October 14, 2010

Alfred M. Pollard
General Counsel
Federal Housing Finance Agency
1700 G Street, N.W.
Washington, D.C. 20552

Re: **Docket No. FR-2010-N-11**
Guidance on Private Transfer Fee Covenants

Dear Mr. Pollard:

The Mortgage Bankers Association (MBA)[1] appreciates the opportunity to comment on the Federal Housing Finance Agency's (FHFA) proposed guidance on private transfer fee covenants (PTFs). Upon final completion of the guidance, FHFA will make significant programmatic changes that will affect potential future homeowners.

FHFA is proposing to issue guidance to the Federal National Mortgage Association (Fannie Mae), the Federal Home Loan Mortgage Corporation (Freddie Mac) (collectively, the Enterprises), and the Federal Home Loan Banks (the Banks) that the entities it regulates should not deal in mortgages on properties encumbered by private transfer fee covenants. The proposed guidance would extend to mortgages and securities held by the Banks as investments or as collateral for advances and to mortgages and securities held or guaranteed by the Enterprises. FHFA is proposing this new policy because it believes PTFs are in opposition to the federal charters of the Enterprises, whose public mission is to "provide stability in the secondary market for residential mortgages." There are various types of PTFs. Some PTFs are used to provide an income stream for private developers or third party investors, whereas other PTFs are used to fund home owner associations (HOAs). Importantly, FHFA does not make a distinction among these various types of private transfer fees.

[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,200 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

MBA's Position

MBA opposes the practice of private third parties, such as developers, builders, licensing companies and real estate brokers, imposing private transfer fee covenants on residential real estate for the purpose of extracting future income. MBA is concerned that encumbering housing transactions with these types of PTFs will impede the marketability and affect the valuation of properties and thus the value of the loans and securities backed by such loans. Moreover, MBA is concerned that such practices are often not disclosed to homeowners because developers or builders often pay the first fee, exempt the sale to the original homeowner, or the fee is hidden.

MBA, however, believes that distinctions among PTFs are necessary. MBA does not oppose private transfer fee covenants that are typical and customary, nominal in amount, limited in duration, and provide a direct or indirect benefit to the homeowner, such as fees to homeowners' associations (HOA) or fees to conserve open spaces or parks within the homeowner's development. Likewise, MBA does not oppose fees or covenants that run with the land, are limited to a particular transfer and are in exchange for a specific benefit afforded the homeowner, such as an equity distribution under a shared appreciation loan. Additionally, MBA does not oppose transfer fees required by government entities and fees that do not run with the real estate such as cooperative and HOA transfer fees.

Disclosures must be unambiguous and not concealed to homebuyers and other parties involved in the transaction. We are aware that in some Declarations of Covenant the fee does not become assessable until two years after the covenant is executed. Thus, if the Covenant is filed in the land records close to settlement, the fee may not be known to the original buyer. Any subsequent buyer will uncover the fee through a title search even if not assessed due to the two-year amnesty period. For allowable PTFs, MBA supports requiring a clear disclosure to homebuyers by the settlement agent prior to settlement detailing the terms of the PTF, its amount, duration and triggers.

MBA supports a prospective application of any prohibition on PTFs to avoid impacting the marketability of the estimated four million properties currently subject to such covenants. Existing homebuyers with PTFs or communities that rely on the income stream from PTFs should not be harmed financially for any change in policy.

Background

A PTF covenant is a transfer fee payable to a private third party upon each sale of the property between a buyer and a seller. The PTF of particular concern to the FHFA often involve the developer, or trustee, which establishes the PTF covenant by either recording a covenant in the local public record, or including the covenant in the deed for each home in a planned subdivision. These PTFs are usually in effect for 99 years, are a percentage of the final sale price (typically one percent), and do not offer a direct or indirect benefit to property sellers or buyers after the original transaction. The original sale from the developer/builder to the first purchaser may involve a discount on the purchase price.

An emerging scheme of particular concern to our members is licensing companies marketing PTF covenants as investment vehicles. The company intends to "bundle" PTF covenants so that they can be securitized and resold on the open market in order for developers to more quickly monetize these streams of revenue. Although bundled PTF covenants have not been securitized yet, MBA strongly opposes the creation of these types of financial transactions. PTFs that are expensive and primarily benefit investors or private developers unnecessarily increase the cost of homeownership by stealing equity from homeowners and distorting home values.

Exemptions for Certain Private Transfer Fee Covenants

MBA shares FHFA's concerns about private transfer fees impact on homeowners and property values, but MBA believes that too broad a prohibition may have unintended consequences. Some private transfer fees serve homeowners with a legitimate purpose and help maintain property values. A widespread prohibition on private transfer fees could have unintended consequences, some of which can be determined today, but others will not be realized until the implementation of the policy. A hasty decision could cause irreparable harm to existing and future homeowners, particularly in cooperatives, condominiums, new developments and bankrupt developments.

For example, in cases where PTF covenants are used to help fund HOA activities, the PTF covenants are a source of revenue to help the associations provide services to the homeowners they represent. The PTF covenant is paid by the buyer at closing, and then used by the homeowners' association for the maintenance, administrative costs, or capital improvements. The key point of these fees is that they help provide direct or indirect benefits to the homeowner in the form of higher property values from community improvements, lower association dues, and generally more desirable communities. MBA stresses that the association supports these PTF covenants when they are nominal in cost and benefit the homeowner's immediate community, not the general geographic area.

Another example is the impact on cooperatives. In many cases, cooperatives are forms of affordable homeownership and are particularly prevalent in New York City. PTFs, also called a "flip tax" or "waiver of option fee" in New York, is one of the ways that many cooperatives and condominiums preserve their affordability, with the proceeds of the fee being paid directly to the cooperative or condominium to fund a building reserve fund. Lending institutions consider the strength of cooperatives and condominium reserve funds when they are evaluating the financial strength of a building. An unintended consequence of the FHFA proposal could be to greatly reduce the reserve funds income stream of many cooperatives and condominiums.

While MBA opposes private transfer fees that are used to benefit developers and other investors, we were made aware that PTFs are being used as a means to facilitate the completion of developments where builders and developers went bankrupt. We imagine that these developments are fraught with legal challenges including mechanics liens, liens by commercial lenders and others, code violations and fines, incomplete infrastructure, etc. The cost of finishing the infrastructure and property (such as paying liens and removing clouds on title) may exceed the fair market value of the properties to be sold. The use of PTF may be a means to encourage developers to take over partially completed developments. MBA does not have sufficient information to comment on this situation, but wishes to raise it for FHFA's further consideration and research.

Prospective Application of FHFA Policy

MBA is concerned with a retroactive prohibition on PTFs, which if imposed, would make large numbers of properties unmarketable, would depress property values, and could harm communities. The current housing market is too fragile to make an entire group of homes essentially ineligible for conventional financing, especially when the current homeowners negotiated their mortgages under accepted property terms without reason to believe that they were purchasing their homes with unsellable traits. The process to "unwind" these covenants may be unnecessarily burdensome to existing homeowners and it is unclear who would bear the financial costs of such actions.

Disclosures

If FHFA adopts MBA's position and excludes existing properties with PTFs and certain PTFs going forward, disclosures are important to ensuring consumer protection. MBA recognizes there may be situations today where private transfer fee covenants are not disclosed to homebuyers (because the covenant does not apply to the builder/developer or the covenant exempts payment for the first several years) or are written cryptically or hidden among other documents the homebuyer receives. MBA fully supports clear, transparent disclosure of private transfer fees in order to protect homebuyers and to prevent lien issues for lenders and mortgage investors. Disclosures should include, but not be limited to, understandable statements regarding the fee and associated costs, its purpose, an expiration date of the covenant, and the entity to be paid. Disclosures and sale contract conditions may help ease FHFA's public policy concerns regarding private transfer fees.

Before lenders close on loans, they require a title search to be performed to confirm that there are no unknown liens against the property or other clouds on title. A consumer's failure to pay a PTF covenant constitutes a lien against the property that would be superior to the mortgage.

Moreover, there is concern that the presence of a PTF covenant may cause the title company or lender to require a subordination agreement from the Declarant when a mortgage is refinanced or the borrower obtains a junior mortgage. While a sample Declaration of Covenant obtained by MBA appears to exempt from the PTF, the securing of debt without a transfer of the property, [2,3,4] other covenants and parties may require such subordination or require subordinations out of an abundance of caution.

[2] A sample "Declaration of Covenant" exempts numerous transfers from the fee. Specifically Covenant 1(f) entitled "Definitions" states. "Conveyance shall not include a conveyance pursuant to devise, bequest or inheritance; the

Finally, MBA is concerned that PTFs could increase lenders' liability under RESPA. HUD is reviewing this issue and we understand no final determination has been made regarding how, or whether, PTFs must be disclosed on the Good Faith Estimate, and whether PTFs are subject to tolerances. If these fees were subject to tolerances, lenders could be liable for amounts that final PTFs exceed GFE estimated PTFs, in excess of the tolerances. Such a result would be inappropriate considering that a title search is needed to ascertain a PTF and title searches are done close to closing due to their cost and nexus to the closing.

The property seller and title agent are in the best position to provide homebuyers with appropriate disclosures regarding PTFs because they are in positions of knowledge. In addition, sales contracts should be conditioned on the buyer's receipt of the disclosure of the PTF, meaning the buyer would be allowed to cancel the sales contract, without forfeiture of the good faith deposit, if a PTF covenant is identified.

Legislation

Notably, because of the growing concern of private transfer fees, their affect on home values, and a growing concern for consumer protection in this arena, the federal government and states have begun introducing and enacting laws aimed at regulating

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creation, modification, extension, spreading, severance, consolidation, assignment, transfer, release or satisfaction of a mortgage; a mortgage subordination agreement, a mortgage severance agreement, an instrument given to perfect or correct a recorded mortgage or deed of trust; or a release of lien of tax.

[3] Id. Covenant 6 states: "EXEMPTIONS. The Reconveyance Fee shall not be assessed or payable in connection with a Conveyance (a) by the Declarant; (b) made by the Owner [i.e., homeowner] in connection with a mortgage or deed of trust where the Conveyance is for the sole purpose of securing the indebtedness of the Owner; (c) resulting from death or legal disability of an Owner, including transfers by will or probate; (d) by or to a Lender or Lender's designated trustee when the Conveyance is by or to a Lender in connection with a mortgage made, held or serviced by a Lender. *(The foregoing 6(d) shall be broadly construed, and shall include dispositions made by a Lender postforeclosure, including dispositions made as a result of acquisition of title by a Lender arising out of a deed in lieu of foreclosure)*; (e) by or to a governmental entity or agency (whether local, state, federal or otherwise) or 501(c)(3) entity; (f) made by a Grantor with a Controlling Interest in the Grantee, where the Grantee owns a Controlling Interest in the Grantor, or where a Person owns a Controlling Interest in both the Grantor and Grantee (an "Affiliate Transaction"); (g) made by order of a court (whether in connection with bankruptcy, divorce or otherwise, but excluding an order for specific performance); (h) where the Trustee cannot be identified by reference to this Instrument or the [Office of Public Records] OPR; or (i) occurring prior to 01/01/2012. Exemptions pursuant to section 6(c), 6(d), 6(f) or 6(h) shall be supported by Grantor's written affidavit under oath that the foregoing exemption(s) apply, which shall be filed in the OPR in connection with the Conveyance." Bracketed item added for clarity.

[4] Id. Covenant 9 states: "LIEN AND PRIORITY; LIABILITY; COLLECTION. To the extent permitted by law, a Reconveyance Fee that is not paid when due ("Unpaid Reconveyance Fee") shall thereupon become a continuing lien and charge ("Lien") upon the portion of the Property that was the subject of the Conveyance giving rise to the Unpaid Reconveyance Fee ("Lien Property"), which Lien shall thereafter be binding upon such Lien Property, and:
a. the Lien is effective from the date the Unpaid Reconveyance Fee became due.
b. the Lien shall secure the Unpaid Reconveyance Fee as well as interest and all reasonable costs and attorney's fees incurred incident to the collection process.
c. the Lien shall be subordinate to a Lender's first mortgage lien or first deed of trust secured by the Property (a "First Mortgage"). The foregoing subordination shall not apply to Unpaid Reconveyance Fees (i) arising from the Conveyance that gave rise to the First Mortgage or (ii) described in a Notice of Lien filed at least 21 days prior to the date of recordation of the First Mortgage."

PTFs. Representatives Maxine Waters and Albio Sires introduced H.R. 6260, the "Home Equity Protection Act of 2010," on September 29, 2010. The bill seeks to amend the Real Estate Settlement Procedures Act (RESPA) by prohibiting the collection of private transfer fees on all federally related mortgage loans. The Act would protect covenants and payments made to lenders holding a lien on a property; licensed real estate brokers; local governments pursuant to laws, regulations, and ordinances; homeowner associations; and charitable organizations. MBA is currently evaluating this bill.

This legislation is the latest in a series of government actions to limit these fees. To date, 18 state legislatures in Arizona, California, Delaware, Florida, Hawaii, Illinois, Iowa, Kansas, Louisiana, Maryland, Minnesota, Mississippi, Missouri, North Carolina, Ohio, Oregon, Texas and Utah have passed legislation that restricts their use. It is important to note, however that while many of the states have legislation that explicitly prohibits private developer or third party fees, these same laws often have detailed lists of exemptions. For example, Hawaii's H.B. 2288 excludes fees payable to a government entity, fees paid to cooperative housing corporations, or any fee payable to a lender for consenting to an assumption of a loan. The inclusion of these exemptions illustrate that at least some states recognize the complexity of the private transfer tax issue and the potential for unintended consequences that could arise if too strict of a policy is enacted.

Conclusion

MBA does not support PTFs that are used as long-term income streams for private developers and third party investors. However, PTFs that benefit homeowners and encourage the stability of neighborhoods should not be prohibited. All PTFs must be disclosed early in the home buying process and with transparency to all parties. If you have any questions, please contact Tamara King at TKing@mortgagebankers.org or (202) 557-2758, or Vicki Vidal at VVidal@mortgagebankers.org or (202) 557-2861.

Most sincerely,

John A. Courson

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Mortgage Bankers Association