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The Changing Nature of IDOT Recordation Tax Collection in Maryland

The Indemnity Deed of Trust (IDOT) structure has long been used in Maryland to defer Maryland recordation taxes, which would otherwise be due had a Borrower entered into a financing arrangement secured by a conventional deed of trust. As of July 1, 2012, however, this structure is no longer available to provide tax relief for loans greater than \$1 million.

An IDOT is structured so that it secures contingency guaranty obligation rather than a direct debt obligation. There are two obligor parties to a loan structured as an IDOT: the Debtor (e.g., Borrower), who is directly liable under the promissory note, and the Grantor, who will become liable for payment of the loan upon a default by Debtor pursuant to a payment guaranty. The Grantor owns the collateral for the loan and grants that collateral to a lender as security under an IDOT to secure repayment of a payment guaranty, which in turn guarantees payment of a promissory note made by the Debtor. Therefore, the IDOT actually secures the Grantor's obligations under the guaranty rather than the Borrower's liability under the promissory note. The basis for the deferral of the recordation tax in the past has been Maryland Code, Tax-Property Article, § 12-105(f)(1), which stated that the recordation tax applies only to the principal amount of the debt incurred at the time of recording. The obligation to pay recordation tax had been triggered only when this contingent liability became a direct liability of the Grantor (such an event is typically triggered by a default under the guaranty or the underlying loan documents).

As of July 1, 2012, Md. Code Ann. Tax-Prop. § 12-105(f) was amended to eliminate the tax advantage of using an IDOT arrangement. Specifically, the amendment imposes a tax on all security instruments that secure a guaranty obligation for which the Grantor is not primarily liable to the same extent that a tax would be due if the deed of trust were given by the primary obligor. However, the tax is not applicable to IDOTs to the extent that an IDOT secures a guaranty of a loan for less than \$1 million. After July 1, 2012, the recordation tax now applies to an IDOT securing loans greater than \$1 million as if the guarantor were primarily liable for the loan. The impact of the amendment on existing, recorded IDOTs is not clear. The stated intention of the amendment is for the new rule to impact only "instruments of writing" recorded after the effective date of the statute. However, the amendment does not address whether the recordation tax will apply to post-July 1, 2012, modifications, assumptions or assignments of existing IDOTs (i.e., those recorded prior to July 1, 2012). We will keep you posted as further clarification is received from recording agents.

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If you have any questions about this Legal Alert, please feel free to contact any of the attorneys listed below or the Sutherland attorney with whom you regularly work.

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