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Federal Housing Finance Agency backs off proposal to ban transfer fees

Many homeowner associations collect the fees when houses or condos are resold and use the revenue for community improvements or to build up reserves.

By Kenneth R. Harney

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Reporting from Washington

Thousands of homeowner associations and condominiums around the country just sidestepped a potentially costly problem: A federal agency this month backed off its controversial plan that would have made obtaining mortgages in their communities much more difficult, and would have dried up a key source of revenue that associations use to pay for improvements and property maintenance.

A proposal in August by the Federal Housing Finance Agency would have in effect banned the covenanted transfer fees that many homeowner associations collect when houses or condos are resold. The fees typically range from 0.25% to 0.75% of the resale price of the house. The revenue is then spent on such things as community improvements — upgrading roads, bike paths, recreation facilities — and building up required capital reserves.

The agency proposed banning the fees from all mortgages eligible for purchase by the major government-controlled enterprises it oversees — Fannie Mae, Freddie Mac and the Federal Home Loan Banks. The same proposal also banned loans containing private transfer fees where the money flows not to community improvements but to investors seeking long-term revenue streams.

"This was a really big deal" to persuade the Federal Housing Finance Agency to reverse its position, said Cort Chalfant, senior vice president of Rancho Sahuarita, a master-planned community with 12,000 residents near Tucson.

Chalfant said the 0.75% transfer fee collected on resales in Rancho Sahuarita is spent on upgrading amenities and facilities. Without the fees, the association would have to raise its annual homeowner assessments dramatically — putting financial pressure on homeowners "at a lousy time [economically] to do that," he added.

Chalfant estimates that if it had been adopted, the federal agency's proposed rule would have cost the association $10 million over the coming decade, and would have decimated sales and property values since none of the houses would be eligible for conventional mortgages.

Peter Kristian, general manager of the Hilton Head Plantation Property Owners' Assn., in Hilton Head, S.C., said the effect on his community of 4,100 homes would have been equally devastating. Kristian's association raises roughly $250,000 to $300,000 a year for public-benefit improvements through 0.25% transfer fees on resales.

When the housing finance agency proposed its initial rule, it was critical of covenanted homeowner association transfer fees for being "unrelated to the value rendered," and at times applying "even if the property's value has significantly declined since the time the covenant was imposed."

The proposal was also highly critical of investor-driven private transfer fee programs, such as one marketed by Freehold Capital Partners, a New York company that imposes 1% transfer fees on home resales for 99 years. The company says it has signed up thousands of development projects worth "hundreds of billions of dollars" around the country. The revenue streams created by Freehold's private covenants are intended to flow to private participants in the program — the developers themselves, bond investors who provide capital upfront and others.

But the housing finance agency did not distinguish between homeowner associations' public-benefit transfer fee programs and Freehold-type investor-driven, private-benefit variants in its proposed ban — all would have been prohibited.

Reaction from individual homeowner associations and groups representing them — primarily the 30,000-member Community Association Institute — was swift and intense. The institute polled its members and found that an estimated half of them — representing about 11 million houses, condos and cooperative units — rely on deed-based transfer fees. Owners of those homes would be cut off from most mortgage financing under the housing finance agency's proposal, worsening the housing crisis that sent Fannie Mae and Freddie Mac into severe financial distress.

The agency's revised proposal essentially says: Oops, sorry. We were a little too broad-brush the first time around. Now we get it, and we'll exempt homeowner associations that use the proceeds of transfer fees to benefit the property or community. Purely investor-oriented programs such as Freehold's, however, would still be barred.

Asked for comment, Bryan Cohen, Freehold's general counsel, said this is "the wrong time to deprive the hard-hit construction sector" of the financial benefits available through a private transfer fee program.

Bottom line: If your house is one of the 11 million exempted from the latest proposal, you can probably breathe easy. The feds are not going to put you on a banned list.

On the other hand, if you're thinking of buying into a community where the developer is offering lots or houses with investor-driven transfer fees, you could have a long-term problem. Get full disclosures and legal advice before signing up.

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