Real Estate - Use of IDOTS

By

In Maryland for the refinance of commercial properties, the use of an IDOT (Indemnity Deed of Trust) may save thousand of dollars in recording taxes - in this case we saved about $369,000.

Consider these facts. In April, 2009, the lender issued to Owner LLC a loan commitment for a loan of $45,000,000 for the refinance of the Owner's office building complex in Maryland. The loan was to be secured by a deed of trust against the Owner's office building complex. Had the loan not been re-structured, the state recordation tax (sometimes known as "state stamps") would be $369,000. To avoid this tax, the loan was re-structured. The re-structure worked and the tax was avoided. How did we do it? Here's how.

We formed a new limited liability company called Borrower, LLC. Its sole member is Owner LLC, which owns the real estate. The bank made the loan to Borrower LLC, a shell entity with no assets. However, Borrower LLC is owned 100% by Owner LLC. Owner signed an unconditional guaranty of the note. To secure its guaranty, Owner signed an "Indemnity" Deed of Trust in favor of the bank. Thus, the loan is made to a borrower which is owned 100% by Owner, meaning that the Owner has the use of the funds through its wholly owned subsidiary. The bank is protected because it got the collateral it bargained for - a first priority lien on the guarantor's office building complex.

Like many counties in Maryland, the county where the real estate is located does not collect recordation taxes on "indemnity" deeds of trust so long as the grantor of the property is not "primarily liable" for payment of the debt. Because the Owner, as guarantor of the note, is not "primarily liable" for the debt and since the Owner pledged its real estate as collateral for its guaranty rather than as collateral for the note, the "indemnity" deed of trust was exempt from the state recordation tax. This relatively simple re-structure saved the client $369,000 in recordation taxes, which would have been collected had the transaction proceeded along traditional grounds, i.e. a promissory note from the borrower secured by a deed of trust on the borrower's real estate.

Warning. Not all counties in Maryland exempt IDOTS. If you are handling a similar transaction, you need to check with the subject county to be sure it will apply the exemption for an IDOT. If not, there is no reason for the re-structure.

Fraudulent Conveyance Issue. Some have asked whether the transfer of the property to secure a guarantee of a loan made to another entity can be set aside in Maryland as a fraudulent conveyance. We think the transfer cannot set aside as a fraudulent conveyance. Case law is fairly clear that when you have a "downstream" guarantee, i.e. the parent is guaranteeing the debt of its wholly owned subsidiary, there is clear benefit flowing to the parent company so that the transfer is not a fraud on the parent's creditors.

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