SUTHERLAND

LEGAL ALERT

July 1, 2013

Changes to the Recordation Tax in Maryland for Refinancing Commercial Mortgage Loans: Recordation Tax Imposed Only on New Money

Maryland Governor Martin O'Malley signed into law an act providing relief to commercial borrowers that wish to refinance or modify loans originally secured by indemnity deeds of trust. This new law, effective July 1, 2013, revises a 2012 statute that required borrowers to pay the recordation tax on the entire balance of their new loans when refinancing an existing indemnity deed of trust.

The indemnity deed of trust structure was long used in Maryland to defer Maryland recordation taxes, which would otherwise be due if a borrower entered into a financing arrangement secured by a conventional deed of trust. As of July 1, 2012, however, this structure was no longer available to provide tax relief for loans greater than $1 million. The 2012 law thus closed a long-standing loophole which permitted borrowers that used the indemnity deed of trust structure to avoid the payment of hefty recordation taxes.

Governor O'Malley, however, has provided relief to the drastic changes made to the recordation tax laws in 2012. Pursuant to the new 2013 law, <u>any</u> borrower that refinances a loan, whether secured by an indemnity deed of trust or otherwise, with its existing lender or a new lender, will be taxed only on the difference between the outstanding principal balance of the existing loan and the outstanding principal balance of the new loan, i.e., the borrower will pay the tax only on the "new money." This new law eliminates the practice of an existing lender assigning its loan and security interest (which assignment was not taxed) to a new lender, which then had to amend and restate the existing deed of trust in order to take advantage of tax savings based on the amount of taxes previously paid or exempted. The new law further clarifies that a "supplemental instrument," which is not taxed, includes any instrument that amends or modifies an existing security instrument, including a previously recorded indemnity deed of trust, and that the tax is imposed only on the new consideration evidenced by such supplemental instrument.

In addition to the advantage given to commercial borrowers refinancing or modifying their existing loans, the new law also permits borrowers to escape the recordation tax by using an indemnity deed of trust structure on a loan that now does not exceed $3 million. All of these changes provide tax advantages to commercial borrowers and will streamline the documentation of new and refinanced loans resulting in lower transaction costs.

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