WITNESS SHEET
SENATE JUDICIAL PR. CEEDINGS COMMITTEE

DATE OF HEARING: FEBRUARY 28, 2007

SENATE BILL NO.: 396

HOUSE BILL NO.:

SUBJECT: GROUND RENTS – REMEDY FOR NONPAYMENT OF GROUND RENT

SPONSORED BY: SENATOR GLADDEN, ET AL

PLEASE PRINT CLEARLY AND LIMIT YOUR SPEAKING TIME TO 3 MINUTES OR LESS

SUPPORT	SUPPORT WITH AMENDMENTS	OPPOSE	NAME AND ADDRESS	REPRESENTING	PHONE NO.
	✓		Chris DiPietro	Bank of America	443-286-6416
✓			Joseph Khome	MYSELF	410-634-1307
✓			Atty General Doug Gansler		
		✓	Amy Macht	Regional Management Inc.	410-539 2370
		✓	Kathy Howard	Regional Management Inc	410-539 2370
		✓	Lorenzo Bellamy, Esq.	Alexander & Cleaver	
		✓	R. Marc Goldberg, Esq.	Ground Rent Owners Coalition	
		✓	Prof. Byron Warnken	UB Law School	
	✓		Bill Pitcher Jim Cossaboom	Maryland Land Title Association	
	✓		CAROLYN COOK	GBBR	410 337 7200

✓ support

Joseph Bryce – Governor's Office

, PLEASE PROVIDE 20 COPIES ONE HOUR BEFORE THE HEARING TO TTEE STAFF, THANK YOU FOR YOUR COOPERATION.

support ✓	Phillip Robinson	~~410-706-0174~~
✓	~~Kathy Ridgeway~~	410-679-8288

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SENATE JUDICIAL PRC EEDINGS COMMITTEE

page 2

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SUPPORT	SUPPORT WITH AMENDMENTS	OPPOSE	NAME AND ADDRESS	REPRESENTING	PHONE NO.
✓			Kathleen Skullney	Legal Aid Bureau	410-951-7784
✓			Paul Graziano	Balto Housing	
✓			William Burgee		
	✓		Kathleen Murphy	Maryland Bankers	443-837-1613
	✓		Bob Enten	MD Bankers	443-837-1613
	✓		Tim Perry	MD Bankers	443-837-63
✓			Phillip Robinson		410-706-0174
✓			Kathy Ridgeway		410-679-8288
		✓	Charles Muskin	self	410.349.9599
		✓	Ned Corey	myself	443-804-9[illegible]

IF THERE IS WRITTEN TESTIMONY, PLEASE PROVIDE 20 COPIES ONE HOUR BEFORE THE HEARING TO THE COMMITTEE STAFF, THANK YOU FOR YOUR COOPERATION.

SENATE OF MARYLAND
JUDICIAL PROCEEDINGS COMMITTEE
VOTING RECORD

DATE 3-16-07

SB 396 HB _____

SJR _____ HJR _____

MOTION FWA BILL PASSED ✓ FAILED _____

FAVORABLE _____

FAVORABLE WITH AMENDMENT ✓ AMENDMENT

RE-REFER _____ I.D. No./SPONSOR _____

UNFAVORABLE _____ VOTE FAV

HOLD _____ ADOPTED yes

OTHER _____ Add Sen Stone
Sen. Frosh

	YEAS	NAYS
SENATOR FROSH, CHAIRMAN	✓	
SENATOR GLADDEN, VICE CHAIRMAN	✓	
SENATOR BROCHIN	✓	
SENATOR FOREHAND	✓	
SENATOR HAINES	✓	
SENATOR JACOBS	✓	
SENATOR MOONEY	✓	
SENATOR MUSE	✓	
SENATOR RASKIN	✓	
SENATOR SIMONAIRE	✓	
SENATOR STONE	✓	
TOTAL	11	—

SENATE JUDICIAL PROCEEDINGS COMMITTEE
BRIAN E. FROSH, CHAIRMAN · COMMITTEE REPORT SYSTEM
DEPARTMENT OF LEGISLATIVE SERVICES · 2007 MARYLAND GENERAL ASSEMBLY

FLOOR REPORT

SENATE BILL 396

Ground Rents - Remedy for Nonpayment of Ground Rent

SPONSORS: Senator Gladden, *et al.*

COMMITTEE RECOMMENDATION: FWA (11)

SHORT BILL SUMMARY:

As amended, this bill alters the remedy for nonpayment of a ground rent. The bill abolishes an action for ejectment as the remedy and provides for the creation of a lien.

To create the lien, the ground lease holder must first give notice to the leasehold tenant and each mortgagee or trustee of the property. Each party receiving the notice has 45 days to file a complaint in circuit court to determine whether or not the lien should be established.

If the court determines that a lien should be established, the court must enter an order finding the amount of the rent due. The court may award to the prevailing party court costs, plus reasonable expenses and attorney fees not exceeding $500 The amount of the lien is for the ground rent found to be due and any costs, expenses and attorney's fees awarded by the court.

If a complaint is not filed and the past due ground rent is not paid, the amount of the lien is for the amount claimed in the notice, plus reasonable expenses and attorneys fees not exceeding $150.

The amount of the lien shall increase by the amount of the ground rent accruing after the filing of the statement of the lien in the land records, plus simple interest. A lien imposed under the bill has priority from the date the ground lease was created. The lien may be enforced by way of a judicial foreclosure. If the property is sold at a foreclosure sale, the ground lease holder is paid out of the proceeds for the amount of the lien and the redemption amount and the purchaser takes title free and clear of the ground lease.

COMMITTEE AMENDMENTS: The committee adopted 11 amendments.

Amendment No. 1 – adds cosponsors and makes technical changes to the title of the bill

Amendment No. 2 -- revises the defined terms and makes the bill applicable to residential property

Amendment No. 3 – makes conforming changes to the bill consistent with the revised defined terms

Amendment No. 4 – provides that this new remedy does not affect the right of ground lease holder to bring a civil action against the leasehold tenant for a money judgment for past due ground rent

Amendment No. 5 -- clarifies that a ground lease holder may initiate action to obtain a lien after the ground rent is unpaid 6 months after its due date

Amendment No. 6 – requires a ground lease holder to give notice to each mortgagee or trustee of the property whose lien is on record when notice is served to the leasehold tenant, and specifies how notice shall be given to those parties

Amendment No. 7 – deletes unnecessary language regarding the docketing of a proceeding under this Act

Amendment No. 8 – alters the amount of court costs, expenses and attorney's fees that may be awarded; alters the calculation of the amount of the lien; and repeals a bond requirement for the owner of the property to release a lien

Amendment No. 9 – clarifies the time when the ground lease holder may file a statement of the lien in the land records

Amendment No. 10 – provides that a lien has priority from the date the ground lease was created

Amendment No. 11 – provides if property subject to a lien is sold at a foreclosure sale, the ground lease holder gets paid out of the proceeds the amount of the lien *and* the redemption amount

BILL SUMMARY:

If ground rent is unpaid six months after its due date, the GLH may obtain a lien in the amount of the ground rent due. The GLH must give notice to the leasehold tenant against whose property the lien is intended to be imposed and each mortgagee or trustee of record. The notice is required to include specified information and must be served on the LT by certified mail, return receipt requested or personal delivery. If the GLH cannot personally serve the LT, notice must be mailed to the LT's last known address, combined with posting the notice on the property.

A party to whom notice is given, within 45 days after service, may file a complaint (containing specified information) in circuit court to determine whether a lien should be established.

A party filing a complaint may request a hearing at which any party may appear to present evidence. If a complaint is filed, the party seeking to establish the lien has the burden of proof. Before a hearing, the party seeking to establish a lien may supplement any information contained in the required notice by means of an affidavit.

If a complaint is filed, the court is required to review any pleadings and must conduct a hearing if requested. If the court determines that a lien should be established, it must enter an order finding the amount of the ground rent due and imposing a lien. The court must enter an order denying the lien if it determines that the lien should not be established. The court may award court costs, and reasonable expenses and attorney's not exceeding $500.

The amount of the lien is for the amount of the ground rent found due by the court, along with any costs, expenses, and attorney's fees awarded. If a complaint was not filed, the amount of the lien is for the past due ground rent alleged to be due in the notice, plus reasonable expenses and attorney's fees not exceeding $150. The lien amount increases annually by the amount of the ground rent due accruing after the filing of the notice of lien in the land records plus simple interest at the legal rate accruing from the judgment's entry date.

A lien filed under the bill has priority from the date that the ground lease was created.

A lien under the bill may be enforced and foreclosed in the same manner and subject to the same requirements as the foreclosure of a mortgage or deed of trust containing neither a power of sale nor an assent to decree. A foreclosure sale may not be made if the lien is satisfied and costs of giving notice of the sale are paid before the sale.

If the property is sold at a foreclosure sale, the GLH must be paid out of the proceeds the amount of the lien and the statutory redemption amount. The purchaser takes title to the property free and clear of the ground lease. If the lienholder cannot be located, the lien may be satisfied and the ground rent redeemed in accordance with provisions governing redemption by application to the State Department of Assessments and Taxation (SDAT).

CROSS FILE:
HB 563 (Delegate Rosenberg and the Speaker (Administration), *et al.*) – ENV

LISA A. GLADDEN
41st Legislative District
Baltimore City

Majority Whip

Vice Chairman
Judicial Proceedings Committee

Vice Chairman
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Ground Rent Modernization Bills

Senate Bill 396 – Remedy for Nonpayment of Ground Rent

Senate Bill 397 – Ground Rents – Conversion of Irredeemable Ground Rents

Senate Bill 398 – Ground Rents – Notices Regarding Ground Leases

Senate Bill 622 – Ground Rents – Limitation of Actions – Registry of Ground Leases

Senate Bill 623 – Ground Rents – Redemption

Senate Bill 755 – Ground Rents – Property Owned by Baltimore City – Reimbursement for Expenses – Notices

Testimony of Senator Lisa A. Gladden
February 28, 2007
Senate Judicial Proceedings Committee

Ground Rent Modernization Bills
SB 396 397 398 622 623 755
Senator Lisa Gladden

	CURRENT LAW	PROPOSED
B buys $100,000 house subject to ground rent.	House costs 100,000 plus $98 / yr ground rent	House costs $100,000. (SB 106 no new ground rents)
B gets mortgage from local bank	Bank pays ground rent through mortgage	Bank gets notice of ground rent
GR owner sells GR to third party	B unaware,	B gets right of first refusal before ground rent is sold. (SB 623)
B wishes to purchase GR immediately	Must wait 3 years for redeemable NEVER for irredeemable	Redeemable at anytime (SB 397) Irredeemable conversion (SB 397)
B does not get notice of ground rent due	No requirement as to who/wherenotice	B must notify ground rent owner of any address changes. GR owner must notify B at least 60 days before due. (SB 398)

B gets notice that ground rent ten years in arrears plus attorneys fees	3 year maximum arrearages,	Form notice. (SB 398)
B fails to pay ground rent	Ejectment proceedings initiated, cause full loss of house	Unpaid ground becomes lien againt property (SB 396)

GROUND RENT BILL TESTIMONY of Amy Macht
February 28, 2007

I am the proud owner and manager of ground leases.

In the book "The Baltimore Row House" by Mary Ellen Hayward and Charles Belfoure published in 1999 by the Princeton Architectural Press the authors state on Page 3.

" The goal of builders to make a profit, the desire of most residents to own a home, investors looking for a return on their money, transit companies seeking to expand, and the governments growing sense of responsibility for public health all came together to create a city. In Baltimore, a special glue held it all together, the ground rent, which made homeownership possible for a much larger cross-section of people."

The current vilification of ground rents has me bewildered.

While I am perfectly happy to assist in the legislative efforts to put into effect a safety net that would prevent a homeowner from losing their home over the non payment of their ground rent due on the ground lease, I am amazed at the way ground leases are being re-characterized as an evil instrument and the way I am being treated as an evil person for holding an investment that has been of great benefit to the development of Maryland, and is the most modest and non-speculative of all real estate investments.

It seems the ground rent is being attacked because, as it is so small, it is unacceptable for it to be of any consequence. I would like to point out that the very fact that it is so small, and therefore could not pose any economic hardship to the person who is supposed to pay it, means that when there is a problem in payment, it does not stem from the inability to pay the ground rent but rather from another problem.

The problem is generally going to arise from some other failure to perform the responsibilities of property ownership, such as failure to obtain title, failure of recordation, failure to give notice of an address change of the homeowner or mortgagee, failure to pay property taxes, actual physical abandonment of the property, or the death or lack of mental capacity of the homeowner. Problems of this kind will generally respond to the intervention of a social worker or legal support to the non-compliant party, and this is how the General Assembly and court should try to address these problems.

Encouraging the non-compliance of people who do not understand their responsibilities for paying a ground rent, or a mortgage, or a tax bill, or a water bill, or an electric bill, by demonizing the entity to which they owe this responsibility will only enlarge the problem for the individual suffering under such misunderstanding and for the general organization of a functioning society where most people must be relied upon to voluntarily meet their responsibilities. The ground rent system as a whole has the lowest delinquency rate of any of the other payments required for property ownership, which is surely due to its low dollar amount, the fact that the amount never changes, and the harsh penalty if non-payment actually continues to ejectment.

In the earlier days of the 20th century the value of the ground lease financing equaled as much as 50% of the sale price of a house. By the 1950's it was more likely to be about 20% of the sale price. Remembering those percentages makes it obvious why the ground lease was a property right and why the penalty for non-payment of the ground rent would be ejectment. Now that the redemption value of the ground rent is generally less than 1% of the house value this arrangement seems strange. This is why it is easy to be confused into making the ground lease owner into the bad guy.

In fact, due to its small amount, a ground lease is more comparable to a small consumer loan. When viewed as such it can be evaluated for its true economic relationship to the homeowner. It is a small loan, usually about $1,600.00 which carries a 6% fixed interest rate without regard to the homeowner's credit rating. No principal payment is required and no prepayment penalty is charged if the consumer decides to pay off the loan. There is no interest charged on late payments, no late charges, no collection fees until payment is more than 6 months delinquent and no default judgment or acceleration payment clause. Compare this to the terms of a credit card advance. This is why ground leases are still around 35 years after the General Assembly made them redeemable, because they are a good deal for the homeowner.

If the legislature intends to alter the fundamental nature of the ground rent as a property right with the ultimate security, then it will need to alter all the other terms of this new financial instrument in order to bring it into reasonable parity with other current loan terms dictated by its new consumer loan status. If not, you will have stripped the ground lease of its value. However, if the legislature proceeds with the concept of transforming the

ground lease into a normally functioning consumer loan, it should realize that 99 % of homeowners with ground rents will not thank you for this change.

Regional Management, Inc. (RMI), the company of which I am president, manages 3,522 ground leases. In the last 20 years, RMI has filed one suit for ejectment. This suit was settled when the investor who owned the home paid the ground rent owed. There are currently 36 entities for which RMI manages ground rents including two non-profits that own 459 ground leases. I personally own 150 ground leases.

Essentially all of these ground leases come from the land development endeavors of my grandfather, Morton Macht, and the building activity of the Welsh Construction Company when it was presided over by Morton Macht, and my father, Philip Macht. That the ownership of the ground leases is now so broadly distributed is because of charitable contributions, bequests at the death of Morton Macht, and gifts.

We have done nothing unethical in creating or holding or managing these ground leases. The homeowners who bought their homes from Welsh Construction Company received a good product at a good price. The ground leases that Morton Macht retained represented the overhead and profit on the sale of the houses he built. These houses have appreciated over time from original sale prices in the 1950's in the $10,000.00 range to a range of $100,000 to $250,000 in 2007. The ground lease owners investment has not changed one dollar. The annual rent that was $90.00 in 1952 is still $90.00 today. Since 1971, a homeowner has been able to redeem any of these ground leases for a 6% capitalization rate of the annual rent. This means a $90/year ground rent can be redeemed for $1,500. In the last 30 years we have had 1250 redemptions. This means that 74% of all the homeowners who could have decided to get rid of this $90/year obligation, by paying off the ground lease owner, decided it was in their best interest to keep their property subject to a ground rent in order to hold onto the $1,500.00 that the ground lease owners advanced to the first purchaser when the house was first sold, and which was transferred to them when they bought the home.

I tell you all this to personalize who you are stripping of the value of these 3,522 ground leases. As an officer, as a trustee, as a director it is my duty to defend the value of these investments. As a granddaughter, I cannot allow you to distort and rewrite the history of ground rents in order to create a

stampede to strip them of their value. Why this has become such a crusade I do not know. I can only guess at the various motives. Perhaps for the city housing department the goal is just to save them the redemption money as they acquire property for re-development, perhaps for others it is to relieve the national mortgage market of the bother of dealing with ground rents or the liability of providing accurate title searches, and perhaps for some it is in order to sell newspapers.

I suspect that the people instigating this mob reaction are comfortable to do so, not because these ground rent investments have been so profitable for the ground lease owners, (because they have not been), but rather because the value of each individual ground lease is so small and has lost so much value over time to inflation. I suspect that these people considered ground lease owners "chumps". After all, people like me, are people who didn't know better than to disinvest in Baltimore in favor of newer less "arcane" investments. The ground rent owners are seen as weak and insignificant, and, therefore, the value of their property can be confiscated as a supposedly unintended or unfortunate by-product of fixing an "evil system ". In fact, the ground rent system is a good system which has provided good value to the homeowners but which has a very solvable problem, a problem that occurs in about one tenth of one percent of ground rents per year, a problem rate which is about 50 times lower than the mortgage and property tax system.

There are many bills proposed in the legislature this year. Not being a coordinated package, nor a response to one another, they have many provisions that are at odds with one another, without actually being alternatives to each other. While I have technical issues with each, I will confine my detailed comments to the two most objectionable bills: SB396/ HB463: SB622/HB 580.

If these bills pass they would make the ground leases RMI manages virtually worthless. How can this be and why do I say it is so?

Effects of SB 396 on RMI managed Ground Leases:

First: The proposed lien system in this bill is a sham. It takes a property right with first standing before a mortgage and puts it in line with all other liens as of the date filed. This changes the priority of the lien, putting it behind the mortgage and will eliminate the lien if the mortgage and

foreclosure costs are greater than the foreclosure sale price. A ground rent is not due until six months in arrears, and one cannot by law send a notice of delinquency until 6 month later. The ground lease owner must wait another 45 days before filing a lien. When a homeowner stops paying on a mortgage, the entity holding the mortgage can file for foreclosure within 3 months. This would be 3 months before the ground rent is even due, and 1 year and 45 days before the ground lease owner could file a lien. As mortgage companies are usually the ones paying the ground rent for the homeowner out of their escrow accounts, once the ground rent is no longer a superior lien to the mortgage, the mortgage holder will stop paying the ground rent.

Second: As written, the ground lease holder cannot file for any costs associated with collecting the delinquent ground rent, even though many of those costs are dictated by the statute and are paid to the Courts, the State, and the City. If the lien is granted by the judge, the judge can award costs of no more than $500.00 to the ground rent holder. Therefore, if the suit is settled before going to a judge there is no cost recovery at all and if it goes to court the cost recovery is limited not by reasonable costs, as are all other liens of this kind, but by a fixed dollar amount, that wouldn't change even if the court cost of filing the suit itself exceeded $500.00 at some future date.

Third: If the Judge awards the lien in the amount of the back due rent, the homeowner has the option of paying the greater of the lien, **or** the redemption value to the ground rent holder! This means that all homeowners are being told by the legislature to stop paying their ground rent for as long as they can before they plan to redeem, because the back rent they owe will be canceled if they redeem. This lien collection system insures that the minimal amount of these rents will not justify the costs of trying to collect delinquent ground rents and strips the ground rents of their value. The owners would be better off having them be normal debts in small claims court than to have the status of property rights under the system proposed which imposes all the legal burden of establishing the property right with none of the benefit.

Effects of SB 622 on RMI managed Ground rents:

First: $20.00 registration fee for 3522 GR = $70,440.00. This is now proposed as a one time initial fee, but requires additional fees for mandated updates, even for the ground rent owner to register and update information on the homeowner, clearly an impossibility. It is easy to see this fee increasing over time to an amount equal to or larger than the annual ground rent. As discussed at the Feb 22nd hearing on HB 580, the State Department of Assessment (SDAT) estimated cost for the registry was $135,000, while the $20.00 fee x 130,000 estimated properties would raise $2,600,000. Why?

Second: As required in the bill, the information required to be collected, copied and delivered to the SDAT will require RMI to dedicate an employee to this effort for the next three years.
Estimated cost = $120,000/ 3 years. Supplying SDAT with copies of all the deeds in the chain of title are really not necessary and will duplicate the land records.

Third: Additional future potential requirements for registration are left vague. The bill allows SDAT to impose other burdens and to deny registration without providing notice or reason.

Fourth: The penalty for non-registration is the elimination of the ground lease. These are property rights that are recorded in the land records. A registration's acceptance or rejection is left to the discretion of SDAT. How can a computerized database of no legal standing trump the land records?

If HB 463, and HB 580 are enacted by the legislature, it will be clear that you as a body are inciting property owners whose properties are subject to a ground rent to stop paying their ground rents.

I really don't understand this. Why would the legislature do this? The Maryland Legislature has legislated continually on matters concerning ground rents from redemption values and collection costs to notice provisions. For ground lease owners who have always followed the laws passed by the Maryland Legislature it is upsetting to suddenly hear ground rents portrayed as unfair and arcane, and to realize that the goal of this legislature is to punish them for having these investments.

I know that the come back response to my question will be, "If one person loses their house over a non payment of ground rent then that is one too many."

I could well challenge the sincerity of that statement by pointing out the hypocrisy of how avidly the city and counties promote the sale of tax certificates. A whole website for Baltimore induces speculators from all over the country to buy tax certificates and allows them to charge 24 % interest and high fees. These tax sales certificates result in the same motions for ejectment and when not redeemed result in the loss of property and equity by homeowners.

However, I do not even need to have anyone face up to the results of government tax sales, or to the impeding disaster of increased foreclosure sales imminent because of sub prime lending practices and teaser adjustable rate mortgages.

And the reason that I don't need to, is because the number of ground rent delinquency cases that go forward to a motion for ejectment is so small (about 110/year) and the amount of money owed so small (except for when the judgment includes city and state property taxes) that these extremely rare exceptions to a system which works 99.9% of the time, could be addressed by an ombudsman to the court who could intercede to find a solution to the problem when a suit proceeds to a motion for ejectment.

For instance, in the highly publicized case of the Onheisers, the central problem was that when Mary and Joseph Onheiser died in 1995 and 1996, their heirs never opened an estate, never transferred title to the property, and never paid taxes or water bills. The relatives who lived in the house also accepted notice on behalf of Joseph and Mary Onheiser, without informing the court that the Onheisers were dead. The court could stay the proceeding in a case for ejectment in order to set up a mediation, order an investigation to proceed, allow time for the appointment of a guardian or, as needed in the Onheiser case, to deal with the Orphans Court and Registry of Wills.

Certainly, I am sure, no one in this legislature would excuse the Onheisers from their obligations to follow the rules established by government for inheriting property, for accepting notice of service by the court, for titling property, for paying property taxes or water bills, (especially as the house valued at $160,000.00 was not even encumbered with a mortgage), but

perhaps having a person who could intercede and explain these duties of property ownership to citizens who find themselves in possession of property without understanding the obligations and responsibilities would be helpful. The State is not accustomed to thinking of homeowners as people so lacking in the understanding of their responsibilities as property owners, but perhaps it is time to recognize that some people become property owners without having acquired the necessary skills to fulfill their responsibilities without assistance. This type of service could be useful not only for potential ground rent ejectment situations, but for the far more common tax ejectment cases, and foreclosures. Of course, these other cases will be far harder to actually solve, because, unlike ground rent cases where the amount of money is so small that it will not actually present a hardship, tax cases and foreclosures most likely do.

There are of course, other ways to make sure that people who have not abandoned their property do not lose the property to ejectment without stripping the value of the ground lease from the ground lease owner. In cases where there is an actual owner of the property, the debt could become a personal judgment, accruing interest, reportable to a credit bureau and subject to wage attachments. If left as a property lien, it could be made to remain a priority lien in front of a mortgage or tax lien. But the legislature should remember that if they alter the security of the investment by ending ejectments they must also change the other terms of the instrument to make them collectable at reasonable and recoverable costs, or they will have preformed a regulatory taking.

If part of the goal is to increase information exchange when ground lease holders and homeowners lose track of one another, the registering of ground leases could be done in such a way as to provide some benefit to the ground lease holder in return for the cost of registration. For example, registration could be a step in requiring homeowners to redeem the ground lease when the property is transferred, and for mortgagees to include the redemption price in any financing offered. A registration system could be more gradually assembled by requiring it only upon transfer or only before bringing suit for ground rent delinquencies. (The legislature might want to consider requiring mortgagees to register on the SDAT site as well when mortgages are recorded and transferred.) Now, however, SB396 and SB622 when taken together end up requiring the payment of a fee and the registration of a property right that has been effectively taken away.

Calling a ground rent evil, calling the Onhesiers situation a suit about a $24 ground rent and $18,000 in fees, when $13,500 of the charges are for 7 years of back city taxes, does not make these things true. The legislature should be wary. The rallying cry may be to protect the few people that get caught up in the ejectment process, but the responses written into these proposed bills are out of line with that objective. The legislature should use a more deliberative process to come up with a rational solution to a very manageable problem that effects a very small number of people and not be pressured to make laws that are ill advised and perhaps unconstitutional.

Regional Management, Inc has asked that the legislature form a study group and I am aware that some people think that the call for study is just a delaying tactic that will allow ejectments to proceed. To make sure that is not true, the legislature should pass a law declaring a one year moratorium on the execution of warrants in ground rent ejectment cases so that no ejectments can happen while the legislature gets a chance to study the issue. During the year the study group should have the court appoint a liaison to present it with the cases that come before the court so that the study group gains first hand knowledge of the different circumstances that people find themselves in.

If the City, banks, mortgage originators, and title companies have reason to want Maryland to change aspects of the ground rent system they need to present their actual objectives to the study group, not hide behind their supposed concern for the person who might lose their house in a ground rent ejectment. We all know that far more homeowners lose their property to tax sales, foreclosures, and seizures for eminent domain. The City, bankers, and title companies' real issues are surely legitimate concerns and deserve your deliberation of their true interests as part of this discussion.

In the long run, if Maryland really wants to get rid of ground rents in an equitable and constitutional way, it will need to decide to require that homeowners redeem the ground rents under certain circumstances such as at the refinancing or sale of the property. This idea can also be examined by the study group.

Even in light of the current rhetoric regarding ground rents and ground rent owners, I am willing to be called upon in legislative hearings to share what I know to help solve the ejectment issue without stripping the value from the ground leases. I am trying to help the legislature avoid the mistake of a regulatory taking. However, I do need to be clear that if legislation passes

that does strip the value from the ground leases it will be my obligation to seek appropriate relief.

In addition to this testimony, I have also distributed to you for historical background a page of information on Morton Macht, and copies of some Welsh Construction Company brochures from the 50's and 60's advertising houses for sale with ground rents.

I remain, a proud owner and manager of ground leases,

Amy Macht, President
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CONSTITUTIONAL ANALYSIS OF SENATE BILL 396

prepared by

Professor Byron L. Warnken
University of Baltimore School of Law

prepared for

The Ground Rent Owners Coalition

SUMMARY OF THE ANALYSIS

S.B. 396 is an unconstitutional "taking" in violation of the Fifth Amendment Takings Clause and art. III, § 40, of the Maryland Constitution. S.B. 396 is a "taking" because it eliminates ground rent owners' reversionary interest through the total destruction of the right of re-entry. Without the right of re-entry, there is, in essence, no real property interest for the reversionary owner. This is a "taking" and not a "mere regulation."

The S.B. 396 "taking" is not a taking for a "public purpose." By eliminating the right of re-entry, the State would be "taking" for a private purpose. For each ground rent, the State would expressly take away the reversionary ownership interest from the ground rent owner, and give that real property interest to the lessee for the private benefit of the lessee.

Even if a court were to hold that the "taking" was for a "public purpose," the State would be constitutionally required to pay "just compensation." Because S.B. 396 would have the effect of (1) taking away virtually all economic value of the reversionary ownership interest for ground rents unpaid. either now or in the future; and (2) causing the fair market value of all ground rents to greatly decrease, the "just compensation" is estimated to be in excess of $150 million.

ANALYSIS

CONSTITUTIONALLY, S.B. 396 IS FATALLY FLAWED. IF ENACTED, S.B. 396 WOULD BE AN UNCONSTITUTIONAL "TAKING." IT WOULD ELIMINATE GROUND RENT OWNERS' REVERSIONARY INTEREST BY STATUTORILY DESTROYING THE RIGHT OF RE-ENTRY. THIS TAKING WOULD VIOLATE THE FIFTH AMENDMENT AND ART. III, § 40, OF THE MARYLAND CONSTITUTION BECAUSE THE "TAKING" WOULD NOT BE FOR A "PUBLIC PURPOSE," BUT WOULD BE FOR A PRIVATE PURPOSE BY TAKING THE REVERSIONRY OWNERSHIP INTEREST AWAY FROM THE GROUND RENT OWNER AND GIVING IT TO THE LESSEE FOR THE LESSEE'S PRIVATE USE. EVEN IF A COURT WERE TO HOLD THAT THE "TAKING" IS FOR A "PUBLIC PURPOSE," THE STATE WOULD BE CONSTITUTIONALLY REQUIRED TO PAY "JUST COMPENSATION."

S.B. Bill 396 proposes the following addition to Md. Real Prop. Code Ann. § 8-402.2(B): "Notwithstanding any provision of a ground rent lease giving the landlord the right to reenter, the establishment of a lien under this section is the sole remedy for nonpayment of a ground rent." Not only would S.B. 396 take away the reversionary property interest of ground rent owners, and replace it with a mere lien, it would amend the line priority, taking the ground rent owners from first in line to last in line.

The constitutional analysis is a three-question process. First, would elimination of the right of re-entry constitute a "taking" under the federal and state Constitutions, as opposed to a "mere taking"? The answer to the first question is that S.B. 396 would constitute a "taking" and would not be a "mere regulation." Second, would such a taking qualify as a taking for a "public purpose," as opposed to a taking for a private purpose? The answer to the second question is that S.B. 396 would constitute a taking for a private purpose and not for a "public purpose" because it would take the reversionary ownership interest away from the ground rent owner and give it to the lessee. Third, even if a court were to hold that the taking is for a public purpose, that taking would only be constitutional if the State paid "just compensation," which would likely exceed $150 million.

A. The essence of the reversionary ownership interest in the ground rent is the right of re-entry. In net effect, without the right of re-entry, there is no real property interest. If S.B. 396 became law and eliminated that real property interest, it would constitute a "taking," under the Fifth Amendment and art. III, § 40, of the Maryland Constitution., and not a "mere regulation."

There are about 160,000 ground rents in Baltimore City. A ground rent owner has a reversionary ownership interest in the real property, through the right of re-entry, in the event the lessee violates the lease. (There are nine procedural steps/protections, taking more than two years before the right of re-entry may be exercised.)[1] The right of re-entry is the only real

[1] The right of re-entry only becomes available after the ground rent owner has taken nine steps designed to provide the lessee with notice and with opportunity to pay the ground rent and avoid re-entry.

(1) Notify the purchaser of real property, through the contract of sale, that the property is subject to ground rent, and notify that if the ground rent is not paid timely, the ground rent owner may file suit for possession of the property.

(2) Wait for the arrearage on the lease payment to become at least six month.

(3) After the six-month arrearage period, send a certified letter, return receipt requested, to the lessee's last known address, stating that the ground rent is six months in arrears.

property interest of any value, and it is only because of that right of re-entry that the reversionary ownership interest can be enforced. Moreover, it is only because of the right to enforce the reversionary ownership interest that a ground rent owner has a property right that others in the marketplace have an interest in purchasing. If enacted, S.B. 396 would destroy the reversionary ownership interest by completely eviscerating the right of re-entry. S.B. 396 would not place a "mere regulation" on the reversionary ownership interest. Rather, S.B. 396 would completely take away that interest.

Under S.B. 396, the reversionary owner would no longer have a reversionary interest. Instead, the reversionary owner would have, at best, a dollar value lien, that may not be collectable for many years. The reversionary ownership interest will have been taken away and replaced with no property interest at all, i.e., there would merely be a lien for future money. If an individual owns a real property interest, but is denied by the Government the right to enforce that property interest, there is no property interest remaining. When the Government takes away a property right that was enforceable in a court of law, the property has lost all value, and there has been, in constitutional terms, a "taking."

The following analogy is instructive. Assume that an investor purchases an apartment building and rents the apartments. Subsequently, the Maryland General Assembly enacts a law that provides that, even if a lessee fails to satisfy the terms of the lease, the property owner may not re-enter the property against the lessee – ever. Instead, if the lessee fails to satisfy the terms of the lease, the property owner may obtain a judgment against the lessee, which may be collectable at some unknown date in the future. In the interim, if the lessee elects to remain on

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(4) Also after the six-month arrearage period, send a first class letter to the title agent or attorney listed on the deed or the intake sheet recorded with the deed.

(5) After another 45-day waiting period, bring an action for possession of the property, which must be personally served on the lessee or, if no lessee is in actual possession of the property, posted on the property.

(6) Prior to entry of a judgment, provide written notice of the pending entry of judgment to each mortgagee of the property.

(7) Record the notice of judgment, indexed under the name of the mortgagor, with all identifying information related to mortgagees, mortgagors, and ground rent lease.

(8) Send a certified letter, return receipt requested, to the mortgagee, at the address stated in the recorded request for notice of judgment.

(9) Wait an additional six month after the execution of the judgment for possession for the ground rent and awarded costs to be paid by the lessee or any other person.

the property for many years, the property owner would merely have the right to collect, but not the right of re-entry. Clearly, that would be a "taking."

The most recent "takings" case in the Court of Appeals of Maryland was decided three months ago. In Neifert v. Department of Environment, 395 Md. 486 (2006), the Court re-stated the standard for determining whether there is a taking, as follows:

> [The] Takings Clause of the Fifth Amendment to the United States Constitution does not prohibit regulation of property, but if a regulation goes too far, it will be recognized as a taking. Whether a particular regulation constitutes a taking depends on the particular circumstances of each case. It has been recognized that most regulatory takings cases should be resolved by balancing the public and private interests at stake, considering three primary factors: (1) the economic impact of the regulation on the claimant, (2) the extent to which the regulation has interfered with distinct investment-backed expectations, and (3) the character of the government action.

Id. at 517.

Applying Neifert to the impact of S.B. 396, if enacted, demonstrates that S.B. 396 is a "taking" within the meaning of the federal and state Constitutions. As the Court of Appeals stated, S.B.396 "goes too far." As for the first factor, S.B. 396 would have a devastating impact on the reversionary ownership interest by (1) taking away virtually all economic value of the reversionary ownership interest for those ground rents unpaid either now or in the future, and (2) causing the fair market value of all ground rents to greatly decrease significantly.

As for the second factor, S.B. 396 would completely defeat the "distinct investment-backed expectations." No investor would purchase ground rents if the investor knew that, in the event that the ground rent went unpaid, the only remedy existing -- that of re-entry -- was gone.

In Stevens v. City of Salisbury, 240 Md. 556 (1965), there was a dangerous public intersection. The Government required property owners to remove masonry corner posts and reduce the height of shrubbery and picket fences. Id. at 572. The Court of Appeals held that this governmental action was "unreasonable, confiscatory in nature, and if enforced, would amount to a taking of private property." Id. at 568. The Court held that the restrictions were substantial, were a severe interference with the property right, and were tantamount to a deprivation of the property interest. Id. If the Government's conduct in Stevens was a taking, certainly the complete destruction of the right of re-entry, as the only property right of the reversionary owner's interest, is a taking.

In Maryland-National Capital Park & Planning Commission v. Chadwick, 286 Md. 1

(1979), the governmental placed privately owned land in a public "reservation" for a term of up to three years. The Court of Appeals affirmed that this was an unconstitutional taking because the "reservation" effectively denied the owners of their right to use the land. If placing a "reservation" on property for up to three years is a taking, so is the complete annihilation of the right of re-entry, as it is the only means of enforcing an owner's reversionary ownership interest. In Howard County v. JJM, Inc., 301 Md. 256 (1984), the Court of Appeals held that a statute that required developers to reserve a right-of-way in a subdivision for a new state highway that was part of the State's long term highway plan was also a taking.

In Leet v. Montgomery County, 264 Md. 606 (1972), the Court of Appeals addressed a trash-removal ordinance that required property owners to remove vehicles abandoned on their property. The Court held that, even though there was no physical invasion by the Government, the ordinance constituted a taking because there was a negative economic impact on the property owner. Id. at 615. Likewise, under S.B. 396, there would be no physical invasion of the property, but the economic taking would be even more unconstitutional than the taking in Leet.

As for the third factor, the character of the government action shows that S.B. 396 constitutes a taking. Although the Government has broad power to regulate, there is no legitimate argument that S.B. 396, if enacted, would be a "mere regulation." It is a taking under Supreme Court and Maryland cases that have interpreted the Fifth Amendment Takings Clause and art. III, § 40, of the Maryland Constitution. Because the property interest is eviscerated, and not regulated, it is a taking.

In Congressional School v. Roads Commission, 218 Md. 236 (1958), the Court of Appeals, addressing the use of zoning as a "back door" for the Government to take without paying "just compensation," stated:

> There seems to be general agreement among the authorities which have considered the question that zoning cannot be used as a substitute for eminent domain proceedings so as to defeat the constitutional requirement for the payment of just compensation in the case of a taking of private property for public use by depressing values and so reducing the amount of damages to be paid.

Id. at 241.

There is no valid argument that S.B. 396 would be a "mere regulation" and not a "taking." The Supreme Court has recognized that legislatures are afforded more flexibility with pervasively regulated industries. Donovan v. Dewey, 452 U.S. 594 (1980). In such a scenario,

the parties are likely to enter into a relationship with knowledge that they are subject to regulation. Ground rents have never been subject to the extreme invasion proposed by S.B. 396.

An instructive case is Ross v. City of Berkeley, 655 F. Supp. 820 (N.D. Cal. 1987), in which the Court found unconstitutional an ordinance that imposed city-wide commercial rent control. Although the Court resolved the case under the Contract Clause, it also held that the ordinance constituted a taking under the Fifth Amendment Takings Clause. It was not a mere regulation. The Court noted that the legal status was "upset in a severe and substantial manner" because the tenancy could be come endless and it would "effectively bar the [owners] from occupying the premises for the remainder of their lives." Id. at 829.

The Court indicated that it would have been one thing if the leasehold was entered with the parties aware that the properties were "sufficiently regulated," but they were not. In that case, as with S.B. 396, the regulation came along well after the fact. The Court stated that "[t]he ordinance's severe, retroactive, and permanent nullification of [the] right to recover possession of their premises thereafter must be measured against 'the public purpose justifying its adoption' to determine the reasonableness of the legislation." Id. at 826. The Court quoted Loreto v. Teleprompter Manhattan CATV Corp., 458 U.S. 419 (1982), in which the Supreme Court stated: "[W]e cannot indulge the notion that a city may eviscerate a property owner's rights and shield its action from constitutional scrutiny by calling it [a mere regulation]." 655 F. Supp. at 838.

Ground rent owners are deemed to know that, under the law of adverse possession, it takes 20 years to extinguish a real property interest. However, all of a sudden, under S.B. 396, the State would take the reversionary ownership interest, by automatically and permanently extinguishing it, if the ground rent registration, and the $20 fee, are more than six months late (three years for existing ground rents). That is a "taking" and not a "mere regulation."

As such, the constitutional analysis is triggered. Once the constitutional analysis is triggered, the next issue is whether that taking would qualify as a taking for a "public purpose" or whether it would be an unconstitutional taking for a private purpose. Moreover, even if a court were to hold that the taking was for a public purpose, to be constitutional, that taking would require the State to pay "just compensation."

B. The "taking" of the reversionary ownership interest violates the Fifth Amendment Takings Clause and art. III, § 40, of the Maryland Constitution because the "taking" would be for a private purpose and not for a "public purpose." Through S.B. 396. for each ground rent,

the State would directly take away the reversionary ownership interest from the ground rent owner, and give that real property interest to the lessee for the lessee's private use by eliminating the right of re-entry.

Courts extend deference to state and local legislatures regarding what qualifies as a "public purpose" taking. The most recent Supreme Court case is Kelo v. City of New London, 545 U.S. 469 (2005), in which the Court held that the taking of private property for development to increase the tax base and revitalize an economically distressed city was a public purpose because the development would increase business, jobs, and the tax base. The Court said that it must look to the purpose of the taking to determine whether it is a public use.

The taking that would be effectuated by S.B. 396 would be a private taking because it would not be for a "public purpose." Through S.B. 396, for each ground rent, the State would directly take away the reversionary ownership interest from the ground rent owner and give that real property interest to the lessee for the lessee's private use. The fact that the Maryland General Assembly would simultaneously "take" 160,000 times does not make each taking any less of a taking and does not make each taking any less of a private taking.

In Van Witsen v. Gutman, 79 Md. 405 (1894), Baltimore City condemned part of a public alley in order to sell it to a private landowner whose property adjoined the alley. As a consequence, other landowners lost easements. Id. at 407-08. The Court of Appeals held that this taking was to promote a private interest and not for a public interest. Id. at 411-12. In so doing, the City unconstitutionally took the property right of some individuals – their easements – and give that property right to another individual for that individual's private use. Id.

In Perellis v. Mayor & City Council of Baltimore, 190 Md. 86 (1948), the Epsteins were the owners of property adjacent to an alley. They entered into a contract with the City to obtain a piece of property in the middle of the alley. Id. at 89. In exchange, the Epsteins would give the City a piece of property with which to construct a new alley, and the Epsteins would pay the associated costs. Id. Other property owners adjacent to the alley claimed that closing the alley would substantially impair their access and thereby devalue their properties. Id. at 90. The Court of Appeals held that the City's plan to close the alley was invalid because it was not for a public purpose. Id. at 95. Instead, the taking was "solely for the private use and advantage of the Epsteins." Id.

Like in Van Witsen and Perellis, S.B. 396 is a private use bill, unconstitutionally taking from the reversionary ownership interest and giving it to a private person for that person's personal use. Regardless of how it is characterized, S.B. 396 constitutes a taking for private – not public – purposes, and it is, therefore, unconstitutional.

C. **If a Court were to hold that the "taking" of the reversionary ownership interest is a taking for a "public purpose," the State would be constitutionally required to pay "just compensation" to the owners of the reversionary interest. Because S.B. 396 would have the effect of (1) taking away virtually all economic value of the reversionary ownership interest for ground rents unpaid, either now or in the future; and (2) causing the fair market value of all ground rents to greatly decrease, the State would be constitutionally required to pay "just compensation" estimated to be in excess of $150 million.**

The arithmetic is staggering. If there is a taking, and if that taking is for a public purpose, the taking is constitutional only if the State pays "just compensation." S.B. 396 would create two "just compensation" scenarios. First, S.B. 396 would eliminate virtually all economic value in the reversionary ownership interest for ground rents unpaid, either now or in the future. Second, S.B. 396 would cause the fair market value of all ground rents to significantly decrease. It is estimated that S.B. 396, even if constitutional as a "public taking," would constitutionally require the State to pay "just compensation" estimated to be in excess of $150 million.

If S.B. 396 is enacted, it would take away the reversionary ownership interest of the right of re-entry. With the State taking away the right of re-entry from the reversionary owner, there would probably be a great escalation in unpaid ground rents in Baltimore City. For all unpaid ground rents, the value of the reversionary ownership interest in those properties would be completely gone.

Ground rents are readily bought and sold as investment properties. If S.B.396 is enacted, it may be that no one would be interested in purchasing ground rents, and they would lose all fair market value. Under S.B. 396, if the ground rent were to go unpaid for many years, there would be no right of re-entry, and the newly created lien, invented as a substitute, may be of no value for many years. As such, the ground rent may have no value for many years. However, assume that willing buyers and willing sellers would still be willing to buy and sell ground rents, but at only one-half of what they are buying and selling for now. If so, the total value of the taking would be in excess of $150 million.

In Mayor & City Council of Baltimore v. United Five & Ten Cent Stores, 250 Md. 361, 369-70 (1968), the Court of Appeals held that "fair market value" means the value prior to the taking, compared with the value as a consequence of the taking. The Court emphasized that "just compensation" must account for all diminution in value in any way occasioned by the taking and even by the announcement of the taking. The last three months have produced a perception of an impending governmental "taking." This has already influenced the "just compensation" that the State would be required to pay if S.B. 396 is enacted. In Brinsfield v. Mayor & City Council of Baltimore, 236 Md. 66 (1964), the Court of Appeals held that rent on a property being condemned is part of the "just compensation" calculation.

In the context of a ground rent "taking," in Mayor & City Council of Baltimore v. Latrobe, 101 Md. 621 (1905), the Court of Appeals stated:

> We cannot close our eyes to the fact . . . that ground rents, especially in Baltimore City, are constantly being sold and have market values (resembling somewhat those of bonds and stocks), depending upon the manner in which they are secured and the length of time they are to continue. As under our system, the taxes are paid by the owner of the leasehold interest, when well secured they are in demand and frequently realize prices far beyond what they could have been capitalized at when the leases were originally made. 'The reversionary ownership interest, when his interest is condemned, is undoubtedly entitled to what his interest is worth in the market and prima facie the leasehold is charged with that value.

Id. at 629.

In Heritage Realty v. Mayor & City Council of Baltimore, 252 Md. 1 (1969), the Court of Appeals stated: "If the owner of the reversion determines to dispose of it, he can seek a buyer in the market place, and the value of the reversion will be the price at which a buyer, willing but not obligated to buy, is ready to pay, and a seller, willing but not obligated to sell, is prepared to accept." The courts are capable of determining the "just compensation" for the reversionary ownership interest, and it will likely be in excess of $150 million.

CONCLUSION

For the foregoing reasons, it is respectfully suggested that S.B. 396 is unconstitutional and should not be enacted.

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