July 22, 2011

Jennifer Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

RE: Docket No. R-1417

Dear Ms. Johnson:

On behalf of Community Associations Institute (CAI),[1] I am pleased to submit the following comments on the Federal Reserve Board's proposed revisions to Regulation Z pursuant to the Dodd Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd Frank) that: (1) require lenders to verify a borrower's ability to repay mortgage obligations (2) limit points and fees for covered transactions and (3) define "qualified mortgage" (QM). CAI is the nation's leading voice on matters affecting the millions of American households residing in neighborhoods and communities governed by a community association.

CAI appreciates the Board's careful approach in the proposed revisions to Regulation Z. The Board has provided housing market participants with extensive insight into the overall approach used in drafting the proposed revisions and seeks comment on aspects of the proposal where statute is unclear or where generally accepted and long-standing market practices may be unintentionally impeded by the proposal. Based on a review of the Board's proposal, CAI's members have expressed four general areas of concern: (1) Verification of Ability-to-Repay; (2) Inclusion of Special Assessments in the Ability-to-Repay Calculation; (3) Treatment of Community Transfer Fees; and (4) Definition of Points and Fees for Qualified Mortgages.

6402 Arlington Blvd.
Suite 500
Falls Church, VA 22042

888.224.4321 TOLL-FREE
703.970.9220 Main
703.970.9558 Fax

www.caionline.org

[1] CAI is the only national organization dedicated to fostering competent, well-governed community associations that are home to approximately one in every five American households. For nearly 40 years, CAI has been the leader in providing education and resources to the volunteer homeowners who govern community associations and the professionals who support them. CAI's 30,000 members include community association volunteer leaders, professional managers, community management firms, and other professionals and companies that provide products and services to community associations.

Verification of Ability-to-Repay

Membership in a community association creates a common bond among homeowners.[2] Under the community association structure, associations are often responsible for waste removal expenses, maintenance of community infrastructure, utility services, and insurance premiums. Additionally, the association is responsible for preparing an appropriate operating budget that funds current association obligations and adequately reserves for anticipated future infrastructure costs. All association members pay assessments that fund these critical association services. To ensure each member of the association pays their fair share, association assessments are mandatory and lien-based. The common bond among homeowners in a community association is an important reason CAI supported provisions of Dodd Frank requiring that lenders verify borrowers have the ability to pay all regularly occurring obligations required to keep their mortgage current, including periodic common expense assessments remitted to a governing community association.

Requirements Disclosure of Association Assessments Prior to Sale
In general, CAI supports the Board's view that community association assessments be a required element in mortgage-related obligations under the proposed rule. A homeowner's community association assessments are critical to the proper functioning of the association. When a homeowner is unable to pay assessments, all other homeowners are forced to bear the expense of the delinquency. Association assessments are lien-based to protect the financial interests of all owners in the community. Ensuring borrowers are qualified on the basis of their ability to pay periodic common expense assessments will reduce assessment delinquencies in community associations, protecting all homeowners from unanticipated housing costs.

Many states have adopted the Uniform Common Interest Ownership Act (UCIOA), drafted and supported by the National Conference of Commissioners on Uniform State Laws.[3] Under UCIOA, property owners are required to provide certain information to a buyer if the unit or property is located in a community association. Included in the information the owner must provide the purchaser is the current periodic common expense assessment for the unit or property as well as any unpaid common expense or special assessment. By matter of industry practice, this information (including other documentation) is supplied by the governing community association to the owner for a fee.[4] CAI notes that UCIOA requires the owner provide information to a purchaser, not the association.[5]

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[2] All community associations have three defining characteristics: (1) membership is mandatory and automatic for all owners; (2) certain documents bind all owners to be governed by the community association; and (3) mandatory lien-based assessments are levied on each owner in order to operate and maintain the community association. There are three basic types of community associations: condominiums, cooperatives and planned communities.
[3] The most recent version of the Uniform Common Interest Ownership Act may be viewed at: http://www.law.upenn.edu/bll/archives/ulc/ucioa/2008final.pdf.
[4] *For the Common Good: Use of Community Transfer Fees by Community Associations*: Page 2, disclosures to buyers occur in 96.3% of transactions.
[5] Uniform Common Interest Ownership Act (2008) § 4-109(a)

Inclusion of Association Assessments in Monthly Mortgage Obligations
In general, CAI's members support the Board's proposed requirement that borrowers be qualified on the basis of their ability to pay all mortgage-related obligations, which includes periodic common expense assessments for properties in a community association. Qualifying borrowers on this basis will reduce incidence of assessment delinquencies, which protects the financial stability of borrowers while also promoting the overall fiscal health and stability of community associations. While CAI's members support this aspect of the Board's proposal, several operational matters must be considered so that creditors receive accurate and timely information about a borrower's association-based mortgage-related obligations.

The Board recognizes that application of an ability-to-repay standard for all mortgage loans is a new regulatory requirement on the housing finance system. This requirement will necessitate that creditors obtain and verify the accuracy of certain information from third parties with no direct interest in the underlying mortgage transaction in order to comply with the ability-to-repay standard. Failure to verify the accuracy of such information can expose creditors to significant legal liability and substantial monetary damages under the Truth in Lending Act (TILA).[6] Additionally, a creditor's failure to comply with verification of a borrower's ability-to-repay can be used by a borrower as a defense to foreclosure.

These are new and substantial liabilities for lenders and, by extension, the third parties providing information that is material to the underwriting process, verification of ability-to-repay, and the determination to extend credit. To avoid delays in obtaining and gaps in the information necessary for a creditor to make a determination on a borrower's ability-to-repay, the Board must consider the practical means by which this information will be collected and shared, and the obligations this may create for community associations.

Association Boards, Managers and Management Companies Hesitant to Assume Liability
CAI is concerned that community association boards, managers and management companies will be hesitant or will refuse to supply information to creditors regarding the periodic common expense assessment for a unit of housing if doing so increases their legal liability. An important example of this in the current market is the reluctance of some condominium associations, community association managers and community association management companies to supply lenders information regarding FHA-related condominium unit mortgages or to fully respond to creditor questionnaires regarding common expense assessments and special assessments.

Recent changes to FHA's condominium unit mortgage insurance programs require creditors and condominium associations to attest under threat of criminal penalty to certain information regarding the condominium prior to approval for participation in FHA mortgage insurance programs and prior to FHA endorsement. Condominium association boards and managers are hesitant to provide information for FHA program approval or lender loan level certifications, as the information is either not readily available or doing so significantly increases legal liabilities. The impact on individual borrowers is that FHA-supported financing is not available. In fact, FHA recently disclosed that of a potential 12,000 condominiums eligible for recertification under the Agency's new condominium unit mortgage insurance program, only 1,000 have been recertified.[7]

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[6] 15 U.S.C. § 1601 et seq.

Legal Certainty for Third Parties, Use of Estimates and Borrower Supplied Information
CAI recognizes the Board attempts to facilitate creditor collection of information material to a determination of ability-to-repay by allowing creditors to use "reasonably reliable" information supplied by third parties, including information regarding mortgage-related obligations.[8] The Board will also permit the use of estimates for certain mortgage-related obligations if the estimate is based on "information that is known to the creditor at the time the creditor underwrites the mortgage obligation"[9] and complies with certain standards for disclosure on the basis of an estimate.[10]

Notwithstanding this flexibility, the Board holds a creditor liable for information affecting a borrower's ability-to-repay if records show that a material change in this calculation may occur after closing. Relevant Official Staff Interpretations indicate that if a creditor knows a borrower's verified current income is likely to be reduced given the borrower's intention to retire within 12 months of closing that the creditor must determine ability-to-repay on the basis of the borrower's future rather than current income.[11] This policy means, by extension, a creditor may be liable for any material change to any variable in the ability-to-repay calculation that the creditor could have discovered in the underwriting process. CAI's members are disturbed by this aspect of the Board's proposal, especially as it may apply to information supplied by a community association to a creditor regarding a unit's common expense assessment. (A discussion of the treatment of special assessments follows.)

Creditors commonly seek information from community associations when financing the sale of property in an association. Such requests are most commonly associated with the sale of a condominium unit and seek information pertaining to the unit's common expense assessment, any outstanding special assessment, and any pending special assessment. Condominium boards, community association managers and community association management companies routinely refuse to provide such information to lenders absent an agreement by the lender that the association, in providing the information, does not attest to its accuracy.

Under the Board's proposal, creditors face substantial penalties for failure to predict or to account for a potential change in any of the variables used to determine a borrower's ability to repay. As creditors will rely on information supplied by a community association to comply with this aspect of the proposal, CAI's members are concerned that creditors will no longer accept questionnaires that limit a responding association's legal liability for the information provided.

The application of ability-to-repay now extends to most mortgage credit transactions. As a result, creditors will be submitting requests to all community associations, not just condominiums, for information on mortgage-related obligations. CAI's members believe it is likely the existing difficulty in sharing such information will spread to most of the 300,000 community associations

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[7] *FHA's new rules: more pain for condo market—calculated phase down under way?* July 19, 2011, by Ken Harney: www.inman.com/buyers-sellers/columnists/kenharney/fhas-new-rules-more-pain-condo-market
[8] Proposed § 226.43(c)(3)
[9] Proposed Official Staff Interpretation Paragraph 43(c)(2)(v)-3
[10] 12 C.F.R. § 226.17(c)(2)(i)
[11] Proposed Official Staff Interpretation Paragraph 43(c)(1)-1

across the country. To minimize the potential for delays and increased costs for borrowers, community associations and creditors, CAI offers the following observations and recommendations for the Board's consideration.

1. CAI Urges the Board to Provide Guidance for Ability-to-Repay Questionnaires

CAI believes the Board can facilitate the exchange of information by community associations to creditors by providing guidance to creditors on the substance of questionnaires that seek information from third parties about a borrower's mortgage-related obligations. CAI does not believe it necessary for the Board to provide a standard form to creditors for this purpose; rather CAI believes proscribing a form would be disruptive.

Appropriate direction in the Board's Official Staff Interpretations describing the acceptable means by which a creditor may verify and document a borrower's periodic common expense assessments could encourage the sharing of information. Incorporating such a system will allow community associations and creditors to work cooperatively to design effective questionnaires to obtain required information in a manner that avoids market disruption and unnecessary increases in costs. Further, this would create a legal structure providing certainty for both the creditor and the association regarding future changes in the information provided, such as an increase in common expense assessments or the adoption of a special assessment by the association. In both cases, neither the creditor nor the association is in a position to predict outcomes.

Placing liability on the creditor, and by extension increasing an association's litigation risk, will only restrict the sharing of information and could restrict a borrower's access to credit on the best possible terms. This is particularly the case if market participants react to this aspect of the Board's proposal in a manner similar to the reaction against FHA's revised condominium unit mortgage insurance guidelines. In this instance, substantially fewer condominium owners or buyers have access to FHA-supported mortgages. Such an outcome seems counter to the goal of the ability-to-repay standard and effectuating the purposes of TILA.

2. CAI Encourages the Acceptance of Estimated Association Assessments for Ability-to-Repay

Notwithstanding any response the Board may contemplate regarding the exchange of information between community associations and creditors regarding mortgage-related obligations, CAI's members believe the Board should ensure that creditors clearly have authority to estimate mortgage-related expenses. In this regard, the Board's proposal discusses the difficulty creditors may have in determining mortgage-related obligations, such as property tax payments, and the challenges this may pose to creditors when making an ability-to-repay determination. The Board requests comments on the appropriateness of allowing creditors to reasonably estimate such payments for the purposes of compliance with the ability-to-repay standard.

CAI's members believe this is an appropriate approach for the Board to take that recognizes the difficulty that creditors will face when complying with the proposal and believe the use of reasonable estimates of association assessments will improve market function. If a creditor should encounter resistance from a community association where the association board has a policy of not responding to creditor questionnaires due to the risk to the association this may pose, permitting the creditor to estimate a borrower's common expense association assessment

will allow the transaction to proceed. Further, if a creditor is permitted to request an estimate of the borrower's common expense assessment, community associations are more likely to provide the requested information.

3. Reliance on Borrower as Source of Association Assessment Information

As previously noted, the Uniform Common Interest Owners Act requires the disclosure of certain information by a seller to a buyer. Specifically, the Act requires a seller to disclose the rate of common expense assessments, any outstanding common expense assessments, and any outstanding special assessment. In its proposal, the Board permits creditors to rely on certain information supplied by the borrower, such as a self-prepared tax return, which is material to a creditor's determination the borrower has the ability-to-repay a loan. CAI believes it an appropriate approach for the Board to permit a borrower, acting through the seller, to provide information regarding (actual or estimated) common expense association assessments. Many states impose on sellers the legal obligation to provide this information to buyers, and verifiable and documented evidence of such regularly occurring payments can be made available to the buyer by the seller. Information pertaining to assessment rates, as well as any outstanding assessments, are generally specific to the unit of housing in question, which would, in CAI's view, meet the Board's standard that all information used by a creditor to make an ability-to-repay determination be specific to the borrower.[12] This approach serves to place the burden of disclosure and associated liability on the parties to the transaction which is the most efficient means of obtaining the information and limited the chain of liability.

Inclusion of Special Assessments in Ability-to-Repay

Community associations raise revenue through limited means: periodic common expense assessments; user and other fees; and special assessments. The last category of revenue, special assessments, occurs when an association faces a large non-budgeted expense and the owners vote to assess an additional amount to cover these costs.

The Board proposes to include special assessments in mortgage-related obligations for the purpose of determining a borrower's ability-to-repay. The Board seeks to define special assessments as "… assessments that are imposed on the consumer at or before consummation, such as a one-time homeowners' association fee that will not be paid by the consumer in full at or before consummation."[13]

CAI's members have strong reservations regarding the inclusion of special assessments as an underwriting requirement to determine if a borrower will have access to mortgage credit or to govern mortgage rates and terms. CAI's members believe the Board's proposed policy, if not amended, will significantly harm the economic interests of the households owning property in a community association. CAI respectfully offers the following observations and recommendations for the Board's consideration.

[12] Proposed Official Staff Interpretation Paragraph 43(c)(3)-1
[13] Proposed Official Staff Interpretation Paragraph 43(b)(8)

1. Special Assessment Criterion Unfairly Penalizes Borrowers in Community Associations

CAI's members are concerned that criteria regarding special assessments may reach beyond the intent of Congress, applying extraordinary underwriting criteria to borrowers seeking to purchase a home in a community association or to refinance an existing mortgage. Special assessments occur when associations face unexpected expenses such as high snow removal costs and other unanticipated costs. In this regard, owners living in a community association are no different than owners in other neighborhoods. Every homeowner faces unanticipated costs from time to time, yet the Board does not propose individual underwriting criteria to address this fact for all borrowers.

A key difference between homeowners in a community association and non-association homeowners is that community associations are required to set aside reserves for the anticipated replacement costs of common infrastructure. The ability to share in these expenses through reserving and through special assessments, rather than covering such expenses individually, provides a substantial advantage to owners in a community association.

CAI believes that by including special assessments as a factor solely for borrowers in community associations, the Board is subjecting this sector of the market to a different set of underwriting requirements, effectively penalizing these consumers for purchasing housing of their choice. CAI's members believe this is fundamentally unfair, as this policy will restrict access to credit for these otherwise well qualified borrowers not due to any credit impairment but simply due to regulatory fiat.

2. Statute Addresses Regularly Occurring Mortgage-Related Obligations

Section 1141 of the Dodd Frank Act states:

> *§ 129C. Minimum standards for residential mortgage loans*
> *(a) Ability to Repay.—*
> > *(1) In General.—In accordance with regulations prescribed by the Board, no creditor may make a residential mortgage loan unless the creditor makes a reasonable and good faith determination based on verifiable and documented information that, at the time the loan is consummated, the consumer has a reasonable ability to repay the loan, according to its terms, and all applicable taxes, insurance (including mortgage guarantee insurance), and assessments.*

Further, Section 1412 of the Dodd Frank Act states:

> *(b)(2)(A)—*
> > *(iv) in the case of a fixed rate loan, for which the underwriting process is based on a payment schedule that fully amortizes the loan over the loan term and takes into account all applicable taxes, insurance, and assessments;*
> > *(v) in the case of an adjustable rate loan, for which the underwriting is based on the maximum rate permitted under the loan during the first 5 years, and a payment schedule that fully amortizes the loan over the loan term and takes into account all applicable taxes, insurance, and assessments;*

The statute, which discusses "taxes, insurance, and assessments," is concerned with payments that are regularly occurring and predictable as well as other terms that are regularly occurring,

quantifiable and clearly defined in loan documentation. CAI supports the inclusion of common expense assessments as a variable in the ability-to-repay calculation as these are expected periodic payments in the same manner that property taxes and hazard insurance payments are both widely expected by borrowers and predictably periodic in nature.

Further, the statute does not require common expense association assessments to be indexed at the maximum rate of increase under applicable state law in the ability-to-repay calculation. Congress was explicit in its concerns over payment escalation and payment shock due to changes in interest rates and other loan characteristics that contributed to borrower default. It is instructive that Congress did not treat increases in property taxes, insurance or assessments in a similar manner, as these are costs that all homeowners bear and have exposure to irrespective of their being located in a community association or not. Congress did not intend to insulate homeowners from the actual costs of homeownership in adopting the ability-to-repay requirement; rather, Congress was protecting borrowers from predatory mortgage terms. The Board's inclusion of special assessments in the ability-to-repay standard moves away from this standard and will cause economic harm to homeowners in community associations with an active special assessment and all future homeowners in community associations that adopt a special assessment. Accordingly, CAI urges the Board to remove special assessments from the proposed ability-to-repay standard.

2. If Special Assessments are Included in Ability-to-Repay, only Current Special Assessments Should be Included in Mortgage-Related Obligations

If the Board elects to retain special assessments in the calculation of a borrower's ability-to-repay, CAI members strongly urge the Board to clearly limit the standard to only those special assessments actually in force at time of disclosure. Community association boards, community association managers, community association management companies and creditors should not be required to speculate if a future special assessment will be adopted. Neither should these parties be asked to speculate on the amount of any future special assessments that may be applied to individual units or properties.

Community association board members and community association managers are increasingly advised not to complete lender questionnaires regarding special assessments due to legal liabilities associated with doing so. By way of example, the case of *Eisenberg v. Phoenix Management* [14]originated when a community association manager indicated on a lender questionnaire that no special assessments were planned by the association in question. Three months after closing, the association voted to approve a special assessment.

Upon approval of the special assessment, plaintiff sued the association's directors as well as the community association manager for failure to disclose a pending special assessment. The District Court ruled in favor of plaintiff, but this judgment was overturned by the Superior Court. Ultimately, the Massachusetts Appeals Court partially overturned and partially affirmed the Superior Court decision and awarded plaintiff damages of $8,000.

[14] Eisenberg v. Phoenix Ass'n Management, Inc: 56 Mass.App.Ct. 910, 777 N.E.2d 1265(2002)

While the dollar amount of damages was not that substantial, the case involved years of litigation and significant legal fees for all parties. Importantly, the case established legal precedent that in certain jurisdictions association directors and community association managers are liable if a special assessment is adopted after a mortgage loan closing has been completed, even when these persons, who are not parties to the underlying transaction, respond truthfully to a lender questionnaire that no special assessment is pending.

Due to the increased liability community association boards, which are populated entirely by volunteer homeowners from the community, and community association managers face when providing information to lenders that is not a requirement under TILA, CAI members are very concerned about exposure to significant litigation risk when providing information regarding special assessments for the purposes of the ability-to-repay standard. If the Board opts to retain special assessments as a variable in the ability-to-repay standard, CAI encourages the Board to clearly state that the only special assessments to be included in the calculation are those that are in force at the time the creditor certifies the borrower's ability-to-repay.

CAI members believe such a clarification is necessary given that proposed Official Staff Interpretation paragraph *43(c)(1)-1* appears to require lenders to take into account information regarding a borrower's ability-to-repay that cannot be readily verified and may be subject to change after closing. If the Board intends to expose creditors and, by extension, third parties providing information to creditors to substantial and open-ended litigation risk, CAI members do not believe the standard to be practical or achievable under any reasonable measure. If the Board does not intend to expose these parties to such litigation risk with regard to future special assessments, then the regulation and accompanying Official Staff Interpretation should be revised to reflect this intent.

3. If Special Assessments are Included in the Ability-to-Repay Standard, Lenders Should Follow *Pro Rata* Monthly Payment

The structure of special assessments can vary from association to association. For example, it is common for some associations to require a one-time payment of special assessments while other associations will accept quarterly payments or payments on a schedule negotiated between the association and the owner. Further, some associations will adopt a fixed special assessment for a certain period of time. If the Agencies pursue a special assessment criterion for the ability-to-repay standard, CAI strongly urges the Agencies provide creditors flexibility when qualify borrowers on the basis of a special assessment. Specifically, CAI members urge that where practical, a creditor use the *pro rata* monthly payment of a special assessment rather than qualifying a borrower on the basis of a one-time or quarterly payment.

CAI notes the Board appears to offer creditors the flexibility to use *pro rata* monthly payments in the ability-to-repay calculation. While there is no specific guidance offered for the treatment of special assessments, the Board refers to "widely accepted governmental or non-governmental standards" in determining *pro rata* amounts.[15] Other rulemakings to which the Board is a party refer to the ability of creditors to use *pro rata* monthly payments for special assessments as do FHA underwriting requirements.[16]

[15] Proposed Official Staff Interpretation Paragraph 43(c)(2)(v)-2

[16] Joint Agency Proposed Rule—Credit Risk Retention: Docket No. R-1411

CAI urges caution as the Board considers the requirement that lenders generally adopt underwriting standards of housing-related government agencies. Such agencies have statutory-based missions to serve specific populations and demographic groups and are not intended to serve as the primary means by which the general population accesses mortgage credit. CAI's members believe that while seemingly prudent, such a policy could apply criteria appropriate for the target populations served by these agencies to the general population, whom are not well-served by certain restrictions required for the agency to serve its mission-related consumers.

Treatment of Community Transfer Fees

In the preamble discussion of the Board's proposed rule, there is a single reference to homeowners association transfer fees. The Board "… solicits comment on how to address any issues that may arise in connection with homeowner's association transfer fees and costs associated with loans for energy-efficient improvement."

Some federal financial regulators, most notably the Federal Housing Finance Agency (FHFA), have recently examined the evolution of deed-based, private transfer fees in the housing market and the impact such fees have on consumers. Additionally, some national trade associations have expressed concerns over the market impact of deed-based, private transfer fees where fee proceeds flow to third parties with no interest in the encumbered land (third party transfer fees), and attempts to sell securities on the basis of these third party transfer fees.

Third party transfer fees are substantially different from deed-based transfer fees remitted to a governing community association. These fees, known as community transfer fees, directly support association activities and therefore provide a direct benefit to the encumbered properties. Community transfer fees have long been regarded by the Courts as falling within the traditional interpretation of the Law of Servitude and meeting the burden-benefit test.

Community transfer fees are a long-standing and important component of community associations and constitute a critical source of financial support for association activities. Ill-conceived regulations restricting the use of community transfer fees or restricting access to credit for homeowners living in a community association subject to a community transfer fee would be devastating. CAI strongly encourages the Board not to amend its proposal to affect the use of community transfer fees or to red-line via regulation communities with such fees.

To supplement CAI's observations and recommendations on the Board's proposal regarding transfer fees, CAI is attaching as an appendix two comment letters submitted to FHFA concerning community transfer fees. These documents discuss in depth the legal basis for community transfer fees, the long-standing and wide use of community transfer fees, and the substantial negative impact on homeowners if federal regulators attempt to vitiate or to regulate previously existing and valid private contractual obligations between homeowners and their community associations.

1. CAI's Members Oppose Third Party Transfer Fees

CAI's members unequivocally oppose deed-based transfer fees where fee proceeds are transmitted to third parties with no interest in the encumbered land. CAI strongly believes such deed-based fees do not meet the traditional interpretation of the Law of Servitude, which, in general, requires that any fee that burdens the land and purports to run with the land also benefit the land. Clearly, a deed-based transfer fee paid to a third party with no interest in the land does not benefit the land. Accordingly, CAI supports efforts by several state legislatures to void or render unenforceable third party, deed-based transfer fees. CAI also supports aspects of a pending FHFA rulemaking that will not permit Fannie Mae, Freddie Mac or the Federal Home Loan Bank System to support mortgage lending on properties subject to a third party transfer fee.

2. Community Transfer Fees Provide Direct Benefit and Positively Affect Valuation

CAI's members strongly support the long-standing practice of transfer fees that are payable to a governing community association. These community transfer fees support the governance, maintenance and operations of community associations, providing a direct benefit to the encumbered land. Indeed, in its proposed rule concerning deed-based transfer fees, FHFA found that "transfer fees paid to associations contribute to the value of the burdened property through the amenities and maintenance that they fund."[17]

CAI's members will strongly oppose any attempt by federal agencies to limit the extension of mortgage credit or to condition the terms of any mortgage credit extended to a consumer on the basis of a community transfer fee. In this context, CAI believes the intent of Congress in establishing the ability-to-repay and QM standards is to improve mortgage underwriting, not to have the Board become *de facto* federal regulator of community associations. Conditioning access to mortgage credit for residents of community associations on the basis of a community transfer fee does not improve mortgage underwriting; rather, it will in many cases irreparably harm the economic interests of these property owners. This is because federal financial regulators lack the legal authority to vitiate or render unenforceable private contracts that are lawful under both federal and state law. Federal financial regulators may only refuse to allow federally-related mortgage credit to flow to such properties or create other regulatory machinations intended to prevent the flow of credit to properties encumbered by a community transfer fee. In either case, the transfer fee will persist, but the owners of these properties will have no ability to market these assets, which will substantially lower values.

3. CAI Members Support Prior Disclosure of Homeowner Obligations

CAI strongly supports prior disclosure of all existing obligations purchasers undertake when living in a community association. CAI's public policy, *Disclosure Before Sales in a Community Association*,[18] clearly states our members' belief that state law should require prior disclosure of all fees, including any community transfer fees, to prospective purchasers well in advance of closing. Such existing prior disclosure requirements in most states allow purchasers meaningful opportunity to negotiate with sellers the payment of any transfer fee along with other *bona fide* costs associated with the transfer of real property in a community association. Further, the Uniform Common Interest Ownership Act provides consumers the right to rescind a purchase

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[17] 12 CFR Part 1228, RIN 2590-AA41, *Fannie Mae, Freddie Mac and the Federal Home Loan Banks Restrictions on the Acquisition of, or Taking Security Interests In, Mortgages on Properties Encumbered by Certain Private Transfer Fee Covenants and Related Securities,* page 18.

[18] CAI public policy, *Disclosure Before Sales in a Community Association*, is included as Attachment A to Appendix A, on pages 33-34 of this letter.

contract without penalty on the basis of their review of resale certificate disclosures required under Section 4-109 of the Act.

Definition of Points and Fees for Qualified Mortgages

The Agencies propose to limit total points and fees for mortgage loans satisfying QM requirements to no more than 3 percent of the total loan balance as required by Section 129C(b)(2)(C) of the Truth in Lending Act.[19] In general, the Board proposes to include real estate-related fees in the definition of points and fees unless the fees (1) are bona fide and reasonable; (2) are not paid, directly or indirectly, to a creditor or mortgage originator; and (3) the charge is not paid to an affiliate of the creditor or originator.

CAI's members are concerned the Board's proposal lacks sufficient guidance on the process of determining whether certain transactional fees, real estate-related or otherwise, are exempt from the 3 percent limitation. In particular, CAI's members are concerned that this lack of guidance may harm the economic interests of homeowners who have purchased a unit or property in a community association if the Board determines that certain community association-related transactional costs must be included in the calculation of points and fees.

CAI's members strongly urge the Agencies to more clearly define the process of determining total points and fees so all market participants have certainty regarding the applicable standards. CAI's members are concerned that creditors will interpret the Board's limitations on points and fees either too strictly or unevenly absent clear guidance. It is vital that consumers understand the regulatory-based factors that may increase their cost of credit and ensure that these factors are established and considered in a fair manner well in advance of closing. To that end, CAI offers the following commentary on practices that are long-standing and commonly associated with the purchase of real property in a community association.

1. Charges for Association Expenses Relating to Change of Ownership

It is a long-standing practice that many community associations assess a fee to purchasers to fund costs associated with a change in ownership of a unit or property. Associations opt for this approach rather than requiring all residents to subsidize expenses related to a change in ownership each time a unit or property is sold in the form of higher common expense assessments. This arrangement is fair to all owners in that each purchaser is required to cover costs to the association for the change in ownership.

2. Charges for Association Expenses Relating to Preparation of Required Resale Certificates

Many states require (and CAI strongly supports) prior disclosure of material information to a purchaser regarding their personal rights and responsibilities with regard to ownership of property in a community association. CAI believes such prior disclosure is fundamental to a purchaser making a fully informed decision based on essential information relating to their new home as well as the governing community association. Prior disclosure ensures the purchaser is fully aware of all obligations with respect to the property before transfer occurs.

[19] 15 U.S.C. 1601

According to CAI's public policy, *Disclosure Before Sales in Community Associations*, CAI supports state law requiring disclosure of:

- pertinent financial information describing the financial condition of the association
- the projected amount of common expense assessments
- the projected amount of approved special assessments
- association governing documents, including bylaws, declarations and deeds, as may be required by statute
- pending legal action or outstanding judgments
- fees pertaining to transfer of ownership
- a statement of remedies at the association's disposal to collect delinquent assessments and association collection policies
- list of association amenities

While it is the duty of a seller to provide a purchaser the information contained in a resale disclosure package, in practice, associations prepare the required disclosures on behalf of the seller. Given the expenses and legal liability associations incur as a result of preparing resale disclosures, associations routinely charge a fee to sellers requesting a resale disclosure package.

3. Community Transfer Fees

CAI's members urge the Board to clarify that community transfer fees paid at closing should be excluded in the calculation of points and fees. Community transfer fees directly benefit encumbered properties and directly support association activities, association reserve funds, and maintenance of common elements. As community transfer fee proceeds provide a direct benefit to the purchaser, the fees are *bona fide* and should fall within the exemption provided by statute and by the Board's proposal. CAI's members will strongly oppose any effort by the Board to classify community transfer fees as falling outside the scope of the points and fees exemption as a secondary means to regulate or limit the use of this critical funding mechanism for community associations.

Conclusion

The community association model of housing has become more widespread and popular over the past several decades. Approximately 1 out of every 5 American households is located in a community association, which represents almost 60 million American families. While the marketplace and consumers have embraced this model of housing, federal financial regulators and federal housing-related agencies have failed to recognize community associations in the regulatory framework. This has led to confusion as new federal regulatory requirements are pushed into the market, having a detrimental effect on homeownership in community associations.

CAI's members urge the Board to solicit information on community association law and practices going forward to ensure that the community association model of housing is not harmed as federal regulations are drafted or revised. Unintended consequences of these efforts will lead to higher association assessments while at the same time unnecessarily restricting access to credit for these homeowners.

To this end, please do not hesitate to contact me or Andrew S. Fortin, Esq., CAI's vice president of government and public affairs, at (703) 720-9220 if we can provide any supplemental information or views on the Board's proposed rule or on any other topics related to community associations.

Sincerely,

Thomas M. Skiba, CAE
Chief Executive Officer

Appendix A

October 1, 2010

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

RE: Proposed Guidance on Private Transfer Fee Covenants: (No. 2010-N-11)

Dear Mr. Pollard:

I am pleased to submit comments on behalf of Community Associations Institute (CAI)[20] regarding the Federal Housing Finance Agency's Proposed Guidance on Private Transfer Fee Covenants published in the *Federal Register* on August 16, 2010. In general, CAI is concerned the proposed guidance published by the agency, if adopted in its current form, will be disruptive to real estate markets across the country, impair the functioning of the secondary mortgage market, create substantial uncertainty at a time when the national economy is struggling to recover from a deep recession, and have a disproportionately negative impact on homeowners in community associations.

I. Unlike Other Private Transfer Fees, Community Transfer Fees Benefit Encumbered Properties.

CAI's members appreciate the time and attention FHFA has devoted to the issue of private transfer fees[21] and recent market innovations that have led to the proliferation of transfer fees that burden properties but offer no benefit to the land or property owner. These fees and the potential securities derived from the income stream they generate are an unreasonable burden on property owners. Additionally, private transfer fees stretch the traditional legal doctrines of servitudes by burdening properties with fees that do not benefit the land. CAI's members support

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[20] CAI is the only national organization dedicated to fostering competent, well-governed community associations that are home to approximately one in every five American households. For nearly 40 years, CAI has been the leader in providing education and resources to the volunteer homeowners who govern community associations and the professionals who support them. CAI's members include community association volunteer leaders, professional managers, community management firms and other professionals and companies that provide products and services to associations.

[21] We define Private Transfer Fees as deed-based fees, whether set forth in a deed, declaration or association bylaws, that is payable to an individual or entity who is not directly engaged in the governance, support, maintenance, enhancement or investment in the property upon which the deed-based fee is levied.

efforts in state legislatures to void or otherwise render unenforceable any private transfer fee or other contract requiring payment to an unrelated third party at a real estate closing, but we object to the inclusion of long-standing and beneficial community transfer fees[22] in such regulations.

In issuing its proposed guidance, however, FHFA has determined community transfer fees are similarly harmful to the interests of property owners, limit the free exercise of private property rights and damage real estate markets. Community transfer fees are an important funding mechanism of common-interest communities and have been widely used for more than 30 years. During this time, community, homeowners, and condominium associations and housing cooperatives have become an important part of the national real estate market and have been embraced by American families. A 2009 survey[23] conducted on behalf of the Foundation for Community Association Research found that nearly 60 million Americans live in a community association and the total value of their homes is $4 trillion. Many of these communities have long-standing community transfer fees that directly benefit the community and individual homeowners through funding of reserves, capital improvement projects and ongoing association obligations.

In response to the proposed regulation issued by the FHFA, Community Associations Institute undertook a survey[24] of our membership to gather data on the use and impact of community transfer fees. The survey represents data collected from 1,254 communities in 40 states, representing 959,295 units in community associations. The data support the following findings:

- 49 percent of responding communities reported having a community transfer fee on units/homes in their communities.

- Nationally, an estimated 11 million residential units have a community transfer fee in place.

- Community transfer fees have existed for more than a generation; more than 40 percent of such fees having been in place for 10 years or more.

- Such fees are collected as either a fixed fee, percentage of sale price or a multiple of association assessments.
  - A fixed fee is typically $500 or less.
  - A percentage of sale fee is typically less than three-quarters of one percent of the sale price of the property.
  - Fees based on a multiple of association assessments are typically the equivalent of two to three months of assessments.

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[22] We define Community Transfer Fees to mean any deed-based fees, whether set forth in a deed, declaration or association bylaws, that is payable to a homeowners, condominium, cooperative, or property owners association, or other entity that is directly engaged in the governance, support, maintenance, enhancement or investment in the property upon which the deed-based fee is levied.

[23] http://www.caionline.org/info/research/Documents/national_research_2009.pdf

[24] *For the Common Good: Use of Community Transfer Fees in Community Associations*, CAI, September 2010. (Attachment A)

- Community transfer fees are disclosed to potential purchasers.

- The existence of such community transfer fees results in the loss of a sale of property in less than 1 percent of reported transactions.

- Such fees are used to support their community association and its residents by 99.2 percent of responding communities.

From a macro-standpoint, one of the primary objectives of community associations is the preservation and enhancement of not only property values for residents, but the property itself. The rules, architectural guidelines and provisions of amenities above and beyond those in non-association communities are all factors that act to support this purpose. Thus, a financially healthy community association benefits its residents by ensuring a higher return on their investment than would be possible in a non-association community. This is not mere speculation, a study undertaken by the Cato Institute found that, "HOAs increase [property] values by at least 5 to 6%."[25] It is also known that such privately enforced rules for community association housing maintenance relieves local government of many of the burdens of code enforcement. If community transfer fees are banned, then local government will have an increased burden at a time they can least afford it. Further, since a recognizable percentage of community associations have low/moderate income housing components, lenders will lose the opportunity to earn valuable CRA credits. Lastly, for new associations, both Fannie Mae and Freddie Mac require their own version of community transfer fees — two months of assessments must be paid to help provide sufficient capital for association finances and association reserves.

If FHFA's proposed guidance is adopted without revision, Fannie Mae, Freddie Mac and the Federal Home Loan Bank System will be prohibited from engaging in any activity that will support the flow of mortgage credit to these neighborhoods. With 49 percent of surveyed community associations reporting a community transfer fee, a potential pool of up to 11 million residential units would not qualify for most, if not all, federally related mortgage products. This will affect the lives of millions of Americans who purchased their homes in good faith, had no participation in the creation of private transfer fees, and would be counter to the substantial effort being undertaken to stabilize real estate markets nationwide and foster economic growth.

II. Community Transfer Fees are Disclosed to Consumers.

Community transfer fees are not a new innovation in the real estate market. Community transfer fees are a common method of community association financing and budgeting. CAI members report that such fees exist in 49 percent of community association documents. Based on our national industry data, up to 11 million housing units are subject to such fees by their community association. In more than 40 percent of these communities, such fees have been in place for 10 or more years.

Federal agencies and state legislatures have acted to require disclosure of any fee or assessment payable to a community association in conjunction with a change of ownership. Within the

[25] *Do Homeowners Associations Raise Property Values? What are Private Governments Worth?*, By Amanda Agan, Alexander Tabarrok, Regulation, Fall 2005, p. 17.

community association markets, CAI members report that such fees are disclosed in nearly all circumstances, with 96 percent of communities indicating that such disclosures are made prior to purchase in their community. Disclosure of deed-based transfer fees are most often the result of state-based regulations that require the disclosure of critical information related to purchases within a condominium, cooperative or homeowners association. The seller usually is obligated to provide this information. These disclosure facts related to community transfer fees are well known to the real estate community.

CAI members report that such regulations account for 40 percent of all disclosures for deed-based transfer fees to potential purchasers. Such consumer disclosures are a critical consumer protection and a public policy goal of CAI and our members.[26] Ironically, our efforts to expand such consumer disclosures are often blocked by the active lobbying efforts of state realtor organizations. Such disclosures provide a purchaser with a full understanding of the costs and the responsibilities of living in a community association. In CAI's experience, such transparency is key to building financially healthy and harmoniously governed communities. Where such disclosures are not a matter of state regulation, disclosures occur through the closing letter, by action of the association, through the professional association manager, or notice by the title company, realtor or escrow agent. Such mechanisms account for non-regulatory methods of disclosure reported by CAI member communities.

Additionally, federal laws already incorporate supplemental consumer protections to those enumerated by states. The Real Estate Settlement Procedures Act (RESPA) contains no less than three disclosure requirements regarding fees payable at a real estate sale closing. Consumer disclosures under RESPA are accomplished (1) by requiring lenders to provide a special information booklet to consumers within three days of a consumer submitting a formal loan application; (2) through enumeration of settlement expenses on the standard HUD-1 Settlement Statement; and (3) by allowing purchasers to obtain and review a completed HUD-1 Settlement Statement one day prior to loan closing.

RESPA requires HUD to publish and lenders to provide to borrowers its *Shopping for your Home Loan: HUD's Settlement Cost Booklet*. This booklet describes the numerous fees attached to real estate purchases and offers practical information so consumers may educate themselves as to their obligations at closing. Included in the special information booklet is a discussion of community association assessments due at closing and an encouragement that all settlement costs be negotiated with the seller to reach agreement on which costs will be paid by the seller, the purchaser or shared.

RESPA requires that all closing costs and transactions associated with a federally-related mortgage be enumerated on the HUD-1 Settlement Statement. The HUD-1 contains specific line items for disclosure of all costs to be paid by the seller or purchaser according to the sales contract agreement governing the closing obligations of the parties. Any community transfer fee will be enumerated on the HUD-1 according to the negotiated sales contract or other negotiated agreement between the parties.

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[26] CAI Public Policy, *Disclosure Before Sale in a Community Association*. (Attachment B)

Finally, RESPA offers consumers the opportunity to review the HUD-1 Settlement Statement one day prior to loan closing. Consumers have the opportunity to waive the right to review a prepared HUD-1 prior to closing, but this is the sole decision of the purchaser, not the lender. Community transfer fees are a negotiable fee which can be paid by any party to a closing or as a shared expense. Purchasers receiving and reviewing a HUD-1 will be able to identify the fee in advance of a closing if the purchaser has not understood their obligations through prior state-mandated disclosures.

III. Community Transfer Fees Do Not Impact Marketability; Rarely Impact Title.

Another concern that FHFA cites as a basis for its draft regulation is that private transfer fees impact both the marketability and title of the properties affected. Such assertions do not hold up when applied to community transfer fees. CAI member communities report that such fees are disclosed at transfers of title, yet they also report that such fees are rarely, if ever, the basis of a lost sale or actions against title.

CAI's member survey reviewed the impact of such fees on properties in community associations. As noted, our survey indicates that community transfer fees apply to approximately half of the 24 million housing units in community associations and have been in place for a generation. Despite the tens of thousands of annual transactions involving such fees, there is little evidence that such fees impact title or marketability of community association properties. In fact, survey data indicates that such fees result in a loss of sale in less than one percent of all transactions.[27] Further, failure to pay such fees rarely results in action by the association. CAI members report that such fees result in commencement of a lien action in only 6 percent of all transactions.[28]

IV. Community Transfer Fees are Proportional.

The draft guidance issued by FHFA specifically notes that "even if such fees are dedicated to homeowner associations, they are not proportional." The data on the levy and use of such fees in the context of community association funding stand in direct conflict with FHFA's statement. Community transfer fees are both proportional and, as noted in section I, such fees are used for the direct benefit of the properties and property owners.

CAI survey data reveals that community transfer fees are levied in one of three methods: a fixed fee, a multiple of monthly assessments or a percentage of sale price of the encumbered property. The most commonly reported fee is a fixed-fee which accounts for 74 percent of all community transfer fees. A multiple of monthly association assessments accounts for 16 percent of community payable fees and approximately 10 percent of such fees are a percentage of sale price of the property. Regardless of the method of assessment, such fees provide value to the purchaser and are proportional to internal measures that are both transparent and equitable.

Community transfer fees that are levied as a multiple of monthly assessments or as a percentage of sale price are on their face proportional to the value received and the ownership interest acquired. The sale price of a home is dictated by market factors such as size, lot, location, condition, local services and the existence of a community association. Thus, because the

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[27] *For the Common Good: Use of Community Transfer Fees in Community Associations*, CAI, September 2010. (Attachment A)

[28] *Ibid.*

purchase price reflects the market value of the property and includes an array of factors weighed by the purchaser, a percentage of sale levy is the most directly proportional mechanism to levy such an assessment. In the case of community transfer fees, such percentages are in nearly always a minor percentage of sale price. In three-quarters of percentage of sale based fees, such fees amount to less than one-half of one percent of the sale price of the property, and, in nearly all cases, such fees are less than or equal to one percent of the sale price[29].

The same analysis applies to such fees when they are levied as a multiple of monthly association assessments. The most typical calculation is a fee equivalent to two to three months of the property's required assessment. Assessments are the mandatory fees that association residents pay to maintain the common elements and amenities of the community association. The level of such fees relates to the size of the community, the scope of the infrastructure supported by the community association and the community's amenities. While such fees may vary in amount, they are assessed based on factors that ensure proportionality to ownership interest. Such factors vary by development and the diversity of units within the community association. Condominiums typically calculate monthly assessments based on the square footage of each unit. Square foot calculations are also the basis of assessments in many townhome and single family home communities. In these types of developments, square footage may be augmented by factors such as lot size and location. The common element to association assessment levels is that the amount is related to the same market factors that determine price.

Even in a fixed-fee scenario, such fees are proportionate when viewed as a levy on purchasers into the community, as such payment is required for all buyers into the community. Additionally, benefits of a fixed fee flow back to the property owner in two ways that provide additional proportionality. First, such fees offset the need to raise mandatory monthly assessments and delay or serve to minimize the amount of any special assessment required by the community. As such fees are generally levied based on size or ownership interest, the benefit of a fixed fee payment accrues a proportional benefit to all owners. Second, the maintenance of the association finances ensures that all owners benefit from the five to six percentage value-premium on properties within a community association when they sell their property.

V. Amending Deed Restrictions is Burdensome and Success is Uncommon.

CAI believes FHFA's proposed guidance will devastate community associations because of the nature of deed-restrictions and the significant barriers to modifying them. It is a long-standing and broadly accepted principle of community associations to require an affirmative vote of at least two-thirds of property owners to modify a deed- or covenant-based restriction; many communities require written consent from seventy-five percent of property owners (or in some instances, unanimous written consent) to modify deed- or covenant-based restrictions. This practice has been actively encouraged by the U.S. Department of Housing and Urban Development in *HUD Handbook 4140.2 Land Planning Procedures and Data for Insurance for Home Mortgage Programs* in sample governing documents provided for planned unit developments.[30] Further, in some instances where the covenant imposing the deed-based fee

[29] *Ibid.*
[30] HUD Handbook 4140.2: Appendix 2 — Article VI: General Provisions, Section 3: Amendment.

preceded the recording of the declaration, the owners have no authority to amend any pre-existing covenants.

Given the exceptionally high threshold of property owner participation required to modify a community association's deed restrictions, the practice is not commonly undertaken and, when attempted, success is rare. The logistics of contacting all property owners in a community association to obtain written consent to modify the association's governing documents is frustrated by numerous factors. Participation of property owners that reside in the association is not guaranteed even despite repeated entreaties for local property owners to do so. Many owners may not reside in the association, having purchased investment properties or relocated for any number of reasons — personal or professional. This is not to suggest the task is impossible; however, the process can be expensive, time consuming and, even if pursued with the utmost urgency and vigor, is not assured of success. The sale and purchase of homes in affected communities will cease as associations struggle to remove offending deed restrictions, placing a hold on the lives of families and causing economic disruptions.

The difficulties discussed above enumerate some of the obstacles facing associations attempting to revise deeds in a normal housing market. The real estate and economic crises compound these problems. Home abandonment by owners owing more on their mortgage than their property's value is a significant issue in certain real estate markets. An association cannot be reasonably expected to identify the location of owners who have vacated their property and are no longer meeting their general obligations to the association.

An additional significant challenge in the current real estate market relates to the foreclosure process and bank owned properties. As the housing crisis has deepened and foreclosures increased, from a practical standpoint, it is impossible for an association to identify a growing set of property owners: lenders. The chief difficulty for associations is the refusal of lenders to record a change in title promptly after a foreclosure has been completed. Lenders across the nation are refusing to notify local governments and community associations of their ownership interest in properties. In a recent survey, more than 61 percent of CAI members reported lender ownership of properties in their communities. Of this number, more than 66 percent reported that lenders were not living up to their obligations to fund association operations. Lenders clearly do not view participation in association matters to be important and are blatantly ignoring their obligations to other homeowners. It is unreasonable to expect that a lender that refuses to pay monthly assessments or that has intentionally failed to take ownership of a property after a foreclosure has been completed will exercise its voting rights in any association matter.

That these conditions may be an anomaly persisting in the real estate market for the medium-term will make no difference to property owners with unmarketable properties if FHFA's proposed guidance is adopted without revision. A careful examination of community association governance shows the removal of deed-based restrictions is exceptionally difficult under normal conditions and in the existing environment even more so. As a result, FHFA's proposed guidance will severely impair the marketability of millions of homes; substantially disrupt housing markets and negatively impact the financial standing and future of millions of American families.

Of additional concern to CAI is the lack of a defined meaning of "private transfer fees." In the literature cited in these comments and in documents used by proponents of bans on private transfer fees, such terminology is applied only to such fees that are payable to third party investors outside of a community. CAI believes that confusing private transfer fees with community transfer fees would have a negative impact on the millions of properties that currently use this funding mechanism. The lack of clearly defined terminology could also expand the rule's application to even more properties.

In a community association context, a deed-based fee regulation might be applicable to a host of requirements in different recorded documents. Such a regulation would clearly apply to any transfer fee recorded in individual deeds, as well as recorded community declarations. It may also be applicable, in some cases, to bylaws adopted by condominium associations, which are recorded in some jurisdictions and are considered to run with the land.

The target of private transfer fee critics and the primary concerns expressed by FHFA are deed-based transfer fees that flow to parties that are not directly affiliated with the operation, management or governance of the communities. This is consistent with both state regulations on the matter and recognized legal principles dealing with deed restrictions. Clearly defining private transfer fees as deed restrictions, payable at time of sale to third party investors or otherwise distinguishing between such investor fees and community transfer fees, will ensure greater clarity of application and work to minimize the negative impact of any regulation on the property market as a whole.

VI. FHFA's Proposed Guidance is Inconsistent with State Regulation.

While FHFA fails to draw any distinction between transfer fees that provide a direct benefit to the land and association in question and those transfer fees that offer no benefit to the land, state legislatures have elected to take a different path. Indeed, the regulation of real estate markets is largely under the purview of the states and is governed by well-established precedent and practice. Many states have chosen to limit third party transfer fees or to put in place a significant consumer disclosure requirement prior to closing if the property in question is encumbered by a deed-based transfer fee.

CAI's research finds that 17 states currently regulate private transfer fees, and there is legislation under active discussion in at least three more states.[31] At least 12 of these states have specific statutory exemptions for fees payable to a community association. In the three states contemplating such regulation, fees payable to a community association are also not subject to enacted legislative bans. Each regulated state excludes fees payable to community associations from the definition of private transfer fee and application of transfer fee bans. At the federal level, legislation has also been introduced which would statutorily ban private transfer fees payable to third party investors, but continue to allow such fees when payable to community associations. Collectively, these approaches reflect legislative findings that community transfer fees benefit homeowners and the underlying property — a relationship that does not exist in the fees payable to third party investors.

[31] This list includes Colorado, Georgia and Pennsylvania.

The effect on homeowners of these actions by state legislatures is substantially different than the potential effect on homeowners if FHFA adopts its proposed guidelines as written. States have rendered deed-based transfer fees unenforceable. However, FHFA does not possess the legal authority to void private contracts between unrelated third parties. Thus, if implemented, the regulation would, through lending restrictions, negatively impact properties in states that have already taken decisive action to curb abusive private transfer fees and distinguish beneficial community transfer fees, an outcome contrary to FHFA's goals.

VII. FHFA Should Follow Law of Servitude Precedent and Differentiate Between Servitudes that Touch and Concern the Land.

The current principles of deed restrictions arise from a centuries-long debate as to what extent such restrictions can impose limitations on the use of land by successive owners. An analysis of the treatment of such restrictions ends in the long-recognized principle often cited as the "Touch and Concern Doctrine" or the "Benefit v. Burden Analysis." Although this standard has been loosened in recent years, under both traditional and more recent interpretations of servitudes, community transfer fees have a sound basis in public policy and law that supports their exclusion from FHFA's proposed guidance on this matter.

CAI can find no better argument for this position than a recent discussion of these principles in the American Bar Association's *Probate and Property* magazine.[32] In his article titled *Putting the Breaks on Private Transfer Fee Covenants*, author R. Wilson Freyermuth concisely and effectively lays out the difference between community transfer fees and private transfer fees:

> "The best example [of touch and concern doctrine] is the typical owners association assessment covenant, which imposes an assessment on each lot payable to an owners association and the maintenance of common facilities. These assessments benefit community residents directly (for example, by providing access to pools or parks) or indirectly (such as by preserving/raising property values because of the presence of valued amenities). Ever since the landmark *Neponsit* case, courts have held that both the burden and the benefit of a lot assessment covenant 'touch and concern' land and bind successor owners of that land."[33]

Under the traditional principles of servitudes and existing case law, community transfer fees meet the legal requirement of benefiting the encumbered property and its owners. FHFA should not override this longstanding principle by regulatory fiat. Such analysis stands, even under the more recent, broader restatement interpretation of deed restrictions, which allows deed restrictions, provided they are not unconscionable, arbitrary, or an unreasonable restraint on alienation or competition.[34]

Private transfer fees, as opposed to community transfer fees, do not pass this standard as they are not transparent to consumers, they unreasonably hinder alienability of property and they benefit private parties. Community transfer fees on the other hand, as discussed in these comments, are

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[32] *Putting the Brakes on Private Transfer Fee Covenants,* By Wilson Freyermuth, Probate and Property, July/August 2010, page 21.
[33] Ibid., p. 22.
[34] Restatement (Third) of Property — Servitudes, Section 3.1(1), (3)-(5)(2000).

demonstrably disclosed, do not hinder alienability of property and benefit not a select group of private individuals, but all property owners in the community.

VIII. FHFA's Proposed Guidance will be Disruptive to Efficient Market Operations.

Setting aside CAI's concerns about the negative impact the proposed guidance will have on property owners, CAI is also concerned that using guidance as a mechanism to eliminate private transfer fees from the real estate market will cause numerous disruptions for loan originators and secondary market participants. As previously discussed, FHFA does not have the legal authority to vitiate deed restrictions or covenants that run on privately owned property. This may only be accomplished by an Act of a state legislature or Congress, a legal determination that such restrictions are unenforceable by a court of law, a ruling by a competent federal government agency that such restrictions violate existing federal statute, or by agreement of the contracted parties. The approach taken by FHFA to cure its lack of legal authority to set aside private transfer fees is to force all market participants to alter long-standing business practices and market operations at all levels of the mortgage finance and real estate industries. Unfortunately, given the wide-spread, long-standing use of private transfer fee convenants in accordance with applicable law and precedent, FHFA's actions will cause the greatest amount of disruption to loan originations and secondary market operations.

From the practical standpoint of a consumer seeking to obtain financing to purchase a home, FHFA's proposed guidance will substantially impair a purchaser's and seller's reliance on a lender mortgage pre-approval when agreeing to a sales contract. Given the number of community associations and the wide-spread use of community transfer fees, numerous contracts signed on the basis of a purchaser's pre-approval will be voided. The sales contract will not be voided due to defects in the physical condition of the home, its potential location in a flood zone, the inability to show a clear title to the property or any other traditional underwriting requirement. Rather, the contract will be set aside due to a decision taken by FHFA that all private transfer fee covenants jeopardize the safety, soundness and prudential operation of the government-sponsored enterprises. This notwithstanding the fact that community transfer fees have been in common use for at least 30 years and have not been cited as a causal factor for the collapse of the nation's housing market. Sales contracts will be subject to cancellation not due to a borrower's impaired credit or any impairment to the property in question; sales contracts will be cancelled due solely to FHFA's purchasing guidance to the GSEs.

Real estate closings will be subject to additional last minute cancellations if FHFA's rule is adopted without revision. As lenders complete the loan underwriting process in the days leading up to closing, borrowers will be notified that, while they are financially qualified for credit, the lender will not fund a mortgage on the property because there will be no secondary market for the loan. The withdrawal of mortgage financing by lenders in advance of closing due to a lack of a secondary market for mortgages secured by real property in a community association will cause substantial disruption to real estate markets across the nation.

FHFA's proposed guidance will have an impact on the operations of the GSEs as well. As currently drafted, the proposed governance will prohibit the enterprises and bank system from purchasing or investing "in any mortgages encumbered by private transfer fee covenants or

securities backed by such mortgages." The guidance further states, "The Banks should not purchase or invest in such mortgages or securities or hold them as collateral for advances." This raises substantial questions for the day-to-day business operations of the enterprises and the bank system relative to the quality of assets currently held in portfolio and of any mortgage backed securities issued by the enterprises. Will FHFA's determination that the presence of such mortgages in the pools supporting mortgage backed securities create a legal obligation on the enterprises to cure these pools or create an obligation for a lender to repurchase any offending loans? Will the presence of such mortgages affect any credit rating attached to the securities or affect accounting or other legal obligations of the owners of securities issued by the enterprises that contain impaired mortgages? Will the enterprises be required to review all mortgages held in their respective retained portfolios to determine which mortgages are encumbered by a private transfer fee covenant and therefore must be divested? If so, will there even be a market for such loans that FHFA has determined to be unsafe and unsound?

The Federal Home Loan Banks will experience similar disruption in their day-to-day operations. Will each bank be required to conduct a review of collateral or investments to determine if any of these assets are encumbered by a private transfer fee covenant? If so, will the Bank be able to sell any impaired investments and will the member banks posting the impaired collateral be able to offer replacement collateral? A further subject for consideration is the impact of FHFA's proposed guidance on the bank system's individual members. Many community banks use advances from the bank system to meet regular funding needs. What will be the impact on these banks now that a portion of assets that were available to post as collateral for advances are no longer accepted?

CAI believes FHFA should give additional thought to and be concerned about the impact of the proposed guidance on other participants in the mortgage origination process and in the secondary market. These important questions must be given serious consideration and be subject to meaningful deliberation if unintended consequences are to be avoided. CAI strongly believes it is acutely possible that unintended consequences of FHFA's proposed guidance will reach beyond property owners in community associations and into the operations of lenders and the secondary market.

IX. Recommendations for Revisions to Proposed Guidance.

As noted, CAI believes that the development of private transfer fees that are payable to third party investors outside of the community are problematic and deserve regulatory scrutiny. We believe that these fees are at fundamental odds with standing legal principles, state legislative findings and the development of financially sound, equitably governed communities. For these reasons, Community Associations Institute recommends the following:

CAI recommends that the FHFA rescind the rule as drafted.

The FHFA rule does nothing to address private transfer fees directly; such fees would still exist if the rule were to be enacted. Thus, the regulation offers no protection for consumers and, at best, negligible protection for the secondary mortgage market entities regulated by FHFA. The regulation as drafted would, however, create a pool of up to 11 million housing units that would

be unmarketable because FHFA would block these properties from access to nearly all federally related mortgages.

FHFA should respect current state regulatory and legal paradigms that distinguish between community transfer fees and private transfer fees.

Community transfer fees have long played a vital role in supporting infrastructure, amenities and operations within a community association. Such fees follow recognized legal principles of benefiting the properties affected, and the resulting revenue is an important part of financing for half of all community associations. The role of community transfer fees is not only supported by traditional legal principles, but also recognized by the more than 17 states that regulate private transfer fees. These states rightfully separate community transfer fees from private transfer fees. FHFA should do so as well.

In its current form, the proposed FHFA regulation would serve to undermine existing state regulatory efforts. Because state efforts regarding private transfer fees typically invalidate enforcement and do not remove the language from individual deeds, any encumbered property would still be subject to the FHFA regulation and be redlined from mortgage financing.

State legislative and Federal efforts should be allowed to continue prior to FHFA intervention.

CAI believes that private transfer fees that benefit third party investors outside of community associations should be banned. However, FHFA does not have the statutory authority to accomplish this task. FHFA's regulatory authority can direct and dictate the flow of funds through the mortgage finance system by stating a class of loans and properties are "off limits" to underwriters, but doing so in the manner proposed would be catastrophic for the reasons outlined in this document. Further, it would place the burden of rectifying the troubling use of deed restrictions for private investor gain on the backs of consumers, who would be left with the arduous and likely futile task of amending or rescinding current deed restrictions. As such, CAI recommends that FHFA withhold any additional action on the regulation to provide time for state and federal legislative efforts on this issue to run their course.

Any FHFA action on such fees should be prospective and limited in scope.

CAI believes that FHFA regulatory authority would be best applied by allowing state efforts to continue for a set period of time. All fifty states hold legislative sessions in 2011. States should be provided with the appropriate time to distinguish between appropriate fees, such as community transfer fees and fees that are against the interest of consumers such as private transfer fees payable to investors. This effort is being facilitated by leading advocates against private transfer fees. Such efforts provide the best chance for curbing this practice while providing protection for consumers in properties with such fees in place. FHFA may then choose, after a set period of time, to draw a regulatory line in the sand and impose a funding ban for any private transfer fees payable to third party investors that are recorded after a specific date. Through this approach, FHFA actions would have the maximum impact on abuse of such fees with the minimal impact on consumers.

We look forward to your response and to working with the FHFA to better understand the critical role of such fees on community associations, the need to distinguish community transfer fees from private transfer fees and to take action that is appropriate to provide the greatest consumer protection while minimizing negative impacts on the overall housing market.

Sincerely,

Thomas M. Skiba, CAE
Chief Executive Officer

Attachment A (to Appendix A)

DISCLOSURE BEFORE SALES IN COMMUNITY ASSOCIATIONS

Policy

CAI believes that homeowners should be informed about association matters that may impact their decision to purchase a home/unit and will educate them about their personal rights and responsibilities with regard to the community association. Disclosure documents/resale certificates are invaluable consumer information tools because it is vital that buyers know what they are buying. Disclosure documents/resale certificates should be mandated by state statute to ensure that every buyer is aware of essential information relating to his new home or unit and the community association.

CAI supports mandating disclosure documents/resale certificates for all ownership transfers of homes or units in a community association to ensure that the association is notified of every pending sale and that the transferee is aware of the obligations with respect to the property

It is the Public Policy of CAI that state legislatures should mandate disclosure to potential buyers of homes or units in community associations by providing copies of the following information:

1) ***Amount of current monthly assessments, maintenance fees and other charges for common expenses;***
2) ***Amount of approved special assessments;***
3) ***Association governing documents;***
4) ***Amount of reserve and capital funds available and committed to current or pending projects;***
5) ***Reserve study, if any;***
6) ***Current operating and reserve budgets and year-to-date financial statement;***
7) ***Insurance certificates indicating association-provided coverage;***
8) ***Pending litigation excluding routine assessment collections;***
9) ***Outstanding judgments against the association;***
10) ***Any amounts the current owner owes the association;***
11) ***Notice of any association alleged and uncured violation pertaining to the home/unit;***
12) ***Fees relating to the transfer of ownership or other transactions;***
13) ***A statement of the remedies available to the association as a result of non-payment;***
14) ***Current collection policy;***
15) ***Notice of any restrictions related to the leasing of a unit;***
16) ***List of association amenities;***
17) ***Contact information for the association;***

CAI recognizes that the preparer of the disclosure documents/resale certificates incurs expenses relating to the preparation and production of such documents and supports the right of the preparer to charge a reasonable fee for such transactions.

Background

The Community Associations Institute (CAI) recognizes that buying a home or unit in a condominium, cooperative or planned unit development should be a positive event, but can be a stressful and confusing time for the buyer.

CAI believes that full disclosure is an essential tool to ensure that the consumer is aware of all relevant data that may impact the decision to purchase a home or unit in the community association. Resale certificates will also educate the consumer about rights and obligations as an owner of a home or unit in a community association.

Additionally, while community associations are obligated to maintain a roster of current owners, it is often impossible to track sales because of the voluntary nature of resale certificates**.** The association may not be aware that a new owner has taken possession of a home or unit until months or perhaps years later. Mandating the submission of resale certificates will enable associations to be alerted to ownership changes in a timely manner.

Frequently an association's management company serves to fulfill the requests for document production related to the sale of a property. Such requests may come several months in advance or with short notice. Preparers incur labor and material costs for such production and must attest to the accuracy of the information. As such, preparers should be allowed to charge a reasonable fee for the liability risk incurred by affirming the correctness of the information as well as the preparation and production of disclosure documents/resale certificates. Although most disclosures are of a routine nature, there may be transactions or circumstances that justify additional charges. Such fees, at the discretion of the association or its agent, may be required in advance of production to ensure costs incurred to the association are properly allocated to the parties to the transaction and in a timely manner. If the resale package is demanded without reasonable notice, an expedited charge may be warranted.

Adopted by the Board of Trustees, March 3, 2010.

Attachment B (to Appendix A)

For the Common Good:
Use of Community Transfer Fees by Community Associations

September 27, 2010

community
ASSOCIATIONS INSTITUTE
Department of Government & Public Affairs
225 Reinekers Lane, Suite 300
Alexandria, VA 22314
(703) 548-8600
www.caionline.org

Background

On August 13, 2010, the Federal Housing Finance Agency (FHFA) issued a draft regulation addressing the issue of "Private Transfer Fees." The proposal would prohibit Fannie Mae, Freddie Mac and federal home loan banks from purchasing mortgages for any property that contained a "deed-based transfer fee" payable at time of sale. Regulatory interest in this matter was driven by the advent of investment vehicles that relied on deed-based transfer fees that require payment to parties outside of the community in which the deed is recorded at the time of transfer — a fee often referred to as a "Private Transfer Fee." In its draft language, FHFA chose to apply the regulation banning mortgage funding to any property with any deed-based transfer fees, including fees payable to community associations.

In their justification for the proposed regulation, it was noted that "FHFA is concerned that the fees fund purely private streams of income for select market participants and do not benefit homeowners." The FHFA went on to note, "even if the fees are dedicated to homeowners associations, they are not proportional or related to the purposes for which the fees are collected." FHFA offered no study or data to justify this position.

In response to these FHFA "findings," CAI surveyed its membership to gather data on the nature, use and benefits of deed-based transfer fees in community associations across the country. The goal of the survey was to provide empirical evidence that demonstrates how "Community Transfer Fees[35]" are used and benefit homeowners in community associations across the country. This report is the product of that survey.

Community Associations Institute (CAI) is a membership organization representing the interests of the more than 60 million Americans who live in community associations. Our 30,000 members represent volunteer board members of associations, managers of community associations and businesses that support community associations across the country. CAI members work to promote harmonious and vibrant communities through our national organization and our more than 60 chapters across the country.

[35] "Community Transfer Fee" is used to refer to a deed-based fee payable to a community association or affiliated entity where the funds collected are used to benefit the properties paying such fees.

Survey Process

CAI's Transfer Fee Survey contained 19 questions on the topic of transfer fees within community associations. The survey was sent electronically to all CAI members.[36]

To ensure data from individual respondents was not duplicated, the survey captured the names, addresses and communities responding to the survey; 99% of the respondents provided this data. When this data was not provided, the responses were not included in the calculations published in this report.

As the terms "private transfer fee" or "deed-based transfer fee" are not clearly defined legal terms, the questions were structured to ensure that respondents provided accurate data on deed-based fees rather than any other fees that may be charged at the time of transfer. CAI data on deed-based transfer fees reflects deed-based fees payable to the community association or community association based entity, not to outside third party investors.[37]

The survey was open from August 31 to September 17, 2010. A total of 1,254 communities, representing 959,295 housing units, responded to the survey.

Although this survey did not use a random sample of communities, CAI believes that the number of communities responding and the geographic diversity of such responses provide data that may be used as the basis to provide accurate estimates for the uses of deed-based transfer fees throughout the national community association universe. This report shall distinguish between summaries of the actual data and national estimates based on such data[38].

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[36] CAI's survey was sent electronically to 21,521 individual members. This number varies from our total membership number due to members opting out of e-mail communication as prescribed by the "CAN-SPAM Act." As of July 31, 2010, CAI had 30,100 individual members.

[37] "Private Transfer Fee" and "Deed-Based Transfer Fee" are not clearly defined legal terms. For purposes of this survey, CAI considered any transfer fee payable to a community association and found in a master deed, individual property deed, declaration or bylaw to be a "Deed-Based Transfer Fee." Each of these documents may be considered to run with the land and bind future purchasers. In some jurisdictions, association bylaws are recorded and are considered to run with the land.

[38] Unless otherwise noted, all results in this report refer to the respondents who indicated that their community has Community Transfer Fees.

Survey Highlights

- CAI's Community Transfer Fee Survey represents data collected from 1,254 communities in 40 states, representing 959,295 units in community associations.

- Community transfer fees on units/homes in their communities were reported by 49 percent of responding communities.

- Community Transfer Fees have existed for more than a generation. More than 40 percent of such fees having been in place for 10 years or more.

- A community-payable, deed-based transfer fee attached to their property was identified by 489,198 units responding to the survey.

- At least two-thirds of all property owners would be required to remove fee provisions by 70 percent of communities with Community Transfer Fees.

- Such fees are collected as either a fixed fee, percentage of sale price or a multiple of association assessments.

- When a Community Transfer Fee is a fixed fee, it is typically $500 or less.

- When a Community Transfer Fee is a percentage of the sale price, it is typically less than three-quarters of one percent of the sale price of the property.

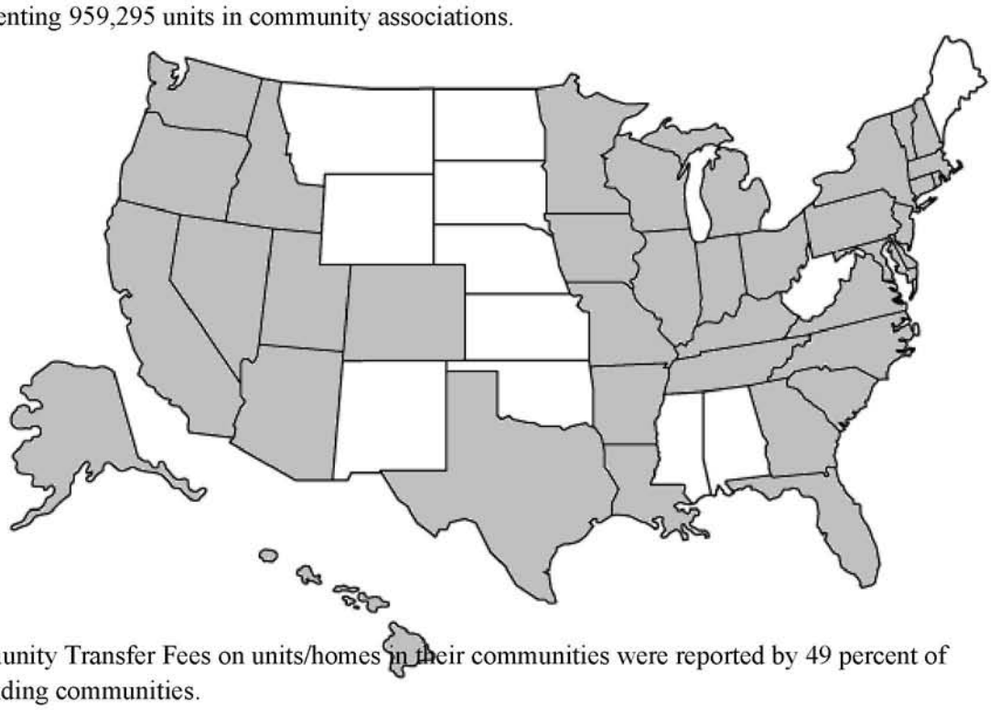
- Community Transfer Fees are disclosed to potential purchasers in nearly all circumstances.

- The existence of such fees results in the loss of a sale of property in less than 1 percent of reported transactions.

- Such fees are used to support the community association and residents by 99.2 percent of responding communities.

Survey Findings

CAI's Community Transfer Fee Survey represents data collected from 1,254 communities in 40 states, representing 959,295 units in community associations.



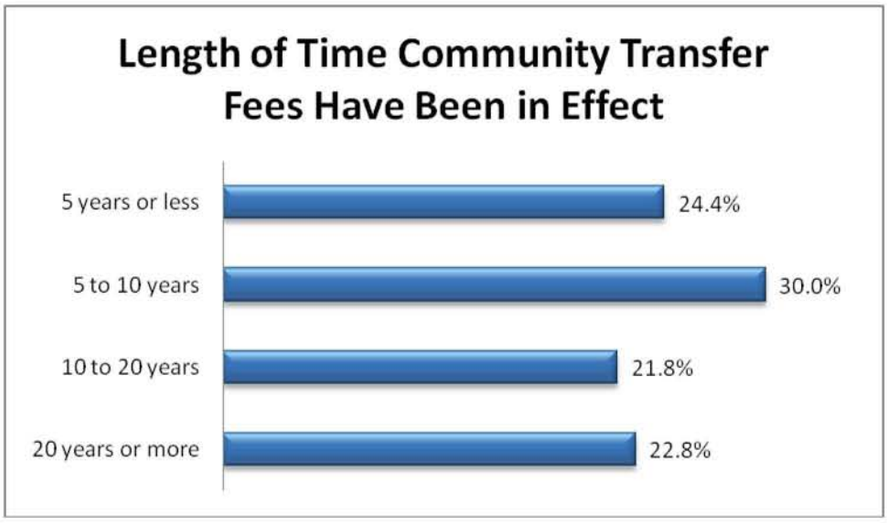
Community Transfer Fees on units/homes in their communities were reported by 49 percent of responding communities.

A Community Transfer Fee attached to their property was identified by 489,198 units responding to the survey.

Action Required to Remove a Community Transfer Fee[39]	
Unanimous Approval	. 3%
Super-majority of two-thirds or more property owners	67%
Super-majority of a quorum of members at a membership meeting	30%

[39] Actions to remove deed restrictions, super-majority or quorums require the participation of all property owners, including bank-owned properties.

Community Transfer Fees apply to the initial and all subsequent sales of the property for 90 percent of respondents.

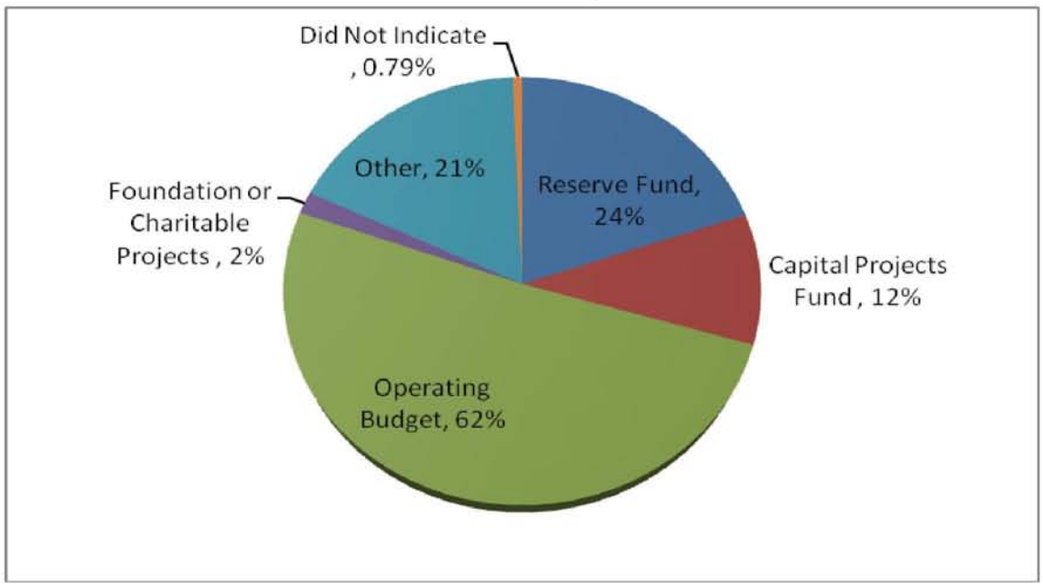


Community Transfer Fees are levied as follows:

1. Fixed fee — 74%.
    - $100 or less — 23%
    - $100 to $250 — 33%
    - $250 to $500 — 22%
    - $500 to $750 — 5%
    - "Other[40]" — 16%
2. A percentage of sale price — 9%.
    - One-quarter of a percent or less — 35%
    - One-quarter of a percent to one-half of a percent — 36%
    - One-half of a percent to three-quarters of a percent — 12%
    - Three-quarters of a percent to 1 percent — 16%
3. Multiple of monthly association assessments — 17%.
    Typically 2 to 3 months of the association assessment.

[40] The response of "other" indicates communities that have a fixed fee that varies depending on the type of unit within the community, e.g., $250 for a townhome and $350 for a single family home.

How are funds from Community Transfer Fees used?



"Other" includes communities who allocate funds to reserves, capital projects *and* operating expenses.

Of communities with Community Transfer Fees, 60 percent report that they would have to increase assessments to recover revenue lost if their ability to collect such fees was prohibited.[41]

Community Transfer Fees are disclosed to purchasers prior to closing by 96.3% of responding communities. Disclosure is accomplished through state disclosure laws, closing letters, action of the association or its agents, notice by the title company, realtor or escrow agent

Community associations with Community Transfer Fees report that such fees result in a loss of sale in less than 1 percent of all transactions.[42]

Failure to pay a community payable, deed-based transfer fee results in the association seeking a lien in 6 percent of reported cases.[43]

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[41] An important distinction with the proposed FHFA regulation is that it does NOT ban such fees; however, it renders properties encumbered with any deed-based fee unqualified for 90 percent of available mortgages. Thus, the impact on a community with such fees would be far more devastating than an increase in assessments.

[42] This figure represents the data as reported to CAI. Associations may not be party to reasons for the cancelation of an individual home sale. As this is an issue raised by the National Association of Realtors, we anticipate their data may supplement our members' reports on the impact of such fees on home sales in community associations.

[43] This figure does not measure if a lien was filed, only if the association began the lien process. American Land Title Association may be able to provide claims experience as to the number of instances where such fees, regardless of beneficiary, have resulted in action against title.

Application of Survey Findings to National Community Association Data[44]

Up to 11 million homes have a Community Transfer Fee in place.

Nearly 45 percent of homes have had a Community Transfer Fee in place for 10 or more years.

Such fees generate up to $3 billion annually to fund community association projects, reserves or otherwise benefit community association residents.

Approximately 7.7 million homes with Community Transfer Fees would require two-thirds or greater consent of all property owners to remove such fees.[45]

The approximate value of all homes with Community Transfer Fees is $1.2 trillion.

[44] CAI industry data is available at http://www.caionline.org/info/research/Pages/default.aspx.
[45] Based on industry practice, obtaining a two-thirds or greater approval of all property owners for deed changes is extremely rare, thus, the proposed regulation issued by FHFA would render many of these homes unmarketable.

Appendix B

March 30, 2011

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

RE: RIN 2590-AA41

Dear Mr. Pollard:

On behalf of the Community Associations Institute[46] (CAI), I am pleased to submit the following comments regarding the Federal Housing Finance Agency's (Agency) proposed rule concerning private transfer fees.

CAI Urges Elimination of Private Transfer Fees Paid to Unrelated Third Parties
In its proposed rule, the Agency prohibits the government sponsored enterprises (GSEs) from purchasing mortgages secured by properties encumbered by certain private transfer fee covenants and from selling or investing in securities backed by such mortgages. CAI supports the Agency's proposed prohibition on private transfer fees paid to unrelated third parties.

Transfer fees paid to unrelated third parties do not benefit the encumbered properties and violate the traditional standard that any covenant that burdens a parcel of land and purports to run with the land must also touch and concern the land. CAI concurs with the Agency's determination that the purpose of third party transfer fees is solely to create a stream of income for parties that do not have an interest in the land.

CAI Supports Finding that Community Transfer Fees Provide Direct Benefit
CAI is pleased the Agency agrees with the preponderance of legal opinion that community transfer fees[47] benefit the land and homeowners. It has long been recognized that community

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[46] CAI is the only national organization dedicated to fostering competent, well-governed community associations that are home to approximately one in every five American households. For nearly 40 years, CAI has been the leader in providing education and resources to the volunteer homeowners who govern community associations and the professionals who support them. CAI's 30,000 members include community association volunteer leaders, professional managers, community management firms, and other professionals and companies that provide products and services to community associations.

[47] CAI defines the term 'community transfer fee' to mean a covenant, including a deed-based fee, whether set forth in a deed, declaration or association bylaws, that is payable to a community association or other entity that is directly engaged in the governance, support, maintenance, enhancement or investment in the common interest community of which the mortgaged lot, home or unit is a part.

transfer fees provide a direct benefit by allowing residents to fund their community association's[48] operations and services.

Community associations allow homeowners to protect and enhance the value of their homes and to gain access to additional benefits they would not otherwise be able to enjoy. To accomplish these purposes, community transfer fees are used by residents for association governance, maintaining common property, providing amenities, supporting reserve funds, and for management of these activities and services. Residents and their land benefit from each of these (and other) services and activities provided by their community association.

The use of community transfer fees is merely an additional method by which residents raise revenue and reinvest in their community. Community associations empower residents to protect and improve their neighborhoods, which increases their use and enjoyment of their land. This empowerment of residents is why the community association model of neighborhood governance has been embraced by homeowners, municipalities, and organizations that advise State and local governments on land use and planning decisions.

The rights of residents to govern, maintain, and enhance their communities through the use of community transfer fees has been validated and preserved by courts and State legislatures across the country. CAI strongly supports the Agency's decision to adhere to established jurisprudence and State statute, which find that community transfer fees touch and concern the land, providing a direct benefit to the owners and residents of that land.

CAI Supports Finding that 501(c)(3) & (c)(4) Groups May Provide Direct Benefit

CAI supports the Agency's finding that properties may benefit when community transfer fees are used to support the activities of certain tax-exempt organizations. Across the country community associations work with tax exempt organizations to provide valuable services for residents. In many cases, the services of these tax-exempt organizations are a key component in the decision-making process as individuals and families consider the purchase of a home.

Preservation of open space for environmental, land management, and recreational purposes are important goals for the homeowners who seek out common interest communities[49] with community associations supporting these activities. Other homeowners seek out common interest communities that actively support cultural and other social opportunities for residents.

This aspect of common interest communities helps focus the housing market on the interests and needs of homeowners. This, in turn, ensures that homeowners have the greatest choice of housing options and promotes the greatest enjoyment of their home and neighborhood.

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[48] There are three types of community associations: homeowners, cooperatives, and condominium associations.

[49] The term 'common interest community' is defined in the Uniform Common Interest Ownership Act and describes the legal relationship of an owner to their community association, irrespective of the form of property ownership or construction.

CAI believes the Agency has adopted the appropriate standard to determine if community transfer fees may support the activities of a 501(c)(3) or (c)(4) organization, which is that the activities of the organization must touch and concern the land. This traditional understanding of servitudes is widely accepted by State courts as valid and CAI supports the Agency's recognition of this legal standard.

CAI Supports Prospective Application of the Final Rule

The Agency proposes to apply any final rule regarding private transfer fee covenants prospectively. CAI strongly supports this aspect of the proposed rule.

As noted in CAI's comments on the Agency's prior proposed guidance, denying millions of homeowners whose property is subject to a private transfer fee or a community transfer fee access to mortgage credit would devastate families and communities. The GSEs continue to provide vital support to the housing finance system. As private capital has not returned to the housing finance system by any meaningful measure, the GSEs continue to be the primary access point homeowners have to the secondary mortgage market. Protecting this access is crucial for homeowners in common interest communities. Prospective application of a final rule will benefit the market while not harming homeowners.

Recommendations on Definitions

CAI appreciates the thoughtful and careful consideration given by the Agency to the definitions contained in its proposed rule. Given the impact of the proposed definitions on homeowners and their community associations, CAI urges the Agency to consider the following recommendations.

Adjacent or Contiguous Property

The limitation the Agency seeks to place on the use of community transfer fees by community associations through its definition of 'adjacent or contiguous property' could have significant negative impacts on common interest communities. CAI does not believe the Agency's proposed 1,000 yard proximity test is necessary as it does not follow the established touch and concern standard and will negatively affect common interest communities by restricting the future land acquisition and use decisions of residents. CAI strongly believes that residents of common interest communities have a right to purchase, maintain, and govern property through their community association for their common use and enjoyment and to use revenue generated from a community transfer fee for this purpose.

The use of commonly owned property is a driving factor in its location. It can be impractical for common interest communities to locate certain community assets, for example a golf course or a marina, in such close proximity to its property lines as the Agency seeks to require. The result of the Agency's proposed 1,000 yard standard would be to limit the future ability of community associations to acquire land—as directed by residents—for the enjoyment of all residents. This difficulty will also apply to new common interest communities under development. CAI advises

against adopting a definition that restricts a homeowner's choice of community as well as the ability of residents to determine how community assets are supported.

An additional area of concern regarding the use of a proximity test relates to master and sub-associations. In communities with this legal structure, all owners are members of a sub-association and the master association. Owners support the operations of their sub-association as well as the operations of the master association, but do not fund or participate in the governance of other sub-associations. The proximity test in the Agency's definition of 'adjacent or contiguous property' fails to capture this form of common interest community governance. In this instance, it is more likely than not that commonly owned or controlled property of the master association would be located well outside the 1,000 yard proximity limitation envisioned by the Agency for many sub-associations.

CAI respectfully urges that the Agency adopt a standard focused on common ownership and use of a property rather than a property's proximity to a controlling common interest community. A standard focused on common ownership, governance and jurisdiction meets the touch and concern test applied by State courts and is in agreement with the Agency's determination that community transfer fees that touch and concern the land provide a direct benefit.

CAI recognizes the Agency is seeking balance in the distance between properties encumbered by a transfer fee and the property that benefits from the fee proceeds. It is, therefore, important for the Agency to consider master associations in its proposed definitions. Regardless of whether the Agency opts to include a proximity test in a final rule, it will be necessary to account for master and sub-associations in any final rule.

Accordingly, CAI offers two recommended modifications to the term 'adjacent or contiguous property'. CAI strongly believes the Agency should adopt Recommendation 1, as it ensures consistent application of the doctrine of touch and concern, respecting established State law and jurisprudence. Recommendation 1 will also remedy the identified issue regarding master and sub-associations.

If the Agency opts to retain the proximity test of 'adjacent and contiguous property', CAI offers Recommendation 2 for the Agency's consideration as this recommendation ensures that master and sub-associations will have the future ability to support commonly owned and controlled property that is in close proximity to the master association with a community transfer fee.

Recommendation 1

> *Community controlled property means property that is commonly owned, governed or subject to the jurisdiction of an association or members of the same common interest community whose property is encumbered by a private transfer fee covenant;*

Recommendation 2

> *Adjacent or contiguous property means property that borders or lies in close proximity to the property that is encumbered by a private transfer fee covenant or to other similarly encumbered properties located in the same community and owned by an association or members of the same common interest community.*

Covered Association

CAI supports the Uniform Common Interest Ownership Act (UCIOA)[50], developed under the auspices of the National Conference of Commissioners on Uniform State Laws. CAI believes that clear, strong, and uniform State laws governing common interest communities benefit homeowners and their community associations by offering consistent legal protections to all parties. UCIOA ensures, where adopted, that homeowners in common interest communities across the country have the same rights, obligations, and protections. This has led to strong industry standards for the establishment, governance, and management of common interest communities. Accordingly, CAI strongly urges the Agency to use terminology in UCIOA to the greatest extent practicable in its final rule.

Rather than the term 'covered association', CAI urges the Agency to adopt the term 'common interest community' as defined in Section 1-103(9) of UCIOA (2008), which is defined, in relevant part, as follows:

> *(9) "Common interest community" means real estate described in a declaration with respect to which a person, by virtue of the person's ownership of a unit, is obligated to pay for a share of real estate taxes, insurance premiums, maintenance, or improvement of, or services, or other expenses related to, common elements, other units, or other real estate described in the declaration...*

Direct Benefit

CAI has identified three areas of concern with the Agency's proposed definition of 'direct benefit' that have the potential to negatively affect common interest communities. CAI's concerns are (1) the definition may prevent community associations from serving the general public; (2) the definition restricts the use of community transfer fees by community associations; and (3) the definition degrades the private property rights of residents of common interest communities by limiting their exclusive right to govern the use of common property or common elements.

Community Association Activities That Exclusively Benefit Encumbered Properties
The Agency's proffered definition of 'direct benefit' is robust with regard to the potential activities of a tax-exempt organization affiliated with a common interest community and CAI supports this portion of the Agency's definition, except for the Agency's use of the word "exclusively". CAI urges the Agency to consider amending the definition of 'direct benefit' to

[50] To view the Uniform Common Interest Ownership Act (2008), click here.

require that activities carried out by such organizations *primarily* benefit encumbered properties rather than requiring that these activities *exclusively* benefit encumbered properties.

By requiring that the activities of the organization exclusively benefit encumbered properties the Agency is placing an unnecessary restriction on the use of private property. Specifically, the inclusion of the word "exclusively" in the definition of 'direct benefit' imposes a restriction on how residents of common interest communities determine the use of commonly owned property. If, for example, community association rules permit non-resident use of property controlled by the common interest community but managed by an affiliated tax-exempt organization, the benefit of a community transfer fee is no longer exclusive to the encumbered properties. This negatively affects the right of residents to determine the use of commonly owned property, which seems unrelated to the Agency's application of the touch and concern doctrine.

CAI urges the Agency to substitute the word "primarily" for the word "exclusively" in this portion of the proposed definition. If the Agency adopts CAI's recommendation, the relevant sentence in the definition of 'direct benefit' would read as follows:

> *"...as well as cultural, educational, charitable, recreational, environmental, conservation or other similar activities that primarily benefit the real property encumbered by the private transfer fee covenants."*

Community Association Activities on Behalf of Residents

Community associations may be practically viewed as not-for-profit entities that serve as the legal vehicle through which residents of common interest communities govern, maintain and manage their community. Residents use their community association to deliver at least three core services: governance services, community services, and business services. The Agency's definition of 'direct benefit' fails to capture the range of services that community associations deliver.

The Agency's proposed definition of 'direct benefit' limits the eligible activities of community associations to only those activities that "...exclusively support maintenance and improvements to encumbered properties..." Such a limited definition of eligible activities of community associations will substantially restrict the activities that association budgets may fund. Associations fund association governance, legal action, contracts for community services, purchase of insurance, reserves planning and contributions, asset investment, and other similar services fundamental to the operation of a common interest community. These activities are beyond the scope of the Agency's proposed definition which allows community transfer fees to fund only those activities that "support maintenance and improvements to encumbered properties".

CAI strongly urges the Agency to revise its proposed definition of 'direct benefit' to include all duties and responsibilities that residents routinely assign to their community associations. Such an amendment would fall within the legal doctrine of touch and concern and therefore should not be subject to limitation by the Agency. CAI recommends the Agency amend its proposed definition of 'direct benefit' to read, in relevant part, as follows:

Direct Benefit means that the proceeds of a private transfer fee are used to provide governance services, management services, or maintenance of and improvements to common elements as such services or elements are described in or required by a deed, declaration or by-law that binds encumbered properties, as well as cultural, educational, charitable, recreational, environmental, conservation, or other similar activities that primarily benefit the real property encumbered by the private transfer fee covenants.

Exclusive Right of Residents to Govern Use of Common Elements & Property

The Agency's proposed definition of 'direct benefit' can fairly be read as restricting the right of residents of common interest communities to determine the use of common elements and common property irrespective of the wishes of residents. The right of property owners to limit the use of and access to their land, subject only to well-established Constitutional restraints, is sacrosanct.

Homeowners, acting through their community associations, have long reserved the right to lawfully restrict commercial and other activities of residents and visitors as an exercise of their basic private property rights. That residents elect to exercise their property rights through a community association by no means degrades their full use of these rights. While CAI does not believe it is the Agency's intent to diminish the right of homeowners to govern the use of and access to properties owned or controlled by a community association, the Agency's proposed definition will have this effect.

Specifically, the Agency's definition of 'direct benefit' states:

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 minimus usage may be provided free of charge for use by a charitable or other not-for-profit group.

This definition clearly limits the property rights of homeowners in common interest communities by restraining the right of residents to determine non-resident use of commonly owned property. Association by-laws or rules adopted by an association's board govern the use of common property and common elements. The Agency's proposed definition reaches into every common interest community across the country that elects to put in place a community transfer fee and places limits on the decision of residents regarding the use of property. A community association may wish to condition non-resident use of and access to common property on the basis of a fee; this is a common occurrence. However, this is a decision reserved exclusively for residents.

Further, the proposed definition may also be read as requiring that common interest communities provide public access to common property or elements in exchange for a fee as a condition for access to mortgage financing supported by the GSEs. The proposed definition of 'direct benefit' appears to condition a finding of direct benefit only when the public may, through payment of a

fee, access facilities funded by a community transfer fee. The Agency's proposed definition states that community transfer fees provide a direct benefit "*when members of the general public may use the facilities funded by the transfer fees…only upon payment of a fee…*" While unlikely to be the Agency's intention, this could force a community into choosing only among unpalatable alternatives.

CAI understands the concern that the Agency has expressed in regards to ensuring that community transfer fees benefit the properties and communities in which they are levied. However, the Agency's concern over the use of community transfer fees is not appropriately remedied by the potential granting of rights to entry into private communities by individuals who do not own property within the community. The benefit-burden test on deed restrictions also does not support such an analysis. The test does require that the benefits of any deed provision, such as a transfer fee, benefit the property or properties upon which the fee is levied. It does not mandate access, for a fee or on any other basis, to burdened property by the public at large.

CAI is unaware of any similar guidance or rule enforced by the Agency that controls or may condition public access to privately owned property in such an intrusive manner. Residency in a community association supported in part by a community transfer fee does not alter the fundamental right of property owners to determine use of their land either for a fee or free of charge and to lawfully restrict the use of or access to their land by members of the general public.

Based on CAI's strong commitment to the property rights of common interest community residents, CAI respectfully, but strongly, encourages the Agency to strike the final sentence of the definition of 'direct benefit'. This portion of the Agency's proposed definition does not apply the doctrine of touch and concern in a manner generally consistent with existing jurisprudence and will create confusion for common interest communities.

CAI understands the Agency is seeking to achieve a public policy goal through this language. Given that the intent of the existing language is unclear, CAI encourages the Agency to issue a clarification of intent describing the activities it is seeking to regulate and request additional comment. This process will provide the Agency the benefit of public comment on those proposed restrictions and will improve policy outcomes.

Excepted Transfer Fee Covenant

CAI encourages the Agency to consider the benefits of more clearly defining the private transfer fee covenants it is seeking to prohibit by adopting a separate nomenclature for the fees the Agency does not seek to restrict. Different nomenclature will add clarity and simplicity to the proposed rule by clearly defining for all parties the transfer fees the Agency seeks to prohibit and the transfer fees the Agency seeks to permit.

As the Agency notes in its proposed rule, compliance with a final regulation on transfer fee covenants will be problematic for a number of reasons. The Agency states that the GSEs should issue seller-servicer guidelines, require representations and warranties, and employ other processes to ensure compliance by their members or customers. This places the burden of

determining if a transfer fee is prohibited or excepted on loan underwriters, title attorneys, or closing agents. Clearly defining what is prohibited and what is acceptable with terms that are accurately descriptive will improve compliance and offer easily understood protections to homeowners.

As evidenced by the use of the term 'community transfer fee' in this document, CAI believes a separate nomenclature offers benefits to all parties covered under the Agency's proposed rule. CAI recommends the following definition of 'community transfer fee covenant' for incorporation in any final rule rather than the Agency's proposed term, 'excepted transfer fee covenant':

> *Community Transfer Fee Covenant means a covenant, including a deed-based fee, whether set forth in a deed, declaration or association bylaws, that is payable at time of transfer to a community association or other entity that is directly engaged in the governance, support, maintenance, enhancement or investment in the common interest community of which the mortgaged lot, home or unit is a part.*

Recommendations on State Adopted Private Transfer Fee Restrictions

As the Agency notes in its proposed rule, several State legislatures have enacted or are actively considering restrictions on the use of private transfer fee covenants. As CAI noted in its comments on the Agency's prior proposed guidance, this is the most appropriate legal venue for private transfer fees that benefit unrelated third parties to be governed. CAI bases this position on the fact that an Act of a State legislature can render a private transfer fee covenant invalid and unenforceable.

It is on this basis that CAI urges the Agency to consider the following amendment to Section 1228.4 of the proposed rule. CAI believes this amendment clarifies the extent to which any State restrictions on private transfer fee covenants are unaffected by the Agency's proposed rule:

> § 1228.4 State restrictions unaffected.
>
> This part does not affect state restrictions or requirements with respect to private transfer fee covenants, such as with respect to validity, enforceability, disclosure or duration.

Recommendations to Improve Disclosure of Deed-Based Fees

CAI strongly supports full and complete disclosure of all rights, responsibilities and obligations of common interest community owners and residents prior to closing. For this disclosure to be meaningful and actionable, buyers must be granted sufficient time to obtain, review and understand all documents relating to the community association's governance, rules and regulations and homeowner obligations. Further, CAI believes a purchaser should have an unambiguous right to cancel a contract to purchase a home in a common interest community on the basis of their review of these documents.

Because different community associations have different requirements, purchasers need prior disclosure to ensure that they are purchasing a home in the common interest community that is best suited to meet their needs. Conflicts between association boards and residents who did not have a clear understanding of association rules and restrictions prior to making a purchase do not benefit any party. These conflicts are all the more frustrating to both homeowners and association boards given that the conflict could have been avoided if meaningful disclosure had been provided to the homeowner well in advance of closing.

UCIOA provides consumers with considerable protections when making a purchase in a common interest community. These protections include, but are not limited to:

- Disclosure of estimated monthly assessments
- Disclosure of any other fee due from the purchaser at closing
- Disclosure of the association's covenants, rules and restrictions
- A consumer's right to cancel, without penalty, a contract to purchase based on their review of required disclosures
- Penalties for disclosures that are false, misleading or by act or omission fail to disclose material information
- A private right of action against parties failing to provide required disclosures to a purchaser while also recommending specific monetary penalties in addition to any damages awarded by a court

CAI believes the Agency could usefully consider the addition of a requirement for mortgages purchased or supported by the GSEs, based on UCIOA, that provides purchasers (1) disclosure of their obligations when purchasing a home in a community association; (2) a reasonable period of time prior to closing to review and understand these obligations; and (3) the ability to cancel, without penalty, a contract to purchase based on their review of the required disclosures.

Such an addition would increase consumer awareness of community transfer fees and other mandatory obligations that are common to community associations. Further, these disclosures are—in many cases, but not uniformly so—mandated by State law. CAI supports mandated document disclosures or resale certificates and acknowledges an association's right to charge a reasonable fee for their production.

Conclusion

CAI appreciates the open process the Agency has used as it considers the question of private transfer fee covenants. The use of notice and public comment allows all interested parties to review and express support or concern about a public policy prior to its implementation. Not all housing related agencies in the federal government embrace this process, preferring instead to implement significant changes in public policy through administrative order. This process results in poor public policy that can have profoundly negative impacts on homeowners. CAI commends the Agency for its commitment to transparency in government.

While CAI has deep concerns with some aspects of the Agency's proposed rule, CAI does strongly support the Agency's efforts to prohibit private transfer fees payable to unrelated third

parties. We wish to continue the productive conversations on this subject with the Agency and will be contacting you soon to arrange an opportunity to discuss the matter in greater depth.

If you require additional information or wish to discuss the contents of this letter, do not hesitate to contact me or Mr. Andrew S. Fortin, Esq., CAI's Vice President for Government and Public Affairs, at (703) 970-9220.

Sincerely,

Thomas M. Skiba, CAE
Chief Executive Officer

Appendix C

community
ASSOCIATIONS INSTITUTE

Resale Certificate Requirements by State for Units in Condominiums and Common Interest Communities

States that require resale certificates/disclosures for purchases of condominiums: Twenty-Five states currently impose a resale/disclosure packet for the resale of a condominium unit. This requirement exists in the following states (light and dark gray states):

AL, AK, AZ, CA, CT, DC, FL, IL, ME, MD, MN, MO, NB, NV, NH, NM, NC, PA, RI, TX, VT, VA, WV, WI, WA

States that require resale certificates/disclosures for units in HOAs: Twelve states currently impose a resale certificate requirement for the resale of units within a homeowners association. This requirement exists in the following states (light and dark gray states) :

AK, CA, CT, FL, MD, MN, NV, PA, TX, VT, VA, WV

States that regulate the fees charged for resale certificates/disclosures for condominiums:

A total of four states regulate the fee that may be charged for the production of a resale certificate/disclosure packet for the resale of a condominium. This requirement exists in CT ($75), NV ($160), VA (Varies – professionally managed communities, volunteer managed communities), WA ($150)

States that regulate the fees charged for resale certificates/disclosures for Units in HOAs:
CT ($75), MD ($100), NV ($160), VA (Varies – professionally managed communities, volunteer managed communities)