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THE FLORIDA BAR

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VIA E-MAIL: regcomments@fhfa.gov

April 8, 2011

Alfred M. Pollard, General Counsel
Federal Housing Finance Agency
Fourth Floor, 1700 G Street NW
Washington, DC 20552

Re: Proposed Part 1228 Rule on Private Transfer Fee Covenants (RIN 2590-AA41)

Dear Mr. Pollard:

On behalf of the Real Property, Probate and Trust Law Section of The Florida Bar ("Section"), I am submitting comments regarding the Federal Housing Finance Agency's Proposed Part 1228 Rule on Private Transfer Fee Covenants (RIN 2590-AA41) (the "Proposed Rule") announced in the Agency's Feb 1, 2011 News Release.

The Section is a group of over 9,500 Florida lawyers who practice in the areas of real estate, probate, trust and estate law, and who are dedicated to serving all Florida lawyers and the public in these fields of practice. We produce educational materials and seminars, assist the public pro bono, draft legislation, draft rules of procedure, and occasionally offer advice to the judicial, legislative and executive branches to assist on issues related to our fields of practice.

The Section is writing to the Federal Housing Finance Agency ("Agency") because the Section has a substantial, institutional history and perspective involving private transfer fee covenants and how they are used in practice. The perspective of the Section is oftentimes broader and more independent than those of individuals or a particular constituency. Indeed, the Section and its executive council are comprised of members who represent virtually every segment of the residential real estate market, including condominium unit owners, residential lenders, consumer purchasers, real estate brokers, contractors, non-developer controlled community associations, construction lenders and developers, to name a few.

So, we appreciated the opportunity to submit comments at an earlier stage of this process and are supportive of the "carve outs" for existing encumbrances and condominium and home owners' associations in the latest draft. However, as is so often the case, the "Devil is in the Details" and we suggest the language of the Proposed Rule is still problematic in several details:

1. Definition of "Direct Benefit"

The term "Direct Benefit" as defined presents a number of concerns:

a. The phrasing around the term "exclusively" in its various usages is problematic as applied to specific examples:

i. How narrowly is "exclusively" to be read? May the association use some of the proceeds to pay salaries, postage, or for contracted services from a management company? Are the fees and charges payable for estoppel letters or certificates issued by the association or its authorized agent "exclusively" for the direct benefit of the encumbered property?[1] None of these charges seem to fall within the "direct benefit" definition. Absent a clarification of the rule, a covered association would have to maintain a very strict segregation of funds derived from an "excepted transfer fee covenant." Perhaps more importantly, the actual use of the proceeds of a private transfer fee is not something that can usually be determined from a review of the recorded covenant.

ii. A normal development practice is to have a separate condominium association for each condominium component of the development, and for those to cooperate through membership in a master association embodying all of the condominium associations. A similar legal structure has been used in many large scale developments. Each "neighborhood" will have its own homeowners' association under a "master association." In many circumstances, the assessments and transfer fees are assessed and collected by the lowest level association and distributed upstream.

The exclusivity concepts in the Proposed Rule present difficulties as applied to this type of stacked multi-tier associations. There is no express approval for a group of related (or unrelated) associations to cooperate on common cultural, educational, recreational or other activities. Further, the 1,000 yard (a little over ½ mile) limitation contained in the definition of "adjacent or contiguous property" is not sufficient for some of Florida's large scale developments. The Proposed Rule also needs to address the potential cooperation among existing associations whose assessments may or may not fall within the scope of the rule.

[1] The charge for an estoppel letter itself is a "private transfer fee" as defined in that it is "required to be paid in connection with or as a result of a transfer of title to real estate." Thus, the question becomes whether the estoppel letter fee provides a "direct benefit" "exclusively" to the encumbered properties so as to be exempt.

iii. Consider the payment by a homeowners' association for road maintenance in a community where (as is the norm) only the subdivision lots are subject to the encumbrance. While this is obviously not the intent of the Proposed Rule, the first sentence of the definition states that the proceeds must be used "exclusively to support maintenance and improvements to encumbered properties." The following sentence states "such benefit must flow to ... the encumbered properties and their common areas or to adjacent or contiguous property." But the term "benefit" in that context could easily be interpreted as limited to the "cultural, educational, charitable, recreational," etc. benefits listed in the prior clause and not to the more narrow category of "maintenance and improvements"

b. The rationale used to sell legislatures on investing public funds in environmental and conservation programs has often been that they provide benefit to all of mankind, even when they are not readily accessible to most citizens. Applying the exclusive benefit concept to environmental and conservation programs is thus problematic.

c. The last sentence of the definition of "Direct Benefit" reads:

> A private transfer fee covenant will be deemed to provide a direct benefit when members of the general public may use the facilities funded by the transfer fees in the burdened community and adjacent or contiguous property only upon payment of a fee, except that *de minimis* usage may be provided free of charge for use by a charitable or other not-for-profit group.

While this may be the appropriate standard for the use of a clubhouse or a golf course, many of the projects funded by an association will be in the nature of roads, landscaping, irrigation, street lighting, parks, and playgrounds and other common areas where the exclusion of non-residents is simply not feasible and, in the case of roads in an un-gated community, not desirable.

2. Definition of Private Transfer Fee.

The definition is still too inclusive. Under the Proposed Rule, FNMA, FHLMC and the Federal Home Loan Banks would not be permitted to hold any property encumbered by a non-exempt private transfer fee covenant. Unfortunately, as defined, the prohibition would apply to:

a. Standard Fannie/Freddie mortgages, which include a "due on sale" clause[2]. Again, this is clearly not the intent – but highlights the drafting concerns.
b. Deferred commission or participation agreements in which the seller, a Realtor®, or other party is entitled to a payment based upon subsequent appreciation, development, or sale of the property.
c. Contracts in which a payment is due from the owner upon the sale of the property. It is not uncommon to tie the timing of a payment under a contract or of an unsecured debt to a liquidity event, like the sale of a certain property, and to record those agreements to assure payment.
d. Participating mortgages in which additional payments are due based on subsequent appreciation, development, or sale of the property.
e. A mortgage which provides for the payment of a fee should the lender consent to a sale and assumption.

If these latter types of agreements are evidenced in the public records, even if subordinate to the mortgage being acquired by the Regulated Entities, it would seemingly fall within these definitions and preclude the holding of the mortgage.

3. Mechanical/Implementation Issues.

The application of the Proposed Rule to each individual parcel, as distinguished from transfer fee covenants which apply to an entire condominium or subdivision, adds a significant level of complexity. If the Proposed Rule is limited to the subdivision or condominium level, the certifications normally done prior to the first FNMA/FHLMC mortgage in a community could be expanded to cover transfer fees[3]. However, applying the Proposed Rule to every single parcel will presumably necessitate some sort of certification process for every mortgage before that mortgage may be placed with one of the Regulated Entities.

The land title industry is not currently equipped to satisfy that need. Under current practices, the title insurance agent will identify covenants and restrictions affecting the property generally.

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[2] In pertinent part, the "due on sale" language of FNMA form 3010 reads:

> If all or any part of the Property or any Interest in the Property is sold or transferred (or if Borrower is not a natural person and a beneficial interest in Borrower is sold or transferred) without Lender's prior written consent, Lender may require immediate payment in full of all sums secured by this Security Instrument.

This falls within the definition of a "Private transfer fee," as it is a "payment, imposed by a covenant, restriction or other similar document and required to be paid in connection with or as a result of a transfer of title to real estate." Since the due on sale clause is contained within the recorded mortgage that runs with the land, the clause meets the test of a private transfer fee covenant . The mere fact that its enforcement is discretionary on the part of the mortgage holder cannot be viewed as a basis for circumventing the rule, or any transfer fee covenant could be drafted as discretionary.

[3] To the extent it can be determined from an examination of the public records.

The agent may also offer certain specific coverages under the ALTA form 4, 5 and 9 series of endorsements. Current examination practices do not include a review and analysis of whether anything in those covenants or other recorded instruments might constitute a private transfer fee as defined in the Proposed Rule, and given the multiple requirements for "exclusivity" of benefit discussed above, an examination of the record alone will not be sufficient to determine whether a transfer fee is exempt.

Under Florida administrative rules, title agents and insurers are prohibited from providing "affirmative coverages" beyond the scope of the approved policy forms and endorsements. Fla. Admin. Code §69O-186.005(7)(b). Any certification by the agent or insurer – even in letter form -- that a property is not encumbered by a non-exempt private transfer fee covenant would likely be a violation of this regulation. In the medium term, it may be possible for underwriters to negotiate a "work-around" of some type for their agents, or working with ALTA to develop and get approval for an appropriate "No Transfer Fees" endorsement – but either of those approaches cannot be accomplished before the proposed effective date of the Proposed Rule.

As discussed above, the prohibition on purchasing and investing is of "properties encumbered by private transfer fee covenants" without regard to whether those interests may be subordinate to the mortgage being acquired. It is thus possible for events occurring subsequent to the recording of the mortgage to render a mortgage ineligible under the Proposed Rule (and such events may not require the consent of the parcel owner, and may well occur without the knowledge of the parcel owner). Certifications made at the time the mortgage was made could not reveal such matters (or necessarily the potential or likelihood of occurrence), so presumably some sort of recertification would be required prior to acquisition by the regulated entities (if a new certification is even possible).

This draft of the Proposed Rule is a substantial improvement over the Proposed Guidance, but would still benefit from further elaboration and clarification.

Thank you for the opportunity to offer our insights into this process.

Sincerely,

REAL PROPERTY, PROBATE AND TRUST LAW SECTION OF THE FLORIDA BAR

Brian J. Felcoski, Chair