LAND RECORDING SEMINAR

Special Issues Session

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RECORDING SEMINAR
SPECIAL ISSUES
"STICKY WICKETS"

A "sticky wicket" is defined in *Webster's II New Riverside University Dictionary*, 1988, at p. 1139, as " [a] problem ... that is ... difficult." This advance training seminar is designed to address those sticky wickets, both old and new, that crop up routinely as the land records department personnel are endeavoring to process instruments for recording. Thanks are extended to all the clerks who assisted by completing and submitting the surveys to help identify the difficult problem areas that are in need of clarification and advice.

I. Recording Issues.

Question 1: When is a financing statement recorded in the clerk's office, in addition to or instead of being filed with the State Department of Assessments and Taxation, and why is it filed in the clerk's office?

Answer 1: A financing statement is filed with the clerk when it belongs in the land records because the personal property collateral on which the financing statement creates a lien is attached to real property. The collateral is fixtures, not-yet-cut timber, not-yet-harvested crops, or not-yet-extracted minerals. Such a financing statement must include a description of the real property to which the personal property is attached and must identify the owner of the real property if other than the debtor on the financing statement. If the owner of the real property later enters into a transaction to sell or encumber the real property, a title search will reveal that there is a lien on the fixtures, timber, crops, or minerals. This knowledge may affect the amount of consideration the buyer is willing to pay or the amount of loan the lender is willing to make.

Question 2: When is a power of attorney recordable?

Answer 2: A power of attorney that authorizes the attorney-in-fact to convey or encumber real property of the grantor of the power may be recorded in the land records before it is used in connection with the execution of a deed, mortgage, or other instrument affecting the real property of the grantor, at the time the deed or other instrument is recorded, or after the deed or other instrument is recorded. If the power of attorney is not recorded before or at the time the deed or other instrument is recorded, it may be recorded subsequently only if: (1) the power of attorney was executed and acknowledged before the execution of the deed or other instrument; (2) the power of attorney was not revoked prior to the recording of the deed or other instrument; and (3) the deed or other instrument contained or was subsequently supplemented by a written affidavit of the attorney-in-fact stating that he or she had no knowledge, at the time the deed or other instrument was executed, of any revocation of the power of attorney by death, disability, or incompetence of the grantor of the power. *See* Real Property Article, §4-107.

Question 3: What is the difference between a modification of a deed of trust and a refinance deed of trust?

Answer 3: When a deed of trust is modified by the filing of a supplemental instrument, the original deed of trust is not released. A release of the original deed of trust releases the supplement, and *vis a versa*. *See* Real Property Article, §3-105(h). The two instruments depend on each other for continuing viability. By contrast, a refinance deed of trust does not supplement a previously recorded deed of trust, it replaces it. The refinance deed of trust secures a new loan that is used to pay off the balance due on the prior deed of trust that is being refinanced. The prior deed of trust is released.

Question 4: Does an assignment of rents and profits and other rights and interests of a landlord under an unrecorded lease require the presentation of the underlying lease and payment of recording taxes on the lease if its original or any renewal term exceeds 7 years?

Answer 4: No. Tax-Property Article, §§12-105(e) and 13-205(c) provide that if a document that publicizes or gives constructive notice of an unrecorded lease is recorded, the original lease must be submitted and recording taxes paid thereon if the lease is one that is subject to tax (*i.e.*, a lease in which any term, original or renewal, exceeds 7 years). The statute includes examples of type of document that triggers submission of the lease; the list includes: an attornment agreement (an agreement whereby the tenant agrees to hold the tenancy as the tenant of a new landlord); a memorandum of lease (a brief synopsis of the lease allowed to be recorded under Real Property Article, §3-101(e)); and an assignment of lease. The term "assignment of lease" is not defined in the Tax-Property Article; the term "instrument of writing" is defined, for purposes of recordation and transfer taxes, as including, among other items, an assignment of a lessee's interest in real property. Tax-Property Article, §§12-101(c)(2)(iv) and 13-101(c)(2)(iii). However, the term "assignment of lease" is defined in *Black's Law Dictionary*, 7th ed., p. 115, as "[a]n assignment in which a lessee transfers the entire unexpired remainder of the lease term." Thus, "assignment of lease" generally refers to the assignment of the leasehold interest by the tenant, as distinguished from an assignment of rents and profits, and other rights and interests, that a landlord has under a lease.

The term "assignment of lease" as used in Tax-Property Article, §§12-105(e) and 13-205(c), is construed as not including an assignment by a landlord not only because of the generally accepted definition of the term, but also because the burden of the tax on the lease is imposed on the tenant. Tax-Property Article, §§12-105(e)(3) and 13-205(c)(3) provide that unless the parties agree otherwise, as allowed by Tax-Property Article, §§12-111 and 13-102, "the lessee is chargeable with the ... tax on the original lease." In a transaction in which the landlord is getting a loan from a lender and pledging the rents and profits under the unrecorded lease as collateral to secure repayment of the loan, the tenant is not a party. The lender may insist on the recording of the assignment of rents and profits. The tenant has no interest in the recording of this assignment and derives no benefit from its recording. Under such circumstances, it would be patently unfair to charge the tenant with the recording taxes on the unrecorded lease as a condition of the assignment being recorded.

Question 5: Can the clerk insist that an allocation statement be filed when a deed of trust covering property in more than one county is recorded?

Answer 5: Yes. Tax-Property Article, §12-110(b)(1) provides as follows: "A person who offers for recordation an instrument of writing for property located in 2 or more counties **shall submit to the clerk** of the circuit court for each county **a certificate showing the apportionment** of the total value of the property between each of the counties." (Emphasis added.) Subparagraph (ii) of ¶(2) of subsection (b) explains the basis for the tax in each county; the statutory provision states that the tax in each county is "based on the ratio that the value of the property in that county bears to the value of the property in all counties." Therefore, the required certificate should reflect the value of each property and show the ratio of each property to the sum of all properties, either as a fraction or percentage, that is then multiplied by the debt secured to compute the portion of the secured debt subject to tax in each county.

Question 6: Is an assignment of proceeds of sale recordable and taxable?

Answer 6: No. An assignment of proceeds of sale assigns the assignor's right to receive money, the cash proceeds from the sale of real property, to the assignee to satisfy some outstanding debt or obligation. This instrument does not convey any title to real property and, ordinarily, does not create a lien or encumbrance on real property. Therefore, the instrument does not "affect" real property. As stated in several opinions of the Attorney General's Office, while an instrument that has a legal effect on real property is recordable pursuant to Real Property Article, §3-102(a), an instrument that does not affect real property is not recordable unless a specific statutory provision makes that type of instrument recordable. There is no statute making an assignment of proceeds of sale recordable.

If an assignment of proceeds of sale includes a provision stating that a lien is imposed on the described real property, then the assignment becomes recordable as an "equitable mortgage," an instrument intended to serve the same function as a mortgage. If it is recordable, it is also taxable. The recordation tax would be based on the outstanding debt secure by the lien.

Question 7: What criteria apply to the legibility of an instrument that is being recorded, and what authority does a clerk have regarding acceptance of an instrument that will not be legible when microfilmed?

Answer 7: If an instrument is not legible when recorded, whether by microfilming, electronic imaging, or other method of recording, its recording does not serve the intended function of providing constructive notice to the world regarding the transfer of title, creation of lien, or other purpose being effectuated by the instrument. To assure that the records are legible, Real Property Article, §3-104(e) establishes, for instruments being offered for recording, certain criteria regarding the size and color of type or print, and the color and weight of the paper. The subsection further provides that if an instrument does not conform and is not otherwise "readily subject to photostating or microfilming," the instrument may not be received for recording until: (1) triple the normal recording charge is paid; and (2) an affidavit, in black type on white paper, is attached to the

nonconforming instrument and made part of it, "stating the kind of instrument, the date, the parties to the transaction, description of the property, and all other pertinent data." Essentially, the affidavit (signed statement made under penalties of perjury) will repeat the substantive contents of the nonconforming instrument. When a title searcher comes across the illegible instrument in the records, the searcher will find the accompanying affidavit that sets forth the contents of the instrument.

In 40 *Opinions of the Attorney General* 128, 132 (1955), commenting on the statutory provisions that preceded §3-104(e), the Attorney General's Office stated that the statutes "would seem to indicate the legislative intent to call for recording standards conducive to easy understanding and legibility, and as a measure to bring about such clarity, exacts extra fees in the event of non-compliance with those statutes." The original statutes did not require the affidavit. In 43 *Opinions of the Attorney General* 114 (1958), the Attorney General's Office concluded that the statute did not permit the clerk to refuse to accept a noncomplying instrument as long as triple the fee was paid. By Acts of 1969, Chapter 472, the General Assembly added the affidavit requirement. The purpose clause accompanying this legislative Act indicated that the amendment to the statute was intended "to require an affidavit listing all pertinent information to be filed with any instrument to be recorded when said instrument is of poor quality for reproduction purposes." Because the law now requires the affidavit, as well as payment of triple the recording charges, as a condition for acceptance of a noncomplying instrument for recording, the clerk may refuse to accept an instrument for recording that is not accompanied by the requisite affidavit and fee.

Question 8: Is a copy of a document or note acceptable for recording if accompanied by a lost note or lost document affidavit?

Answer 8: No. Maryland does not have a law that authorizes the recording of a copy of a document if accompanied by a lost document affidavit.

Question 9: Other than a disclaimer, a copy of which may be recorded in land records pursuant to Estate and Trusts Article, §9-202(c), is there any law that permits a copy of an instrument to be recorded in land records?

Answer 9: The only law authorizing the recording of a copy of a document in land records is Real Property Article, §3-104(e). That statute provides that once a document is recorded in some official records in Maryland or in another state, commonwealth, territory, or possession of the United States, a copy certified by the official custodian of such government-maintained records may be accepted for recording.

Question 10: What is the difference between a rerecording and a supplemental instrument (modification)?

Answer 10: A rerecording of a previously recorded instrument involves the recording of the same original instrument, or a duplicate original, with **no changes** to the original instrument. By contrast,

a supplemental instrument involves some modification to the original instrument. The supplemental instrument may be created by taking the original instrument, or a copy of it, and making the modification on the original or copy. The modification must be initialed or signed by a party. In the alternative, a supplemental instrument may be drafted from scratch, identifying the original instrument, explaining the error or omission in the original that is being corrected, and setting forth the modification or addition. Sometimes the deed of trust is completely rewritten, including such changes as the parties desire, and title as an amended and restated deed of trust. Rerecordings are relatively rare; supplemental instruments are fairly common.

Question 11: Can a supplemental instrument modifying a deed be recorded to change the grantee?

Answer 11: Generally no. It would be a rare circumstance that a grantor would convey the property to the wrong grantee and that the wrongly-named grantee would accept the deed at settlement without knowing that the property was supposed to be conveyed to someone else. In the event that such an unlikely mutual mistake occurred, the original grantor would have to execute a corrective deed, and the wrongly-named grantee would have to join in the corrective deed, conveying the property to the grantee who was intended to get the property but was inadvertently not named in the original deed. To support the claim of mutual mistake, the parties should proffer some evidence, such as the written contract of sale underlying the original deed that indicates that the intended grantee is the one identified in the corrective deed.

Question 12: May the clerk refuse to accept for recording a deed of trust that fails to identify the trustee or identifies the trustee only by the title of a position in an office (*e.g.*, manager of the regional office of HUD)?

Answer 12: Yes. Real Property Article, §3-302(a) provides as follows:

> The clerk of the circuit court of each county shall make and maintain a full and complete general alphabetical index of every deed, and other instrument in a well-bound book in his office. The index shall be both in the name of each grantor, donor, mortgagor, and assignor, and each grantee, donee, mortgagee, or assignee.

The grantee on a deed of trust is the trustee. In Real Property Article, §4-401(1), the enumerated items that any deed must contain to be sufficient include "the names of the grantor and grantee." ("Deed" is defined in Real Property Article, §1-101(c) as including a deed of trust.) In 1886, the Court of Appeals held that the designation of a grantee in a deed as the owner of a certain house was not sufficient. *See Schaidt v. Blaul*, 66 Md. 141. The Court explained:

> By the common law it was not necessary that the name of the grantee should be inserted in a deed, provided he was described with sufficient certainty to distinguish him from all other persons. If a grant were made to the earl of Essex, or the duke of Norfolk, without other description, it was good; because there could not be two persons at the same time holding either of these titles, and therefore the identification

> of the grantee would be complete. And probably to describe a grantee as heir of John Thompson [a deceased person] would be sufficient, inasmuch as the character of heir would show the person intended with sufficient certainty. But the ownership of a house is a casual circumstance, which is liable to change from time to time, and does not impress upon an individual any permanent characteristic by which he may be identified. We cannot, therefore, hold that such a description is sufficient to enable any one to claim as grantee in a deed; and we might probably go further, and say that the proper construction of the ninth section of article 24 of the Code requires that the name of the grantee should always be set forth in the deed.

Even under common law, the identification of the grantee by reference to a job title would not have been sufficient. As the Court indicated in the above-quoted passage, the Maryland laws on the registration (recording and indexing) of deeds likely replaces common law and requires the name of the grantee in any deed.

Question 13: If a clerk accepts for recording a deed of trust that fails to name a trustee, must the clerk accept the recording of the corrected deed of trust without payment of the recording fee?

Answer 13: No. While the clerks may refused to accept an instrument proffered for recording if it does not satisfy the prerequisites for recording, failure of the clerk to catch the deficiency and refuse the instrument does not entitle an interested person to file a supplemental instrument correcting the deficiency without payment of the ordinary recording fees. While there is an exemption from recording taxes for a supplemental instrument under Tax-Property Article, §§12-108(e) and 13-207(a) (4), there is no exemption from recording fees under Real Property Article, §§3-601 through 3-603 for a supplemental instrument.

Question 14: What is a "homestead deed"?

Answer 14: A homestead deed is not a deed. A resident of Virginia who is a debtor in a Virginia insolvency (bankruptcy) proceeding may exempt assets (cash or property) up to a certain value from the insolvency estate that will be liquidated to pay the creditors. The assets so exempted may include real property, even real property owned by the debtor in another state. When the value of the debtor's equity in the real property does not exceed the amount of allowable exemption, the property may be declared exempted from the insolvency estate by filing a document called a "homestead deed."

Question 15: When does the surcharge apply and when not?

Answer 15: Courts and Judicial Proceedings Article, §13-604(a) provides that the State Court Administrator may establish a surcharge "for each type of **recordable instrument** to be recorded among the land records and the financing statement records." (Emphasis added.) The term "recordable instrument" is defined in §13-601(d) as "(1) [a] deed defined in §1-101 of the Real Property Article; and (2) [a]ny other instrument affecting property that may be recorded under §3-102 of the Real Property Article." The term "deed," as defined in Real Property Article, §1-101(c),

includes: "any deed, grant, mortgage, deed of trust, lease, assignment, and release, pertaining to land or property or any interest therein or appurtenant thereto, including an interest in rents and profits from rents." All such instruments are subject to the surcharge. In addition to all the instruments comprehended by the generic term "deed" as defined in §1-101(c), Real Property Article, §3-102(a) provides that "[a]ny other instrument **affecting property**, including any contract for the grant of property, or any subordination agreement establishing priorities between interests in property may be recorded." (Emphasis added.) As stated in 73 *Opinions of the Attorney General's Office* 345, 348 (1988), "[t]his provision, like similar predecessor language, has long been understood to require that the instrument itself affect title to land." To affect property, an instrument generally must either convey an interest in the property or create a lien or encumbrance on the property. In the above-referenced opinion, the Attorney General's Office concluded that a covenant not to convey or encumber is not recordable because it does not affect property and is not otherwise made recordable by a specific statute.

A few examples of instruments that do not fall within the generic definition of "deed" and do not affect real property, but are recordable by reason of a specific statute, are: a power of attorney recordable pursuant to Real Property Article, §4-107; a transfer of development rights recordable pursuant to Article 66B, §13.01(k); and an assumption and/or release of personal liability agreement recordable pursuant to Real Property Article, §3-102(b). These instruments are not subject to the surcharge.

II. Recording Tax Issues:

Question 1: When is a "zero consideration" deed subject to recording taxes and when not?

Answer 1: When the grantor is receiving nothing of economic value in exchange for the conveyance, the consideration payable is truly zero, and the tax based on zero consideration is zero. Often a deed that states that the consideration is zero is not accurate. Perhaps the grantor is not receiving any **monetary** consideration (cash), but the grantor is receiving something of economic value. In that case, the "consideration payable" is not zero. The consideration payable is the value of the economic benefit received.

For example, if the grantor is exchanging one real property for another (which is known as a "like kind exchange" for purposes of avoiding liability for capital gains tax), the grantor is receiving something of economic value for the conveyance. The grantor is not giving real property away for nothing; the grantor is receiving, as "consideration payable" for the conveyance, another parcel of valuable and marketable real property, which may be sold and, thereby, converted into cash. The same is true if the grantor is trading real property for a valuable painting or other tangible personal property. Sometimes the grantor is receiving, as consideration payable for the conveyance of real property, intangible personal property such as stock in a corporation, shares in a business trust, membership interest in a limited liability company, or partnership interest in a partnership. As stated by the two appellate courts in Maryland, even if the grantor obtained the stock, shares, or membership or partnership interest prior to making the conveyance of real property to the

corporation, business trust, limited liability company, or partnership, the value of the stock, shares, or membership or partnership interest is being increased as a result of the conveyance of the real property to the grantee entity. The increase in value is a real economic benefit to the grantor and constitutes "consideration payable" for the conveyance. After the conveyance of real property to the entity, the grantor may sell the ownership interests in the entity for that much more than before the conveyance. Another form of consideration payable to the grantor is relief from a debt or obligation that the grantor owes. In some cases, the grantee is taking the real property subject to a mortgage or deed of trust that secures repayment of a debt that the grantor owes. The grantee agrees to pay the balance due on the secured debt. This relief from paying the debt constitutes consideration to the grantor. Similarly, if the grantor owes a debt to the grantee and the grantee agrees to accept title to the real property in exchange for marking the debt satisfied, the relief from repaying the debt to the grantee constitutes consideration to the grantor for the conveyance.

Question 2: When does a deed to a limited liability company (LLC) qualify for the exemption under Tax-Property Article (TP), §12-108(y)?

Answer 2: By opinion dated October 12, 1999, 84 *Opinions of the Attorney General* ___ [Opinion No. 99-015], the Attorney General's Office held that a conversion of a partnership to an LLC may be either by the statutory method under Corporations and Associations Article ("CA"), §4A-211 or by a non-statutory method. Under the statutory method, the articles of organization for the LLC must include the name of the converting partnership, its date of formation, and, if of the type to be registered (*e.g.*, a limited partnership), the filing reference for its certificate of registration. Under CA §4A-213(a), the converting partnership and the LLC to which it converts are deemed the same entity. The partnership does not dissolve; rather, it becomes an LLC. This is like the sofa that converts into a bed; the sofa does not cease to exist, it has simply changed in appearance and function. Similarly, CA §4A-212 provides that a sole proprietorship may be converted into a single member LLC. The articles of organization must include the name of the sole proprietor and a description of the property used in the business. Under CA §4A-213(b), the assets and liabilities of a converting partnership or proprietorship are vested in the LLC to which the partnership or proprietorship converts. In such a case, the clerk generally will receive for recording a confirmatory deed reflecting that, by operation of the conversion accomplished by the filing of the articles of organization, the real property asset is now owned by the LLC to which the partnership or proprietorship converted. The clerk should be shown a copy of the filed articles of organization that include the information required by §4A-211 or §4A-212, as appropriate. A conversion of a partnership or proprietorship to an LLC is not the same as a contribution of real property to a preexisting LLC. Under the conversion, the LLC comes into being as a result of the conversion. The partnership or proprietorship and LLC never exist as distinguishable operations at the same time.

Under the non-statutory method of conversion referenced in the October 12, 1999 opinion, the partnership dissolves and all its assets and liabilities are conveyed to the LLC consisting of the same owners (LLC members), with the same percentage of profits and losses as they had as partners of the dissolving partnership. In this case, the partnership ceases to exist and is replaced by the newly formed LLC. The deed submitted for recording should reflect that the partnership is

dissolving and that the members of the LLC to which the property is being conveyed are the same, with the same percentage of profits and losses, as the partners of the dissolving partnership.

Part of the confusion, to date, has arisen because of the inclusion in TP §12-108(y) of a reference to a proprietorship, consisting of one or more persons, under the definition of "predecessor entity." A proprietorship, as that term is defined and commonly used, is an unincorporated business owned and operated by one individual. A proprietorship is not an "entity;" on that point, it is notable that CA §4A-213(a) does not include any reference to a converting proprietorship when providing that a converting partnership and the LLC to which it converts are deemed the same entity. Additionally, the term generally is not used to refer to a business owned and operated by more than one person.

There is pending legislation that, **if enacted**, will resolve this confusion. House Bill 1187, as rewritten, will remove from TP §12-108(y) the reference to a proprietorship and will create a new subsection (aa) in TP §12-108. The new subsection will provide that a contribution of real property owned by one or more individuals, even property jointly owned by a married couple as tenants by the entireties, to an LLC will not be subject to State transfer and recordation taxes under certain circumstances. The property owner(s) must be engaged in a business enterprise involving principally the buying, selling, leasing, or managing of real property. The property owner(s)/operator(s) of the enterprise must be the member(s) of the LLC to which the property is conveyed, with the same percentage of profits and losses as before the conveyance. The conveyance must be for no consideration other than issuance of the membership interest(s). Operation of the enterprise is discontinuing; thereafter the business will be operated as the LLC. All real property owned by the individual(s) and used in the enterprise must be conveyed to a single LLC.

Question 3: What simple rules can be applied in determining the proper amount of recording taxes on deeds from agencies and instrumentalities of the United States Government, such as the Department of Housing and Urban Development (HUD), the Veteran's Administration (VA), etc. that are exempt or immune from paying such taxes?

Answer 3: The clerk must first note whether the deed is a qualifying first-time Maryland home buyer deed. If so, the State transfer tax due is zero because State law imposes that tax on the seller, at the reduced rate of .25%, and does not allow it to be contractually shifted to the buyer. The State recordation tax and county transfer tax, if any, payable on the deed may also be zero. The State law presumes that such taxes will be paid by the seller on a first-time home buyer deed unless the parties contractually agree otherwise. While it makes little sense for the parties to contractually shift the taxes to the buyer, thereby losing the advantage of the seller's exemption or immunity, sometimes the parties do so. In that event, the clerk may receive payment of some or all of the State recordation tax and, if the clerk is the collector of the county transfer tax, some or all of the county transfer tax. Any purchase money mortgage accompanying the deed is exempt from State recordation tax only to the extent such tax is paid on the deed. Thus, if no recordation tax is paid on the deed, the mortgage will be taxable on the full debt secured. If some recordation tax is paid on the deed, the

amount of consideration subjected to tax on the deed may be deducted from the amount of secured debt in the mortgage, and recordation tax then paid on the balance of the secured debt.

Example - first-time Md. home buyer deed and mortgage: (Using a State recordation tax rate of $5.00 per $1,000 and a county transfer tax rate of 1%)

(1) State law presumption applies; parties have not contractually provided otherwise:

Deed consideration: $150,000
State transfer tax: $0
State recordation tax: $0
County transfer tax: $0

Mortgage secured debt: $110,000

State recordation tax: $550

(2) Parties contractually provide for a 50/50 split of the taxes:

Deed consideration: $150,000
State transfer tax: $0
State recordation tax: $375
County transfer tax: $750

Mortgage secured debt: $110,000

State recordation tax: $175

If the deed does not qualify as a first-time Maryland home buyer deed, State law presumes that the taxes will be divided equally between seller and buyer unless the parties contractually agree otherwise. In that event, half the taxes would fall on the seller. Since the seller is exempt or immune from paying such taxes, the clerk may receive only half the State transfer, State recordation, and county transfer taxes. Again, while it makes little sense for the parties to contractually shift the taxes to the buyer, thereby losing the advantage of the seller's exemption or immunity, sometimes the parties do so. In that event, the clerk may receive payment of more than half of the recording taxes. As explained above, any purchase money mortgage will only be exempted from recordation tax to the extent such tax was paid on the deed.

Example - non first-time Md. home buyer deed and mortgage: (Using a State recordation tax rate of $5.00 per $1,000 and a county transfer tax rate of 1%)

(1) State law presumption applies; parties have not contractually provided otherwise:

Deed consideration: $150,000
State transfer tax: $375
State recordation tax: $375
County transfer tax: $750

Mortgage secured debt: $110,000

State recordation tax: $175

(2) Parties contractually provide for buyer to pay all the taxes:

Deed consideration: $150,000
State transfer tax: $750
State recordation tax: $750
County transfer tax: $1,500

Mortgage secured debt: $110,000

State recordation tax: $0

If any taxes are paid in excess of the minimum amounts payable, the taxes should be accepted. The law permits parties to seek a refund of any tax mistakenly or erroneously paid.

Question 4: Can a mortgage qualify as both a purchase money mortgage and a refinance mortgage?

Answer 4: Sometimes, when an individual is purchasing a residence and currently owns real property, on which there is an existing mortgage, the purchase money lender wants a lien on both properties to secure repayment of the loan, but does not want the lien on the currently owned property to be subordinate to the existing mortgage debt. In that event, the purchase money lender will require the purchaser to borrow, in addition to the purchase money, enough to pay off (refinance) the balance due on debt secured by the existing mortgage. In that way, the new lender's mortgage will constitute a first lien on both properties.

Only if the newly purchased property is not intended to be the buyer's principal place of residence, and the currently owned property is and will continue for an indefinite time to be the purchaser's principal place of residence, will the mortgage qualify for both the purchase money exemption and the refinance exemption. If the newly purchased property is intended by the buyer to be his or her principal place of residence, then the existing residence, albeit used to date as the buyer's principal residence, no longer qualifies as his or her principal residence. To qualify as a principal residence, the residence must be the one at which the owner intends to reside for an indefinite period of time and to which the owner intends to return after any temporary absences (business trips, vacations, etc.). When the buyer of the newly purchased property intends to shortly move into the new residence, and to sell or lease out the existing residence, or keep it as a vacation home, the existing home is not the one at which the owner intends to reside for an indefinite period of time and to which the buyer intends to return after any temporary absences. Thus, the deed of trust on the newly purchased home and the current home will qualify for the purchase money mortgage exemption, but not for the refinance exemption.

Question 5: What are the criteria for determining whether a guaranty deed of trust ("idot") qualifies to be recorded without payment of recordation tax?

Answer 5: There is no exemption from recordation tax for a guaranty deed of trust under Tax-Property Article, §12-108 (Exemptions from tax). The reason tax is not paid upon the recording of a guaranty deed of trust is because Tax-Property Article, §12-105 (Calculation of tax) provides in subsection (f)(1) that the tax need not be paid until the secured debt is incurred. "Incur" is defined in *Black's Law Dictionary*, 7th ed., at p. 771, as "[t]o suffer or bring on oneself (a liability or

expense)." When a person other than the borrower gives the lender a guaranty of payment of the borrower's debt, under which guaranty the person will become liable for the debt if the borrower defaults on payment, the guarantor's debt to the lender is not yet "incurred." The guarantor's debt will be "incurred" only if the borrower defaults. If the guarantor gives a deed of trust on the guarantor's property **to secure the guarantor's obligation under the guaranty**, the deed of trust qualifies for the tax deferral under §12-105(f)(1). Recordation tax will only become due if the borrower defaults, at which point the guarantor's liability for the debt will be incurred.

If a deed of trust is given by a person other than a borrower, but is given to secure the borrower's obligation under the note, such a deed of trust secures a debt that has been incurred. The debt evidenced by the note has been incurred by the borrower. Thus, such a deed of trust does not qualify for the tax deferral afforded mortgages and deeds of trust that secure debts not yet incurred. Nothing in the Tax-Property Article provides that a mortgage given to secure a debt incurred by someone other than the mortgagor is exempt from recordation tax.

To determine whether a deed of trust qualifies for the tax deferral afforded a deed of trust that secures a not-yet-incurred debt, the clerk must review the "to secure" clause of the deed of trust, in addition to verifying that the grantor of the deed of trust did not co-sign the note. If, for example, the deed of trust provides that it is given to secure "the Obligations as herein defined," and "Obligations" is defined as including the borrower's obligation under the note, the deed of trust does not qualify for the tax deferral under §12-105(f)(1) because it secures, among other things, the borrower's already-incurred debt under the note.

Question 6: What is a "mirror note" and what effect does it have on the recording of an guaranty deed of trust without payment of recordation tax?

Answer 6: Sometimes a loan transaction is structured to appear, in form, to be one in which the deed of trust will qualify as a guaranty deed of trust, but, in substance, is equivalent to loan to the "guarantor," grantor of the deed of trust. The lender lends the money to a "borrower;" the "borrower" executes a note to the lender and the "guarantor" executes a guaranty and a guaranty deed of trust to the lender. As part of the same transaction, the "borrower" lends the loan proceeds to the "guarantor;" the guarantor executes a note (the "mirror note") to the "borrower." The interjection of the "borrower" into the transaction to act as a pass-through agent between the lender and the "guarantor" is simply done to avoid the recordation tax on the deed of trust. This would constitute a "step transaction," and the deed of trust would be subject to recordation tax. Unfortunately, the clerk will not know the guaranty deed of trust is taxable unless the deed of trust discloses that the loan money is being passed through to the guarantor/grantor of the deed of trust or both the note and mirror note are presented with the deed of trust.

Question 7: When unimproved property is conveyed from a developer to a builder, what charges on the settlement sheet should be included in the "consideration payable" on which the recording taxes are computed?

Answer 7: Several years ago it was discovered that some developers and builders were engaging in a practice of disclosing only half, or some other portion less than 100%, of the consideration payable for a lot on the deed from the developer to the builder. The undisclosed portion of the consideration payable was appearing on the settlement sheet as payment for "personal property/development fees." Having caught that practice and curtailed it by requiring the settlement sheet to be submitted with the deed, the clerks have become concerned about other items appearing on the settlement sheet as a debit to the builder/buyer and a credit to the developer/seller. Many of these charges are genuinely not part of the consideration payable for the conveyance of the real property. For example, if the developer/seller is being reimbursed for the pro rata portion of prepaid annual property taxes covering the date of settlement to end of the fiscal year, that is not part of the consideration payable for the real property. On the other hand, if the developer/seller paid certain government charges for water/sewer allocations that must be paid by a certain deadline after subdivision approval as a condition of retaining the allocations and the subdivision approval, as well as avoiding a lien on the property for the unpaid charges, recovery by the developer/seller of a per/lot portion of those charges from the builder/buyer is part of the consideration payable for the real property. While there is no absolute, bright-line test, recovery by the developer/seller from the builder/buyer of fees and expenses incurred by the developer in developing the property, making it more valuable, and enabling the developer to convey marketable, unencumbered title, generally will constitute part of the consideration payable for the conveyance.

Question 8: When are transfers to and from business entities (corporations, partnerships, limited liability companies) subject to recording taxes and when not?

Answer 8: Transfers between business entities and persons who own interests in the entities are subject to transfer and recordation taxes unless the transfers qualify for a specific exemption set forth in TP §12-108 (p), (q), (v), (w), or (y). Similarly, a transfer between two entities with common ownership is subject to transfer and recordation taxes unless some specific exemption applies, such as TP §12-108(y). A donation to a non-profit, non-stock (*e.g.*, a §501(c)(3)) entity is not subject to tax because there is no consideration payable, not even the issuance of stock or increase in value of stock already issued and held by the grantor.

Question 9: When are transfers to trusts subject to recording taxes and when not?

Answer 9: A transfer to a trust is subject to transfer and recordation taxes when there is consideration payable to the grantor. Consideration payable includes the marketable investment interests (shares) received by a grantor making a contribution of real property to a business trust. This is comparable to a contribution by a stockholder to a corporation, contribution by a partner to a partnership, or contribution by a member to a limited liability company. When the grantee trust is not a business trust, and the grantor is simply gifting real property to the trust, the consideration is zero. Tax on zero is zero.

Question 10: How are the recording taxes calculated on a lease when the amount of annual rent will change based on some currently unknown figure, such as the annual percentage increase in the Consumer Price Index?

Answer 10: When the average annual rent over the total of the lease terms is not capable of being presently calculated because the annual rent will change over time on the basis of some figure, or formula, not presently knowable, the law requires the recording taxes to be based on the greater of: (1) 105% of the minimum average annual rent capitalized at 10%, plus any additional consideration payable, or (2) 150% of the assessed value of the property. If there is no minimum or "base" rent and, thus, the minimum average annual rent cannot be calculated, then the tax is based on 150% of the assessed value of the property.

Example: The lease is for a total of 24 years (3 terms of 8 years each).
The base rent per year for the first 4 years is $50,000.
The base rent per year for the next 4 years is $55,000.
The base rent per year for the next 4 years is $60,000.
The base rent per year for the next 4 years is $65,000.
The base rent per year for the next 4 years is $70,000.
The base rent per year for the last 4 years is $75,000.
The lease provides for additional annual rent equal to1% of the tenant's annual profits.
The "assessed" value of the property (40% of full value) is $400,000.
The minimum average annual rent ("maar") is $62,500.
105% of the maar capitalized at 10% equals $656,250.
150% of the assessed value is $600,000.
Tax will be based on $656,250.

Question 11: If an individual owns commercial real property in Maryland and then buys a home, does the deed qualify for the first-time Maryland home buyer reduced transfer tax rate?

Answer 11: Yes. To qualify as a first-time Maryland home buyer, the individual must not have previously owned in Maryland residential property that was used as the individual's principal place of residence and must be purchasing the residential property that is the subject of the deed for use as his or her principal residence. Thus, prior ownership by the grantee in Maryland of commercial real property or residential property that was not used as the owner's principal residence does not disqualify the deed for the special .25% transfer tax rate afforded first-time Maryland home buyer deeds.

Question 12: If there are two or more grantees on a deed and one of the grantees is neither a first-time Maryland home buyer nor a guarantor of the purchase money loan who will not reside at the premises, what transfer tax rate is applicable?

Answer 12: The full .5% rate is applicable. For the special .25% rate to apply, every grantee must qualify as a first-time Maryland home buyer or a guarantor who will not reside at the premises.

Question 13: How is recordation tax calculated on a refinance mortgage when the real property covered by the mortgage includes property in addition to the mortgagor's principal place of residence?

Answer 13: If the property encumbered by the mortgage that is being refinanced was strictly the original mortgagor's principal residence, the new mortgage on that principal residence qualifies for the refinance exemption even if additional property is included under the new mortgage. This is comparable to not losing the purchase money mortgage exemption simply because property in addition to the newly purchased property is included in the purchase money mortgage. On the other hand, if the mortgage that is being refinanced covered not only the mortgagor's principal residence but also other real property owned by the mortgagor, the new mortgage will be afforded only a partial refinance exemption from recordation tax; this is true even if the new mortgage covers only the principal residence. The amount exempt from tax is determined by multiplying the principal balance due on the former debt times the ratio of the value of the principal residence to the value of both properties. The following example is provided to illustrate this calculation.

Old mortgage covered principal home and other property.
Principal balance due on old mortgage is $200,000.
Amount secured by new mortgage is $200,000.
Value of home is $150,000.
Value of other property is $100,000.
Ratio of value of home to value of both equals 60%
Amount exempt from recordation tax on refinance is $120,000 (60% of principal balance).