
FEDERAL HOUSING FINANCE AGENCY



NEWS RELEASE

For Immediate Release
August 12, 2010

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FHFA Proposes Guidance to Restrict GSEs from Investing in Mortgages with Private Transfer Fee Covenants

Washington, DC – The Federal Housing Finance Agency is proposing a guidance for public comment that would restrict Fannie Mae, Freddie Mac and the Federal Home Loan Banks from investing in mortgages with private transfer fee covenants. The guidance would extend to mortgages and securities purchased by the Federal Home Loan Banks or acquired as collateral for advances, and to mortgages and securities purchased or guaranteed by the Enterprises.

The covenants, often attached to property by a developer, require a transfer fee upon each resale of the property. FHFA has expressed concerns about the fees in congressional testimony and other statements. A Notice of Proposed Guidance that has been sent to the *Federal Register* for publication details these concerns and seeks public comment on the proposal.

“The private transfer fee covenants appear to run counter to the important mission of the housing GSEs to increase liquidity, affordability and stability in the nation’s housing finance system,” said FHFA Acting Director Edward J. DeMarco. “Encumbering housing transactions with fees that may not be properly disclosed may impede the marketability and the valuation of properties and adversely affect the liquidity of securities backed by mortgages on those properties.”

The Notice of Proposed Guidance describes concerns that private transfer fees may:

- increase the costs of homeownership;
- limit property transfers or render them legally uncertain;
- detract from the stability of the secondary mortgage market, particularly if such fees will be securitized;
- expose lenders, title companies and secondary market participants to risks from unknown potential liens and title defects; and
- contribute to reduced transparency for consumers because the fees often are not disclosed by sellers and are difficult to discover through customary title searches, particularly by successive purchasers.

Although proponents of the private transfer fees advocate that they are beneficial when used to fund projects that enhance community investments, FHFA is concerned that the fees fund purely private streams of income for select market participants and do not benefit

homeowners. Further, even if the fees are dedicated to homeowners associations, they are not proportional or related to the purposes for which the fees were to be collected.

“The risks and uncertainties for the housing market that come with the use of private transfer fee covenants do not appear to be counterbalanced by sufficient positive effects,” said DeMarco. “We are seeking public comment before finalizing this guidance in order to identify and respond to any related issues or concerns.”

The public comment period on the proposed guidance will remain open for sixty days after the Notice of Propose Guidance is published in the *Federal Register*.

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The Federal Housing Finance Agency regulates Fannie Mae, Freddie Mac and the 12 Federal Home Loan Banks. These government-sponsored enterprises provide more than \$5.9 trillion in funding for the U.S. mortgage markets and financial institutions.

FEDERAL HOUSING FINANCE AGENCY

[No. 2010-N-11]

Private Transfer Fee Covenants

AGENCY: Federal Housing Finance Agency.

ACTION: Notice of proposed guidance; request for comments.

SUMMARY: The Federal Housing Finance Agency (FHFA) is proposing to issue a Guidance, "Guidance on Private Transfer Fee Covenants," 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. Such covenants appear adverse to liquidity, affordability and stability in the housing finance market and to financially safe and sound investments. This 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.

DATES: Interested persons may submit comments on or before [INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER].

COMMENTS: Submit comments to FHFA using any one of the following methods:

- E-mail: regcomments@fhfa.gov. Please include “Guidance on Private Transfer Fee Covenants, (No. 2010-N-11)” in the subject line of the message.
- Mail/Hand Delivery: Alfred M. Pollard, General Counsel, Federal Housing Finance Agency, Fourth Floor, 1700 G Street NW., Washington, DC 20552, ATTENTION: Public Comments “Guidance on Private Transfer Fee Covenants, (No. 2010-N-11)”.
- Federal eRulemaking Portal: <http://www.regulations.gov>. Follow the instructions for submitting comments.

FOR FURTHER INFORMATION CONTACT: Peggy K. Balsawer, Assistant General Counsel, (202) 343-1529 (not a toll-free number), Federal Housing Finance Agency, Office of General Counsel, Fourth Floor, 1700 G Street NW., Washington, DC 20552. The telephone number for the Telecommunications Device for the Deaf is (800) 877-8339.

SUPPLEMENTARY INFORMATION:

I. Comments

FHFA invites comment on all aspects of the proposed guidance, including comments on which actions by FHFA would be most appropriate to address the concerns posed by private transfer fees. The comment period will end on [INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER]. Copies of all comments will be posted on FHFA’s Internet web site at <http://www.fhfa.gov>. In addition, copies of all comments received will be available for examination by the public on business days between the hours of 10 a.m. and 3 p.m., at the Federal Housing

Finance Agency, Fourth Floor, 1700 G Street, NW., Washington, DC 20552. To make an appointment to inspect comments, please call the Office of General Counsel at (202) 414-6924.

II. Background

Establishment of FHFA

FHFA is an independent agency of the Federal Government and was established by the Housing and Economic Recovery Act of 2008 (HERA), Public Law 110-289, 122 Stat. 2654 to regulate and oversee the Enterprises and the Banks (collectively, the regulated entities). HERA amended the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (12 U.S.C. 4501 et seq.) (Safety and Soundness Act) and the Federal Home Loan Bank Act (12 U.S.C. 1421 through 1449) to enhance the authorities and responsibilities of the new agency. FHFA's regulatory mission is to ensure, among other things, that each of the regulated entities "operates in a safe and sound manner" and that their "operations and activities ... foster liquid, efficient, competitive, and resilient national housing finance markets." (12 U.S.C. 4513(a)(1)(B).)

III. Federal Housing Finance Agency Guidance

A private transfer fee covenant is attached to real property by the owner or another private party, frequently, the property developer, and provides for a transfer fee to be paid to an identified third party (such as the developer or its trustee) upon each resale of the property. The fee typically is stated as a percentage, such as one percent of the property's sales price and often survives for a period of ninety-nine (99) years.

FHFA has expressed concerns about private transfer fees in congressional testimony and in other public statements. FHFA is publishing this Notice in order to receive public comment on this proposed draft Guidance.

Promoters of private transfer fees and their possible securitization argue that such fees are beneficial when used to fund project developments or to enhance community investments through homeowners associations or through affordable housing groups, environmental groups, or other charitable organizations.

FHFA is concerned that such fees are used to fund purely private continuous streams of income for select market participants either directly or through securitized investment vehicles. Further, it is unclear that the fees, even if dedicated to homeowners associations, are proportional or related to the purposes for which the fees were to be collected. FHFA's draft Guidance is based on the view that investments in mortgages on properties with private transfer fee covenants and securities designed to generate income from the fees are not acceptable for the regulated entities. FHFA's draft Guidance does not distinguish between private transfer fee covenants which purport to render a benefit to the affected property and those which accrue value only to unrelated third parties.

Encumbering housing transactions with fees that may not be properly disclosed and that may limit the alienation of property means that such fees may impede the marketability and the valuation of properties and adversely affect the liquidity of securities backed by mortgages so encumbered. FHFA is concerned that such consequences will have a particularly detrimental effect on still fragile housing markets. FHFA's position is also influenced by considerations of consumer protection where disclosures may be insufficient and add costs not fully understood by consumers.

FHFA recognizes that there is a range of actions it can take, including to require the regulated entities to report on the extent of their exposure to private transfer fee covenant investments, change seller/servicer guides to identify restrictions on the purchase of encumbered mortgages, create and enforce additional representations and warranties against encumbered mortgages, or to prohibit the purchase or investment in the mortgages or the revenue generated by the fees.

FHFA's draft Guidance directs that the Enterprises should not purchase or invest in mortgages encumbered by private transfer fee covenants or securities backed by private transfer fee revenue, as such investments would be unsafe and unsound practices and contrary to the public missions of the Enterprises and the Banks. Likewise, the draft Guidance would direct that the Banks should not purchase or invest in such mortgages or securities or hold such mortgages as collateral for advances.

IV. Proposed Guidance

The proposed draft Guidance follows:

Federal Housing Finance Agency

Guidance on Private Transfer Fee Covenants

Issuance Date: August XX, 2010

I. Introduction

The Federal Housing Finance Agency (FHFA) is an independent agency of the Federal Government and was established by the Housing and Economic Recovery Act of 2008 (HERA), Public Law 110-289, 122 Stat. 2654 (2008) to regulate and oversee the Federal National Mortgage Association (Fannie Mae), the Federal Home Loan Mortgage

Corporation (Freddie Mac) (collectively, the Enterprises), and the Federal Home Loan Banks (collectively, the Banks). HERA amended the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (12 U.S.C. 4501 et seq.) and the Federal Home Loan Bank Act (12 U.S.C. 1421 through 1449) to enhance the authorities and responsibilities of the new agency.

The respective federal charters of the Enterprises reflect their public mission to “provide stability in the secondary market for residential mortgages,” “respond appropriately to the private capital market,” “provide ongoing assistance to the secondary market for residential mortgages . . . ,” and “promote access to mortgage credit throughout the Nation . . .” (see section 301 of the Fannie Mae Charter Act and section 301(b) of the Freddie Mac Corporation Act.) FHFA’s regulatory mission is to ensure, among other things, that each regulated entity it supervises “operates in a safe and sound manner” and that their “operations and activities . . . foster liquid, efficient, competitive, and resilient national housing finance markets.” (12 U.S.C. 4513(a)(1)(B)).

II. Private Transfer Fees

A private transfer fee covenant is attached to real property by the owner or another private party (frequently, the property developer) and requires a transfer fee payment to an identified third party, such as the property developer or its trustee, a homeowners association, an affordable housing group or another community or non-profit organization, upon each resale of the property. The fee typically is stated as a percentage (e.g., 1 percent) of the property’s sales price and often survives for a period of ninety-nine (99) years.

Some states have legislated against private transfer fee covenants in all circumstances. Other states permit them only when they benefit a homeowners association or community organization or when they have been adequately disclosed. Still other states have no position on such covenants.

Proponents of private transfer fees argue that these fees have positive effects when the proceeds offset initial infrastructure improvements or to fund new improvements to existing communities. Further, they argue that payments at the time of a resale are intended to reimburse the developers or investors for their initial outlays. At the same time, opponents argue that these community goals can be achieved through more transparent and equitably distributed assessments on all commonly affected property owners. Many covenants are not intended for purely community purposes and, instead, create purely private continuous streams of income for select market participants either directly or through securitized investment vehicles.

III. FHFA Guidance to the Enterprises and the Banks

FHFA has found that the typical one percent fee at the time of resale is neither a minimal nor a reasonable amount; further, such fees may be in excess of one percent. Such fees increase by a meaningful amount the seller's and potentially the buyer's burden at the time of a property sale. Expanded use of private transfer fee covenants poses serious risks to the stability and liquidity of the housing finance markets.

Further, FHFA has concerns that private transfer fee covenants, regardless of their purposes, may:

- increase the costs of homeownership, thereby hampering the affordability of housing and reducing liquidity in both primary and secondary mortgage markets;
- limit property transfers or render them legally uncertain, thereby deterring a liquid and efficient housing market;
- detract from the stability of the secondary mortgage market, particularly if such fees will be securitized;
- expose lenders, title companies and secondary market participants to risks from unknown potential liens and title defects;
- contribute to reduced transparency for consumers because they often are not disclosed by sellers and are difficult to discover through customary title searches, particularly by successive purchasers;
- represent dramatic, last-minute, non-financeable out-of-pocket costs for consumers and can deprive subsequent homeowners of equity value; and,
- complicate residential real estate transactions and introduce confusion and uncertainty for home buyers.

The risks and uncertainties for the housing finance market that are represented by the use of private transfer fee covenants are not counterbalanced by sufficient positive effects. To the extent that private transfer fee covenants benefit unrelated third parties, one cannot claim that a service or value is rendered to the relevant property owner or community. Even where such fees are payable to a homeowners association, unlike more typical annual assessments they are likely to be unrelated to the value rendered, and at

times may apply even if the property's value has significantly diminished since the time the covenant was imposed.

FHFA regards such purchases as inconsistent with the Enterprises' public missions to promote liquid, efficient and stable housing finance markets. FHFA does not consider mortgages encumbered by private transfer fee covenants to be prudent or safe or sound investments for the Enterprises or the Banks. Consequently, Fannie Mae and Freddie Mac should not purchase or invest in any mortgages encumbered by private transfer fee covenants or securities backed by such mortgages. The Banks should not purchase or invest in such mortgages or securities or hold them as collateral for advances.



Date: 8/10/2010

Stephen Cross

Deputy Director of the Division of Federal Home Loan Bank Regulation, By delegation
Federal Housing Finance Agency.