior to such supplement, Debtor had paid the original loan down to \$90,000. At the time of such supplement, Lender re-advances \$10,000 of the original \$100,000 plus all \$50,000 of the increase. Recordation tax on the supplement is properly computed on the \$50,000 increase above the amount secured on which recordation tax was previously paid (not on the \$60,000 difference between the new loan amount of \$150,000 and the immediately prior principal balance of \$90,000).

(2) Debtor grants a mortgage in the face amount of \$100,000. All \$100,000 is advanced and incurred as debt at the time of recording, and so recordation tax is computed and paid on all \$100,000. Time passes and Debtor pays down the debt to \$50,000, at which point Debtor asks Lender to re-advance \$25,000. For whatever reason, Debtor and Lender also agree to execute a supplement that reduces the face amount secured to \$75,000. No recordation tax would be due on such supplement because it reduces, rather than increases, the amount secured (and should not be computed based on the \$25,000 re-advance in connection with such supplement).

(3) Debtor grants a credit-line mortgage in the face amount of \$100,000. Only \$75,000 is initially advanced, but, in accordance with Tax-Prop. § 12-105(f)(4), Debtor elects to compute and pay recordation tax on the full secured amount of \$100,000. Then, Lender agrees to increase Debtor's credit limit to \$150,000, and Debtor decides to draw an additional \$50,000 (increasing the debt incurred to \$125,000). Lender and Debtor execute a supplement to increase the maximum amount secured to \$150,000. Debtor may choose to compute and pay recordation tax on the full increase to the secured amount (\$50,000) or may choose to pay only on the amount of debt incurred above the original \$100,000 (\$25,000).

DISCUSSION

As you know, the Tax-Prop. § 12-108(e) provides that:

A supplemental instrument of writing is not subject to recordation tax except to the extent that:

actual consideration is payable on the supplemental instrument of writing; or

the amount of debt is increased by the supplemental instrument of writing.

This exemption was enacted as part of Chapter 8 of the 1985 Laws of Maryland, which Act re-codified parts of former Article 81 as the Tax-Property Article. As indicated in the Act, § 12-108(e) was derived, without intending substantive change, from former Art. 81,

§ 277(h) & (i), which addressed supplements to instruments securing debt and supplements to all other instruments, respectively. (Parts of such former subsections became the term "supplement instrument of writing" defined in Tax-Prop. § 12-101(g).) Because only supplements to instruments securing debt concern us herein, only Art. 81, § 277(h) needs to be addressed herein. Art. 81, § 277(h) provided that:

No tax shall be required for the recordation of any instrument securing a debt that merely confirms, corrects, modifies or supplements an instrument previously recorded, or conveys or pledges property in addition to, or in substitution for the property originally conveyed or pledged, if such supplemental instrument does not increase the amount of the debt secured by the instrument previously recorded. *[emphasis added]*

As noted above, the re-codification of former Art. 81, § 277(h) & (i) as Tax-Prop. §§ 12-101(g) and 12-108(e) was not intended to effect any substantive change. Whether the word "secured" after the phrase "the amount of debt" was left out as superfluous or as an oversight, the meaning was clearly intended to remain the same. Therefore, we must read the relevant part of Tax-Prop. § 12-108(e) as if it stated:

A supplemental instrument of writing is not subject to recordation tax except to the extent that . . . the amount of debt secured is increased by the supplemental instrument of writing.

Similarly, former Art. 81, § 277(k) was the precursor to Tax-Prop § 12-105(f)(1) through (3). Such subsection originally stated:

If the total amount of the debt which may become secured by any instrument securing a debt shall not have been incurred at the time such instrument is offered for record, the tax shall be computed solely in the principal amount of the debt then incurred and secured by such instrument. Before any additional debt is incurred which is to be secured by an instrument previously recorded, the debtor shall file with the clerks of the courts with which such instrument has been recorded a duly verified statement showing the amount of such additional debt and shall pay tax with respect thereto upon, but only upon, the amount of such additional debt so secured which has been incurred after May 31, 1937 *[i.e. after the recordation tax took effect]*, and with respect to which such tax shall not theretofore have been paid, less the principal amount of any debt then outstanding and secured by such instrument which is to be paid or refunded out of the proceeds of such additional debt.

As you may have noticed, the option to pay on the full secured amount (now embodied in Tax-Prop. § 12-105(f)(4)) was not an explicit part of in the original Art. 81, § 277(k). At first, that option was only made explicitly available for "consumer borrowers" with the provision that for such borrowers "the total tax liability shall be satisfied by payment of tax based on the aggregate principal sum, whether expressed as the aggregate principal amount or the maximum credit line." The option was made explicitly available to all borrowers by

Chapter 599 of the 1988 Laws of Maryland, which amended Tax-Prop. § 12-105(f)(4) as follows:

~~If the borrower under paragraph (1) of this subsection is a consumer borrower, as defined in § 12-901 of the Commercial Law Article, the~~ The ~~recording tax may be computed and paid on the aggregate~~ maximum ~~outstanding~~ principal sum, however expressed, that is stated to be secured by the instrument of writing, without regard to the amount of secured debt actually incurred, advanced, or readvanced.

Other than the change to allow all borrowers to take advantage of such paragraph, the other changes were described as "clarifying."

Finally, as held by the Court of Special Appeals in the case of Howard County v. Howard Research and Dev. Corp., 34 Md. App. 411 (1977):

when the modifying document includes a previously unsecured obligation, the recording tax properly will be calculated only upon that previously untaxed obligation and may not be levied upon the sums so refunded. *[emphasis added]*

(Id. at 418) In other words, the intent and policy here is similar to the intent and policy behind the purchase money mortgage exemption – generally, don't tax the same dollars twice.²

² Of course this "don't tax twice" policy is only one of the competing policies inherent in the recording and transfer tax laws – for example, "assumed debt" is generally part of the "consideration payable" on a deed, regardless of whether such debt was already taxed.

Assignment of Loan Documents. Notwithstanding anything to the contrary contained herein, at Borrower's election in consideration of payment in full of all amounts on account of the Loan and/or secured by this Deed of Trust (including, but not limited to, principal, interest, any prepayment amounts, swap termination or similar amounts and all accrued fees on account of the Loan,) Lender hereby agrees that it will assign the Loan Documents, at Borrower's request and direction, to the designee of Borrower, without representation or warranty and without recourse to Lender. Such assignment shall be at no cost to Lender and Borrower shall pay to Lender all fees and other costs incurred by Lender in connection with the assignment of the Loan and the Loan Documents.

Assignment of Loan Documents. In order to enable Borrower to refinance the Loan without paying excess costs, Lender agrees that upon Borrower's written request, Lender will sell and transfer the Loan, the loan documents, and all security for the loan, at par, to a new lender designated by Borrower ("Assignee"). Lender with endorse the Note to Assignee without recourse. Lender's transfer shall be made without recourse other than Lender shall represent and warrant to Assignee as follows:

(a) Lender is the owner of and holds the Loan and the Loan Documents free and clear of any lien or encumbrance, and Lender has the right, power and authority to assign the Loan to Assignee.

(b) The Loan is fully reflected on Schedule 1 [list of documents to be drafted and attached], without amendment except as set forth thereon.

(c) Lender has obtained all necessary consents to the assignment of the Loan from any participants holding interests in the Loan.

(d) There are no amounts due and owing by Borrower to Lender which are not reflected in the Payoff Statements.

(e) Lender has not, in whole or in part, released its lien or encumbrance on the Property described in the Deed of Trust or of any obligations of the Borrower under the Loan.

Lender shall not impose any cost, fee, or expense in connection with the assignment of the Loan (other than reasonable out-of-pocket expenses, including attorneys' fees not in excess of \$ _____). Lender shall cooperate and shall timely take any and all action necessary for the transfer of the Loan to occur on such date as may be determined by Borrower.