

**Title Insurance (C) Task Force  
Public Hearing on Private Transfer Fee Covenants  
Orlando, Florida  
NAIC Fall National Meeting  
Sunday, October 17, 2010**

Chair Alan Seeley: Well good afternoon everyone, we have an enormous room for this. So whatever, we will try to make you feel cozy. So this is a public hearing on private transfer fee covenants. It's an issue that the Title Insurance Task Force will be discussing at its meeting on Tuesday morning. And we have a variety of presenters today and I want to thank them all in advance for their willingness to come here and feel us in on private transfer fee covenants. We might as well jump in and get started. Joe Bieniek will do the roll call.

We have the Task Force chair Alan Seeley, New Mexico, Florida, Alaska, Arkansas, California, Colorado, Indiana, Kentucky, Maryland, Michigan, Minnesota, Missouri, Nebraska, New York, Rhode Island, Utah, Virginia, Washington, and Wisconsin

Alan: Okay, thank you Joe. I'm also glad to see the good attendance here from our membership. The first person we have on our list to talk to us is Charles Proctor from the National Association of Independent Land Title Agents, welcome Charles.

Charles: Thank you very much. Is this on? Good afternoon and on behalf of the members of the National Association of Independent Land Title Agents I thank you for the opportunity to not only address this group to also thank you for your attention and consideration of this matter to the title insurance industry and to consumers and particularly to consumers. Title insurance as you know is probably the least understood and appreciated form of insurance in the United States. Very few people realize the significance it plays in our economy. In fact, I believe and Hernando De Soto Desoto who wrote books on this subject believed that it is the keystone of our economy. Why is that? The United States has one of the best if not best land records systems in the world. Not only do we have records that some parts of the countries, particularly in the 13 original colonies, that goes back over 300 years. We have these records indexed and managed in such a way that they are retrievable, particularly in today's computerized society sometimes at microseconds notice. That is not always the case and that is one of the reasons we are here today to talk to you about, not only this private transfer covenants but also the process that it takes to find a private transfer covenant. In addition to have the best records system in the world we also have title insurance to back it up. And title insurance means that when someone buys a property, whether it's a home or a business, they know that they're the owner. They know that they can invest in it with assurance. They know that the money that they are going to spend it well spent. For example a home owner goes out and buys a home what is the first thing that they do? They go to Home Depot, they go to Lowe's they invest in the property, even a commercial property a business owner is going to take that property and he's going to improve it. Why, because the previous owner probably fully depreciated it. If it's brand new, he's investing significant new capital into that property. The fact that we have a stable reliable system of title insurance and record keeping is the keystone to our economy.

I am not sure if perhaps if some other people here today will know the value of real estate in this country. Hernando De Soto referred to 300 developed countries where there were in his book, about 10 years ago that was comprised of shanty towns. And the three cities were Mexico City, Port au Prince Haiti, and another city in Egypt and that acreage undeveloped un-owned uninsured, he believed 10 years ago for it to be worth \$10 trillion to those countries if they could develop that land. But because they

don't have those fundamental blocks to the economy, the record keeping and the title insurance the land remains unused, undeveloped and there is no money going back into the economy. I'll talk about this later but one of the key concepts that we are going to be talking about is the title insurance is risk avoidance as opposed to risk assumption. And I'll talk about that later but that's one of the fundamental concepts that we need to keep in mind as we address this issue. When you get a deed to a home today, you get a fee simple deed. A fee simple deed means that you own that title, that property absolutely. That you have the right of quiet enjoyment and quiet enjoyment is that privilege that comes with the ownership of land which can happen very quickly most home transactions sales are completed in any where from 30-60 days, maybe 90 days. But when you get that deed there are six covenants that go along with it, including this one of quiet enjoyment. And it means that you own that property free of any encumbrances, any restraints, anything that would interfere with you use of property. However, in today's society we have quite often covenants running with the land. A covenant running with the land may be something as simple as basic as an easement allowing access for the electric company, sanitary sewer, or cable. It might be a shared drive way, it might be some other form of usage of the land that benefits two parties or more. Those covenants running with the land go on perpetually in addition covenants running with the land can refer to the usage of the property. Sometimes restrictions are put on property that restricted taps usage as to what it may be used for. If you look at older deeds back in the 1800s you will see the equivalent of our zoning codes and building codes today. Saying such as no house should be built for less than \$3000.00. No house shall be within 20 feet of a roadway. No property should be used for a tannery or slaughter house. These are all restrictive covenants but generally the benefit public good and the public interest. Today we are talking about private transfer covenants and a private transfer covenant is one where by for and what's being proposed what has caught everyone's attention is Freehold Capital Partners, marketing and supposedly effectively having put in place covenants where by every time the property is sold the next 99 years, 1% is paid by the seller to a holding company established by Freehold Capital. This is done with purported purpose of allowing the builder to have capital to build the new development supposedly. As well as insure an income stream, some of which they say is going to go to charitable or public works. Unfortunately based on the documentation I've seen most of the money for the next 99 years at 1% is going to the builder, developer and/or Freehold Capital. Who benefits in this scheme? The builder and Freehold. How does it benefit the consumer, I'm not sure. I haven't seen anything yet that says that it would benefit them. Freehold would like you to believe that the benefit comes from a reduced sales price. But let's look at that reduced sales price because I don't believe that it is all it's reported to be. When you reduce the sale price of two equal homes and one of them is reduced by the 1% that Freehold alleges, the other home is still assessed at the market price and the home with 1% transfer tax is devalued. Not only does it devalued but it also affects things such as transfer tax payable to the state government and local property tax assessed by state government. It also affects the depreciation, which means instead of buying a house at \$200 thousand you're buying it at 195 because of that transfer tax. When it appreciates you have to go that much further to purchase the property or make that back up in appreciation. And by the same token, if faced with the choice of the two properties, the one with the transfer tax and one with out, which one are you going to take. It'd be a pretty clear option. This type of covenant becomes restraint on alienations, in other words it inhibits the free sell and transfer or real estate. The restraint on alienation is fundamentally against our concept of real property in this country. It violates a number of principles. Number one, and these are common law principles that have been established for many years in this country and there's much case law to support it. There's a need for the parties to agree on the intent of the covenant. In most instances, I can't see a buyer agreeing to pay a 1% transfer tax to a private entity when they sell the property. And it looks like this is mostly a unilateral decision forced on the buyer by Freehold and others that will attempt to duplicate their process. Number two, this covenant does not touch and concern the land. And if you look in your materials there is a great deal of discussion about this concept of touching and concerning the land. But after the initial development, which supposedly

the developer is getting capital to build a project there is no benefit to the land. There is nothing touching the land except it may create a lean on the land. There is no benefit. And I go back to the other concept that if the developer is so under capitalized that he needs a 1% transfer tax like this in order to fund the project instead of using his own capital to being able to raise it from the bank, should he even be in the business to begin with. Three, lack of privity, basic concept law talks about privity between two people. There's after the original builder and home owner have gone their separate ways the next home owner has no privity of contract with the developer or with Freehold or with their holding company that is going to hold the funds. There is no nexus, there is no connection between the two. Fourthly, it's clearly a restraint or alienation of the sale or transfer of the property.

The next problem with it is in the process of a real estate transaction, a normal real estate transaction, buyers, appraisers and lenders will not be aware of the transfer tax even if a disclosure provision is put into law that would inform them of this. Why, because the basic way a real estate transaction occurs. First you have your agreement of sale, then you submit your agreement of sale to the mortgage company and a tile is ordered. The title search may come back in two or three days, it may come back in two or three weeks. But there is a gap between the time the agreement of sale is signed, the mortgage is applied for, and the time the search comes back. And I'll talk more about the search in a little bit. So when the transaction is entered into, it's generally done blindly and even if you have a sophisticated consumer that can understand the 10 or 12 page document that purports to be of this declaration of covenant that Freehold is setting forth, it would not likely be able to understand it. It is full of legalese and fine print and most realtors also would be unable to explain the implication of what it means in terms of the value of property and the effect on the property of the years that the homeowner has the property. If this tax is not paid, if it is missed by the title company, it creates a lien on the home. When it creates a lien on a home, this creates a risk for the lender it creates a risk for the title insurer because I'm sure there is going to be some lawyer out there that's going to find a way to file suit. And it eventually must be paid, it can't be ignored. That means that it may come down the road at a later date. It also effects the lenders position in terms that they're priority for the lien and creates additional record keeping at the court house and in the public records. The restatement of third, restatement of third of property suggests goes so far as to suggest that these types of covenants are unconscionable and at best against the public interest for good.

Now let's go back to the process of the real estate, the real estate process itself. Once the searcher gets the order they start searching the record. And in most states the time frame for looking at a full title search is 40-60 years; the equivalent of at least two generations. And during that time frame, they are looking at deeds, they're looking at mortgages, they're looking at other documents such is covenants similar to an easement or what have you that effect the property. I have the privilege of teaching, of being and edge on professor Widener University School of Law and I teach a course called Title Search and Examination. I believe it is the only if not one of a handful if that of courses like this in the United States. The course is not taught often. I actually take my students into the course house and show them the record system. And although the basic record system is very similar, we do something called the Russell Index System. There are variations from county to county throughout the United States. And those variations include not only the way the documents are recorded but the type of media that they are recorded on; everything from hand-written books to microfiche to now days computer. I can tell you this without taking away time from the other speakers that a search can quite often take more than just an half hour, an hour, it could take two days, it could take three days because the different things you find in a search, the different things you find in looking at a deed, looking at a mortgage when looking at other documents affecting the property. And the trails that you can go off on are quite often very extensive. The searcher, who is completely objective, their job is to put the information down on a piece of paper that is given to an examiner. A title examiner looks at that information and starts making some decisions about the quality of title. Are there liens? Are there encumbrances? Are there things that

would hinder the transfer of the sale of this property? Are there things that hinder or transfer the insurability of this property? And in going through that process the private transfer companies would be added to the list of things that have to be reviewed. It's just there is one thing, as time goes on the search would have to go back a 100 years or more. Why a hundred years or more? Because the covenant is good for 99 years. Why more than 99 years? Because the type of lien may be created in the 80<sup>th</sup> year and may good for 20 years or longer depending upon how this finally folds out. We may be searching for restrictive covenants for many many years after this. In addition Freehold Capital partners, even though they've asked for a business methods patent are not the only people who are going to be doing this. Once they get on the band wagon other people join, they'll find a way around the patent issue and come up with other types of things. Now the examiner has looked at this and has, depending upon the underwriter, the title underwriter, is going to put some conditions down in that title commitment. As to private transfer covenant and those conditions can include information regarding the beneficiary, which supposedly is this trust holding company that Freehold is proposing. Other liens that may have been put on the property in previous years, where the money is to go, how it's to get there, all these things are determined by the examiner but then have to be communicated to the attorney, the real estate agent, the buyer and the settlement clerk whose charged with the responsibility of collecting the money and seeing that it is sent to the proper parties. In addition just like property taxes and income taxes there will have to be certifications obtained telling the title company that there are not other previous transfer taxes outstanding. Another set of record keeping, both at the court house because it's a lien against the property and as well as with the records maintained by the title company—another level of bureaucracy imposed by this process.

Let me talk again about the risk assumption versus risk avoidance. By going through this process title insurers avoid a risk. That's why there is a one time premium on the life of the property. There is not a premium every year. The idea is that the risks have been eliminated, that the risks have been evaluated, that the risks have been taken into consideration and decided whether the property can be insured or not. Under risk assumption every year in the casualty business it's determined whether or not certain property, car, automobile or what have you, even health insurance, what's the likelihood that someone's going to have a fire in their house, get in an accident in their car or require health insurance. It's a different concept. And that's looking forward. In title insurance we are looking back, what happened in the past. Title insurance doesn't insure after they pay a settlement, only up to the day of the settlement. The potential for failed transactions, the potential for property that's unmarketable, the potential for property that has a permanent cloud on title, we can't even foresee it at this point. We have enough of a challenge as it is today with the search examination and settlement process not to add another layer to this. In Pennsylvania about 10 years ago, there was a case called Bortz. And in the Bortz case the Superior Court of Pennsylvania determined that the title closing agent was the gate keeper for the transaction, irrespective of what the issue was. In that particular case they held the title agent responsible for a failed septic system. Septic systems have nothing to do with title to property. The Bortz case is still good law in Pennsylvania and the concept of the title agent being the gate keeper is still good law. Title agents in Pennsylvania and in other states have taken the approach of making sure of whether it's a use and occupancy certificate, a septic certification, a homeowner's inspection that those things have been resolved to everyone's satisfaction before they settle the deal because they don't want to end up being sued as that's what happened in the Bortz case.

All of the things that I've discussed increased not only the cost of the transaction of the record keeping and certifications and examinations and everything that I have discussed increases the risk to the homeowner. Some of the articles that Justin Ailes has provided as attachments to his presentations, some of his newspaper articles talk about real live people who found out after they brought the property that was subject to these transfer tax covenants. That in itself is worthy of note, because that practice no

matter what we say about disclosure up front right now at any real estate transaction when the home owner buys a home, they want between the agreement of sale and mortgage application they have more paper than they can ever imagine and what to do with it. Currently there are 18 states that have passed legislation affecting private transfer covenants. Most of them have abolished it. California and Texas seem to have a slightly different approach. There are other states where it's under consideration. FHA will no longer fund a loan that is subject to a private restrictive covenant, a private transfer covenant. Federal Home Finance Agency has given guidance to both Fannie Mae and Freddie Mac and the Federal Home Loan banks not to fund loans with a private transfer tax. Private transfer taxes are not only imposed by not only the National Association of Independent Land Title Agents but by the American Land Title Association, Pennsylvania Land Title Association and many other individual state land title associations throughout the country.

In summary, in our opinion, private transfer covenants only benefit developers and Freehold Capital and other people like them. This is typified by the fact that Freehold is attempting to securitize these monies. That means put them on Wall Street and sell them just as you would other types of securities, whether its mortgages or bonds. In order to do that you must be generating a tremendous amount of money, money coming out of the consumer's pocket. It's more work and complexity for searchers, examiners and closers and would necessitate mandating a longer search time for a full search. There is more risk to title underwriters and to mortgage lenders. More risk in that the possibility of a claim, a lien coming up, and either one that would affect the property. There is a lack of transparency in this process, even if there is a disclosure how many homeowners are really going to understand what the builder is doing with the money, what Freehold is doing with the money and what the supposed I think it's 5% that they say they use for public works or charitable organizations where it's really going or what it's doing. But it's not benefitting them. The key here is, it's unlike a homeowners association where in a homeowners association sometimes you might \$500 or a \$1000 to fund your capital reserve account with that homeowners association. That \$500 or \$1000 when you sell the property is generally repaid by the new buyer of the property. But that money is going directly into your homeowners association to capitalize the necessary repairs and improvements to the property you own directly. There is nothing in a private transfer covenant that shows that any of that money is going back into the property. It's a violation of, as I mentioned, common law principles and our basic understanding of the free right of alienation of property. And I know alienation may, it sounds strange to you, it's a legal term, to transfer or sell property without restriction. But mostly I think the biggest thing we have is a devaluation of property, which people don't even realize when they are getting into it and money going to someone under a pretense that as I hope I've shown that is instantly veiled and that only benefits the builder and Freehold.

The key example is this; if you have two similar properties or identical properties and one had a private transfer covenant and the other didn't which one would you buy? What can the National Association of Insurance Commissioners do? There are a number of things. Obviously writing or issuing an opinion paper on this subject would be helpful. Drafting or supporting model legislation—I've seen several drafts of model legislation in my research on this matter. I've seen states that have model legislation pending, I've seen other drafts out there. In addition letting people at HUD, Fannie Mae, Freddy Mac, federal home finance agency know what your position is on this matter and supporting individual state efforts to stop these types of covenants which benefit no one except Freehold and their developers. I thank you for your time and your consideration on this important matter. And if you have any questions, I'd be glad to answer them.

Alan: Sorry, thank you Charles. I'd be happy to take question from the Task Force; I do simply want to remind everyone that we do have certain, even though we have a hunk of time here, we do have a total

of four speakers and certain do have time constraints so I'll be happy to take just a few questions but just be mindful that we really don't have the time to develop into full blown discussions right here. Bill.

Bill Lacy (AR): Thank you, mostly in the way of clarification I just want to make sure I understand. Now even though these things are good for 99 years in a typical situation there is nothing that prohibits them from putting them on for 120-200 or into perpetuity.

Charles: Well that's an interesting question, they're proposing the 99 years, however there are covenants in land records today that are good for perpetuity and that potential is there in my opinion. Now I've seen, some research I did felt that 99 years would be the maximum that it could be enforceable but that would be for a court to decide.

Bill: So in essence you couldn't limit your search to 100 years, you would have to go back almost; I mean when we get way out in the future, you'd be going back potentially hundreds of years to eliminate the possibility.

Charles: That possibility is there. And the possibility of the lien unless there is some legislation created saying the lien would expire for 20 years the lien might be there forever.

Bill: And there would be nothing in this that wouldn't prevent more than one of these to be placed on property by various entities as they come into possession of the title or like some other purpose.

Charles: I hadn't thought of that, but it's possible you could have more than one private transfer covenant on a property. I think what's more significant is that Freehold won't be the only players in the game. And you'll have a number of people out there doing a copy cat type of product or whatever and putting the private transfer covenants on property and just keeping track of that and with different forms, there would be no uniformity to it. They could bury it in the deed, they could bury it mortgage, all kinds of documents get reported at the court house, they could bury it somewhere and it would be very difficult to find.

Bill: You also might run into situations where someone buys a particular piece of property on a contract for deed and doesn't ask for title insurance. Or the title company misses it so the next one that comes around really has to go back to make sure it's been properly assessed and paid in each closing.

Charles: That's correct, and in addition, in spite of the efforts of our industry to educate our people, continuing education is mandatory in many states, it would mean retraining our searchers to look for these. And I recently had a case where I was defending a title claim and in 1958 as recently as 1958 a mortgagor and a mortgagee had recorded a document called a consent agreement and buried in that consent agreement was a covenant running with the land regarding payment for common space. Nobody saw it until 2007. It was valid. But because it was in this consent agreement which was supposedly would no longer be in effect after the mortgage was satisfied but it was still a covenant running with the land. Even though the mortgage was satisfied it wasn't picked up, no searcher picked it up. I wouldn't fault any searcher. So this would be a whole new level of work to train searchers and title examiners in. And for underwriters to develop standards as to how they are going to deal with it.

Bill: I just had one more question. You talked earlier about the offer and acceptance process, generally that's done blind. The buyer knows nothing about the title to the property. And generally if the seller can deliver a marketable title and financing is obtained and all those good things, and the sell is going to go through or you can force it. So in this case if these are valid liens and they are not disclosed until you get

basically get your title report. The prospective buyer would have received no notice of that and still be forced to go ahead with the closing and give up his 1% later when he sells.

Charles: That's exactly what we are afraid of although there is discussion about a disclosure form. But as I said earlier, how many people are really going to pay attention to that disclosure form. As it is today, in example Pennsylvania it's required that you give a sellers disclosure regarding the condition of the house. I can't tell how many cases I've seen that a house that has problem, whether it's a leaky roof, a wet basement or what have you, even though that disclosure form is given and many times that disclosure form is either inaccurate or never given at all even though it's law.

Bill: Well now days when so many properties are bought maybe through foreclosure, chances of missing all those disclosures are increased.

Charles: Oh absolutely, the volume of work that is involved and the complexity of the search process. I mean I can't even begin to get into the complexity of the search process but I can assure you that when you look at a title, yes you might have one that you can do in 45 minutes. The property next door could take you two days. It's that complex and computers are great but there isn't a computer yet that goes back 300 years. And although that is not a requirement that generally isn't an issue until you can show me a county that really can give you about a 100 years worth of properly recorded documents on the computer and the indexing that will lead you from one document to the next which is part of the process. You need qualified searchers to make sure our land records are accurate. It's been estimated that we spend approximately \$230-240 million a year in our industry correcting public records. Just making corrections to the deeds that are wrong or misreported or mortgages or what have you. That's a tremendous amount of money just to keep the records straight. But that's an investment that the title insurance industry makes on behalf of the consumers, on behalf of the lenders, on behalf of the underwriters to make sure that we've got good and marketable title for all the real estate in this country.

Al Bottalico (CA): One question for you, do you know when Freehold did its deal and how long it's been going on and how wide spread. Do you have any sense of how wide spread this is?

Charles: From a date stand point I don't know. But I did see in some of my research that I believe they are saying they have already \$600 billion worth of real estate subject to private transfer taxes. Now that's a drop in the bucket in terms of total real estate in the United States in terms of its value. But that's the dollar amount that they say that they have encumbered so far. When they actually started I'm not sure. But there is a fair amount of property. And I have seen other people besides Freehold with something similar to private transfer tax, that's why I say there is going to be copy cats. There are others way to do that to have something the equivalent of it. And if this idea catches on, it it's not nipped in the bud and it's already out of the gate so to speak it's going to become an increasing problem.

Al Bottalico: What happens to if a state outlaws it after deals have already been done in that state? What does that do?

Charles: Well under the United States constitution you can not have any law that is *ex post facto*, meaning retroactive. So the properties that are already subject to the transfer tax of private transfer covenants, they would still be subject to it. However, perhaps through some litigation or other things the number of properties that are subject to it might be decreased but it would only be effective as the date the legislation took effect.

Al Bottalico: So the sooner the better.

Alan: We are facing the clock here, so if there are no other questions from the Task Force, I want to thank you, Charles Proctor for making your presentation. Paul do you want to...

Paul Hanson (MN): I have one quick question, there is nothing that limits this to 1% is there?

Charles: Well that's another question; no it could be 2%. It is quite common to have a transfer tax in real estate that the governments collect. In Pennsylvania the state gets 1% and the other 1%, it's 2%, is divided between the county and the local governments. But within Pennsylvania there are municipalities that I believe Philadelphia is 3 or 4 %, Redding and Brooks County is 5% and most of that stays with the local government entity. So they proposed 1% that Freehold or somebody else could make the two or three or any other number. There is nothing to limit that if they are not controlled right now.

Alan: Okay thank you, thank you very much Mr. Proctor

Charles: Thank you.

Alan: I do want to let the Task Force know that we are recording these sessions so if you could give your name and your state before you ask questions that would be helpful. For the record we had five questions from the Working Group for Mr. Proctor. The first two were from Bill Lacy of Arkansas, the next two from Al Bottalico of California and the fifth one from Paul Hanson of Minnesota. Our next speaker is Jeffrey Troutt, who we all know as a former colleague of ours here a regulator now has his own law practice. Jeffrey welcome.

Jeffrey: My name again is Jeffrey Troutt. I have my own law practice. I'm a former regulator and worked as council and as president of a title company and I've worked as outside council and outside litigation council for a title company. I'm going to do what I can to shorten the time because a lot of what I talked about has already been covered restraints against alienation, legal enforceability etc. Those are problems with private transfer fees. I should say, if I weren't sort of a bit jittery I would have said right up front, I'm testifying in opposition to them and I'm not representing anybody but me. But I think they are a bad idea and based on my experience as a regulator, as a sort of grunt in the title industry, in leadership at least in the title industry, and as an attorney I think they are a very bad idea. Among the problems you create and you already heard the previous speaker talk about restraints against alienation of title. To go in to just a little bit of it, if you don't pay the transfer fee there is a transfer for lien on the property. And that creates a right to sell the property in order to satisfy; it's a debt, evidence of a debt. Which if the transfer fee is legal it is owed upon purchase of the property and it creates a debt. And if that debt isn't paid then the person who is owed money has a right to put a lien on the property and sell the property in order to pay off the debt. The discussion has been a little bit, they have been 99 years and there are legal reasons to use it but they are not necessarily rules that you can't get along with. To talk about how difficult, what a cloud this would create I thought a little bit of the state of Pennsylvania. You can imagine that William Penn said I got an idea that's going to make me and my family rich. Every time anybody... I've been given by the King of England the state of Pennsylvania. Every time someone buys or sells property in the Pennsylvania I or my descendents share a pound. And you can imagine how difficult that would become to track over time. It would be impossible and you never would ever have a clear title in Pennsylvania. That would make insuring title extraordinarily difficult. Again we discussed what they are; one thing is people are focusing on a particular type that this would be by the developer for 99 years. But as I look at it, the first thing I thought of, is gosh I sold my house five times why didn't I put one of these things in my deed trust or in the deed of conveyance because I'll happily knock a couple thousand dollars off of the price of my house if I can get some money every time the title is

transferred. And there is no real difference between me and the developer. If the developer is doing it to make it easier to buy property, well maybe I'm doing it to make it easier to buy property. The developer has done work on this, I've improved every house I've ever been in. I've improved it some way. So I ought to get a chunk of it too. Add that up; add that up a few times, pretty soon it's impossible to find trustors or heirs or beneficiaries or whatever category of people that has to get paid. If you are trying to find them it will eventually become impossible to do. So it is in that sense a train wreck that is going to happen and will cause significant problems in our real estate transfer industry. And as well all know that's extremely vital we know our economy would not function. If I can't move from Alaska to New Mexico or as I did from New Mexico to Alaska. Which made a lot of people happy I would mention. If I couldn't do that, it would impact the economy. Or if anybody couldn't do it, it would impact the economy. Another comparison, I don't know if it's been heard or mentioned yet but it's the equivalent of a copyrighter royalty. I build a building I get a royalty. I don't see any of these legal, any of the reasons to create a copyrighter royalty or patent that would apply to a house. They are more like the quests is; they are like the plot lines. Nobody gets a royalty for a plot line, you get a royalty or copyright for unique juxtaposition of words of light or sound that's creative. And a unique configuration of a house, not that unique, when you think Paul's cathedral maybe his decedents should get a royalty. But you know, I changed the flooring in my bathroom, if I do something unique and creative I'm not entitled to a royalty. No one would argue that I'm entitled to a royalty for that work. And it's the same thing with a house, you build a house and you sell it, you sell it and you are done. Again what would prevent subsequent sellers from imposing their own royalty or transfer fee? I can't think of anything.

Talk a little bit about the market model. The whole point of conveyances and really part of, it's not just part of our land system. But it's part of the development of freedom in this country and in others is a gradual letting go of the conditions that are imposed by government or by other institutions. We're no longer serfs so we don't have to, even though we own our land, we are not serfs so we don't have to pay the lord of the manor a certain amount of our production. In that, lots of that has created a great deal of freedom in the loss, in the usage of land. Generally we stop uses of land unless there is some sort of basic public good or common interest in property holders. And we stop restrictions on the use of land also if there are reasons such as racial sometimes religious or other types of restrictions on the use of land that are countered to public policy. Again, as been stated before title insurance companies serve a public good that is beyond the insurance that they provide. It's usually not recognized by many other than people in the title industry. I noticed it at first. Because I saw how every time we would close a file, we usually did some clean up. There was a deed that didn't get signed right or something like that. We did something. Or a quick claim deed that was needed from somebody who owned the property 10 years ago. We did something to clean it up, and I realized within three years it will be a complete mess for title companies. And because private transfer fee covenants create messes that title companies aren't going to be able to clean up you are going to have a messy public record, and you are always going to have, you are going to end up with doubt with whom owns the land, who owns the property.

As I was going over what I was going to talk about most of the things I've read, most of the arguments that were circulating in my head and getting on a piece of paper or computer were all sort of real estate related. Why would I be talking about this to the NAIC, shouldn't I be talking about this to the real estate commission. These are really public policy elements that have to do with real estate rather than insurance. And I thought why should NAIC care about this and I came up with, basically I had some reasons that I do I believe is genuinely a concern of NAIC even though it relates to something real estate and touches real estate. First of all insurance exists to reduce risk. Private transfer fee covenants increase risk and increase them in a way that you can't do anything about. You can't decrease it. You automatically have risk that title companies can't really do much about. Title insurance companies are really great at reducing the risk of a transfer. That's why none of you really worry about whether you

actually own the house. Title insurance companies have been so good to remove all doubt, in all the messy things that can happen like divorces the deaths the frauds in the states and the people who don't pay their mechanic liens and some things like that. All those kinds of things are taken care of and they are cleaned up and you don't have, and the risk to you becomes nominal. That's why the rate of claims is so low it's because it's very labor intensive and costs a lot of money but they do a good job in reducing risk.

Private transfer fee covenants because they cannot reduce, because they create risk that they eventually never will be able to be reduced are going to make properties uninsurable so it's going to give title insurance companies a choice. They are going to either have to insure property that's a risk, insure around the risk, which they do at times, they knowingly take a risk and say we realize that this is caught on title but we are going to provide insurance because we think it's a nominal risk. They will either do that, or suffer losses or they will refuse to insure certain properties. Either one is not good; the former ensuring the round risk; if you do it enough you will have solvency questions because you are going to have claims. And if you refuse, if you refuse to insure property then you make a property unmarketable. You know you can't sell you home because title insurance company's not going to insure it. Again why should NAIC care? The other issue is the risk of escrow losses are going to go up dramatically because somebody's going to, people will, you know the way, the way it's supposed to work is the title company gets money, it does the conveyances, it distributes the money, and the money they received in from the lender or other sources less the money that they pay out the day after closing should be zero, there should be nothing left with a few exceptions. Any time they have to pay money after that there is an escrow loss and they lose money. And there will always be somebody coming out of the woodwork in a situation like that. And they will end up having to pay money. That's going to affect their solvency. The other thing is the risk of not paying a private transfer fee. That can become an exclusion in a policy. We will not reinsure your property, you have a good title except we will not insure a private transfer fee. Well what that means is there is a lien now that nobody knows what the exact amount would be that could cause your house to be sold out from under you. And that again is a problem for land owners and it will make property unmarketable. The other issue is that, the other issue along those lines is the potential for insolvency for title insurers is going to increase. That means either they're going to have to raise their rates, which we don't want them to do. Or they are going to have to suffer losses and put their solvency at risk. Those are the issues that I think are important that I think the NAIC should care about. Just a brief summary, I believe that private transfer fees are bad for the economy are bad for the title insurance industry and more importantly they are bad for the public. And NAIC's role I think in stopping these is a legitimate one, it protects insurance, it protects the insurance industry, and therefore it protects the public. Thank you very much.

Alan: Thank you Jeffrey.

Does anyone on the Task Force have questions for Jeffrey, okay seeing none thank you again. We appreciate it.

Our next speaker is Kenneth Jannen from the First American Title Insurance Company, welcome Kenneth.

Kenneth: Good afternoon and thank you for the opportunity to come in and speak this afternoon. My name is Kenneth Jannen, I'm Vice President and Council and Associate Senior Underwriter Home Office Staff at First American Title Insurance Company. I am a member of New York and Florida Bars. I've been in the title insurance industry for 37 years. The reason that I am here today is ask your good offices to support transfer fee legislation in the United States to restrict transfer fee covenants. I am here

to inform you as the other gentlemen who preceded me have, as to the issues and I thank Mr. Proctor and Mr. Troutt and credit them for the discussion that they had particularly on covenants and restricts, encumbrances, particularly with regard to the functions that the title insurance industry and its related settlement service industry serves to the public.

One of the primary components of the lending industry, particularly residential lending is that there is a standardization of product that can be securitized, that there is consistency as far as the security goes for the underlying loan. In order to do that, lenders have addressed it with the use of title insurance and they have addressed it through the use of standardized title insurance forms that insure the validity and enforceability and priori of the mortgage. We do this through various products whether they be directly in the policy of title insurance itself or through endorsements. There is an expectation that an endorsement will have certain coverages, again to ensure the priority of that loan, that it won't lose priority to a matter that occurs subsequently and that there are certain kinds of covenants and restricts and encumbrances that are not going to impede the value of the security should the lender go and foreclose its mortgage later on. For instance, we give coverage in an ALTA Form Nine endorsement that there is no private charge or assessment. If there is, then it must be expressly stated in the policy so that the lender can go ahead and look and evaluate that. Of course, the lender will give its closing instructions to the settlement agent who often wears the hat of a title insurance agent as well. The lender will say "Do not fund my loan unless you are in a position to give me these certain products that assure me as to the priority of my mortgage, those products that carry those coverages through the endorsement or the policy itself."

So, in our function, in underwriting the title insurance risk, we do as Mr. Proctor outlined and Mr. Troutt, we do a search and examination of the public records. We evaluate, we scrutinize the documents that are there and evaluate and determine whether or not there are these risks to the lender. Then, we can underwrite them that way. So, we have an added cost in scrutinizing and dealing with these encumbrances that are on the title that are going to add to our cost and should we miss them, or should we not dispose of them properly through getting a release, then there is an added risk that we will have losses. There are two components of our cost that will be addressed in dealing with transfer fee covenants. One is increased search and clearance costs and the other is potential increased title insurance claims.

We have other issues that relate to the settlement services side and their function in disposing of some of these matters. For instance, if we do encounter a transfer fee covenant, what are our obligations with regard to the purchaser and the seller and the lender? The purchaser and the seller have executed a document, a purchase and sell agreement. It may have personal, financial information in it. In fact, in a sense, it is personal financial information. That information may be protected by various regulations, both on a federal and state level. So, it may be our obligation to go back to the purchaser and the seller and get a waiver or an authorization to disclose the purchase and sell agreement to the collecting agent for the transfer fee covenant. Of course, we are going to have to do that because how else other than looking at the contract is that collecting agent going to know what the purchase price is. We have the issue of giving personal financial information to the collecting agent but we also have delays involved in the process because we are going to have to get those waivers or authorizations and then we are going to have to get that document over to that collecting agent. He or she is going to evaluate it and make a determination as to what amount is due under that transfer fee covenant. Now, we are going to going back to the seller and saying, "Okay, this amount is the amount you are going to have to pay in order to transfer a marketable title to your buyer." Again, we face delays. We face increased cost on the settlement side in order to do that.

Remember, I alluded to lender closing instructions. The lender says “Don’t disperse my money unless you can give me a policy that provides these coverages.” Well, if we are not in a position to do that, if we are going to have to put an exception in the policy for this transfer fee covenant that creates a private charge or assessment, we are going to have to go back to the lender and they are going to have to re-underwrite the loan in a sense. They are going to have to make this loan based upon the appraisal, the loan to value and now, shaving off some of the value of that security because of the existence of the transfer fee covenant. So, there are going to be further delays there and some loans might not make it. Some lenders may say, okay, we had very close margins on our loan to value and we are not going to be able to allow this loan. Things are going to have to be modified. So we have delays, we have possible transactions that won’t be able to occur because of the impairment of the title essentially or the encumbrances on the title that are created by these.

Once we get back, if the lender decides to take the loan with the exception in the policy and they are comfortable with it and they advise the settlement agent in writing that the exception is acceptable, they are going to require an estoppel letter which we should have gotten in due time from the collecting agent that says when you pay me x dollars then I will provide you a release as to this transaction of the transfer fee covenant—not future transactions—but for this particular transaction. Once the transaction closes then we are going to disperse that sum to the collecting agent and we are going to have costs in following up to make sure, not only do we get the promised release but the promised release says what it needs to say and also, we are going to have to record that in the public records to maintain a marketable title in the public records. Again, there are additional costs for us and there will be additional costs for the seller because he is going to have to pay for the recording of that release. I think one of the biggest concerns is my mind is actual real world situations where there is surprise on the part of a seller once he is going to get to the closing and often times, when you sell a house, you buy another house. There is an expectation as to what you are going to get out of that closing. I fear that there are going to be times when we are at the closing with the buyer and the seller and the seller finds out that he is going to get several thousand dollars less out of closing. The furniture is on the truck and he is headed to the next closing and wants to get his kids registered at the new school. What is going to happen there? Are those closings going to be aborted, those second closings. I have looked through the internet and looked at some of the investigative reporting that I have seen around the country where the reporters have gone and they have found sub-divisions that have these transfer fee covenants that have been imposed on the sub-divisions. They have knocked on the door and spoken with the consumer and said “Did you know that this applies to your property? Did you know that when you sell, you are going to have to pay 1% back to the developer or to a trust for which the developer assigned his rights?” These consumers are surprised. They don’t know about it. I think it is unfair to the consumer to impose this on them without them understanding it and I don’t know that there is a way that many of them will clearly understand the imposition of this covenant. Again, they have already signed a contract to purchase the land. Are they going to lose their deposit once it is disclosed to them that the land they are buying is going to be encumbered by this restriction. Are they exposed or are they going to be pressured to go ahead with it by the developer and by the potential loss of their deposit or because they have to move. Are they going to accept title with these restrictions on them, notwithstanding the fact that later on, when they sell, this property is going to be less valuable to them.

Those are my comments. Those are the concerns that I have with regard to the imposition of these. Again, I ask you, use your good offices, please where you are able to take a position and oppose these, not only because they are going to increase the costs and the risks to the title insurance industry but that they are just not fair to the consumer. I think that you can play a role with regard to the state legislatures in their consideration of these. There is a model act out there that has been offered by ALTA and it has been introduced in several legislatures, passed in several. I think it is a good law. It is going to impede

these and I think again, it needs to be passed, state-by-state in fairness to the consumer. That is all I have. I welcome any questions.

Alan: Thank you, Kenneth. Any questions from the Task Force for Mr. Jannen?

Paul Hanson (MN): You don't know of any benefit to the neighborhoods where these are? Are there any benefits to the neighborhood or the house?

Kenneth: I really don't. There have been arguments that there are potential benefits if they go to the homeowners' association totally. There is an argument that if they take a certain portion, and they allocate it for charitable purposes, or for improvements to the subdivision as a whole, that is going to benefit but it depends primarily on how much of a benefit and what charitable association. As a consumer, if my funds are going to a charitable association, I would like the opportunity to decide what charity my funds are going to go to and if it is to a homeowners' association for capital improvements it seems in a way to be confiscatory to me. I think the way homeowners' associations and condominium associations have been set up previously you pay as you go and I think that it penalizes someone who is selling and leaving the condominium or leaving the homeowners association and now paying forward for purchasers after him. There have been arguments made that it will benefit the smaller community association or condominium and there may be ways to set it up so that it would seem to but I question whether it actually will and whether there is fairness there.

Paul: Okay. Setting aside the homeowners' associations and those entities where there may be arguably some benefit, for the ones Freehold has with the builders, where the money is just going to the builder or to Freehold, do you know of any benefit for those funds going to the neighborhood or the home?

Kenneth: If it is just going to the builder or just going to Freehold?

Paul: Yes

Kenneth: No, I don't.

Paul: Then do you know of any basis where this is going to improve the efficiency of the real estate transaction?

Kenneth: By improving the efficiency through the imposition of transfer fee covenants?

Paul: The transfer fees, are they going to make the real estate transaction more efficient?

Kenneth: No. I think just the opposite.

Paul: Are they going to reduce the time of real estate transaction?

Kenneth: No. I think they are going to extend the time of real estate transaction.

Paul: So basically, the argument can be made that they are just going to raise costs for the real estate transaction for a party's private benefit that has no public benefit. Correct?

Kenneth: I would agree with that.

Paul: Thank you.

Alan: Any other questions from the Task Force? Thank you Mr. Jannen. I appreciate it very much. For the sake of the recording, the previous questions were from Paul Hanson of Minnesota. Our last presenter, no stranger no stranger to this Task Force is Justin Ailes of the American Land Title Association. Welcome, Justin.

Justin: My reputation precedes me. Thanks very much for calling together this hearing this afternoon. I would like to ask that the NAIC would join the title industry in opposing these predatory fees. I would like to outline three points that have not yet been touched on this afternoon which might be useful to your making a decision in terms of which you might be able to join us in opposing these predatory fees.

First, I would like to give an overview of the title industry's advocacy on this issue. We first learned about these fees in September 2008 when a few of our members started to ask us if we had seen these fees in the past or heard of them. We had not and we had not had a great number of our members asking the same thing. About this time last year we had a great number more of our members asking if we had heard of these fees and we started to investigate. We met with Freehold senior leadership on a number of occasions to learn more about their product. We studied the issue closely. We then joined with the National Association of Realtors to design a state model legislation along with a joint editorial board for uniform real property acts. This organization is enfranchised by the Uniform Law Commission to write uniform legislation relating to real estate and so the three organizations developed draft state legislation and then ALTA and that National Association of Realtors sent that out to our state organizations and asked that during the 2010 legislative session that they introduce that legislation and get it passed. In January of this year, six states had taken action. Today, 12 additional states have banned these fees and we expect that next year an additional 20 states will have introduced and passed legislation to ban these fees as well. We didn't stop there, however. We created a coalition called the Coalition to Stop Wall Street Home Resale Fees. The reason we call it the Coalition to Stop Home Resale Fees is that as you may have heard, Freehold Capital Partners has been attempting to securitize the revenue stream that they expect to produce out of these covenants. We understand that they have attempted to do this even going to the Treasury Department and the Federal Reserve to access TARP or TALP money when they were not able to access funding from private sources.

I was going to mention the names of our coalition partners and I have it on a different piece of paper so let's just do an overview. We have pulled together the Center for Responsible Lending, Consumers Union, Veterans Organizations such as Vote Vets, a number of labor unions, Service Employees International, the AFSME, other organizations as well from the left. From the right we have pulled in the Property Rights Alliance and the Institute for Liberty. ALTA is a part of it as is the National Association of Realtors and we continue to build our members in that group. ALTA and the realtors wrote a letter to the Federal Housing Administration (FHA) asking what their policy was regarding these fees. They responded to us, indicating, that their authorizing legislation prohibits legal restrictions on conveyance therefore no FHA insured mortgage may be used to purchase a property which has one of these covenants attached to them. We asked the Federal Housing Finance Agency (FHFA) what their policy was regarding these fees. They responded by issuing a proposed guidance to Fannie Mae, Freddie Mac and the federal home loan banks which prohibited essentially any of these organizations from guaranteeing, purchasing, issuing a mortgage for a property which has a private transfer fee covenant attached to it. In the interest of getting in front of appropriate legislatures and Congress before Freehold might, we approached Congress in September simply wanting to indicate to them, you may hear from constituents who are concerned about an FHFA proposed guidance. A few of those members indicated that they would like to issue a comment letter to FHFA endorsing their proposal and a couple of them

went so far as to introduce legislation which would ban these fees under RESPA. So, I note that later on the agenda we will hear about HR 6260, The Homeowner Equity Protection Act, introduced by Maxine Waters.

Our view is that federal legislation is helpful but that this issue is really going to best addressed at the state level because it deals with real estate which is a right reserved to the states. Likewise, federal legislation will be limited because it will only affect federally related mortgages on one to four family properties. Private transfer fee covenants are applied to other properties as well. Competing federal legislation was introduced by Congressman Gingrey from Georgia. His bill would simply provide a disclosure of these fees to the consumer in a standardized form. All of the state legislation that we have been advocating for and the federal legislation that we have been advocating for is on a go forward basis. That means that covenants already in place cannot be considered necessarily unenforceable until a court rules that they are. We will be working with state attorneys general and through the legal system to ensure that in those states where transfer fee covenants have been banned that those covenants that were in affect before the legislation was passed are also declared unenforceable, null and void.

There was a reported agreement between Fidelity and Freehold which appears to be Attachment Seven to this packet. I would simply highlight that it was released on October 11 by PR Newswire. You will note that Freehold Capital Partners are the only ones that are quoted in this press release. You will note that there is no Fidelity person that has been quoted in the press release. You will note that the release indicates that earlier in the year Freehold entered into an agreement with Fidelity. That agreement occurred very early this year in the first quarter. That agreement did four things that are not indicated on this recent press release; that Fidelity would lift its ban on continuing transactions with transfer fee covenants attached to them; that they would insure these properties with these covenants attached to them with an exception to the covenant, therefore leaving consumers unprotected against Freeholds' predatory fees; that a separate disclosure would be issued and that Fidelity would not be required to collect the fee on behalf of Freehold. I didn't know this when I saw the release and had maybe the same reaction that many of you have had when you saw this release. I also did not know that anyone can post a release to PR Newswire for the cost of \$1500. I did not know that this is something that is often practiced when an organization cannot achieve earned media coverage that tilts their way and so when you would like to see something in the press when nobody will report it for you, you can pay a fee and someone will report it for you and that is what has occurred here.

The last thing I would like to mention is disclosure because this is the key defense that Freehold Capital Partners has been pushing, not only at the state level in introducing competing state legislation but also at the federal level in introducing the Gingery bill. Fee disclosure as a general public policy purpose is a legitimate and useful tool if the fee that is charged is used to reimburse a cost of a service that is provided. When there is no service that is provided and there is no cost involved in providing no service, disclosure fails to do its job as a useful public policy tool. Disclosure such as the model that Freehold has been advocating is inadequate. It does not allow the consumer to properly understand the valuation of the property which has the covenant attached to it. The reason that it fails to offer valuation disclosure is because nobody, including Freehold itself has an understanding of the real estate economics of one of these encumbrances and its affect on the valuation of the property. That valuation concern is a key concern for the title industry because the policy is issued in the amount that the mortgage is worth and the property is worth. When there are valuation challenges there are challenges that we have as well as an industry in determining the amount of coverage that should be issued to the consumer and to the policyholder. FHFA noted this as well in its guidance and therefore issued its policy concern about how valuation would affect the entire portfolio of mortgages and properties that Fannie Mae and Freddy Mac have in its portfolio and you know, the smartest folks in the real estate and regulatory world at the

federal government don't have an appreciation for the valuation and so this is a challenge that no one has a solution to.

So, I once again ask that the NAIC might be able to join us in opposing these predatory fees and I would be happy to respond to any questions. That anyone has.

Alan: Thank you Justin. Are there any questions for Justin from the Task Force? Yes, please identify yourself.

Brian Gaudiose from Virginia. Justin, I have seen, in fact I think it was in your presentation where there are some claims that you know, from developers that the property is cheaper with these covenant fees. I think I saw the number of 2% cheaper. Have you all done any analysis on that and looked to see whether in fact—I know it would be kind of hard to do it because actually the people who build it are the ones who set the prices. How would consumers know they are getting a 2% reduction? Is there any way for them to know? Is it in the contract? Have you seen anything like that/

Justin: We have any analysis on this because we cannot find any evidence that this practice is taking place. Let's say it is though for the sake of argument. You will note in page six of my written testimony, we go through the exercise which indicates, say a property has an initial value of \$250,000. We have gone an out on an average ownership cycle is about seven years so you would have three owners in 21 years. Those three owners, if they were to purchase a property with a covenant attached to it, which comes with a 2% reduction, which Freehold's materials say that this allows the developer to do, those three owners would receive a total of \$2, 123.77 in lost appreciation over those 21 years. Those three consumers would pay a total of \$9,349. 62 in additional charges paid to Freehold and their agents. So, the total cost to the consumer over a 21 year lifecycle on what otherwise would be a \$250,000 initial home purchase price is \$11,473.39. We have not seen evidence that builders are in fact discounting prices, so the cost may be higher. In fact, when you look at real estate marketing and valuation, generally, a seller of a piece of real estate will sell the property for the highest price that the market will provide. So, the concept that someone is able to discount a property, that someone would actually discount a property, seems difficult for us to understand and for many others as well.

Brian: Thank you Justin. Just one quick follow-up, just so I understand, there is no evidence that you have seen that any of this property has ever been reduced that has that has these covenant fees. There is no evidence of that and just so I am understanding, I mean, it is the developers who set the prices and so they are the ones that control that whole aspect of it and we just don't have any evidence that they in fact reduced property prices.

Justin: That is right. Freehold enters into an agreement with each of the developers that it contracts with to put these covenants on to properties whereby the developer, and let me be clear, we think the developers that are doing this are just as big a victims as anyone else because they are being duped into this snake oil sale that Freehold is doing. The developer is obligated to disclose to Freehold a legal description of each property where one of these covenants has been attached. It is required to disclose additional information about that property as well. That contract is included in our testimony today. Freehold is a privately held company. It is not required to disclose this kind of information. Freehold, and as Chuck mentioned earlier, Freehold indicates in press reports that some \$600 billion in 45 states already have these covenant fees attached to them. They know where they exist. But the only way that you and I, or the average consumer is able to discover where they exist is for someone owning a property is to try to sell it, at which point a title search occurs. There is an opportunity and I think there is a great opportunity for any regulator whose mission is to protect consumers to call on Freehold to

disclose where these covenant fees are placed. That would be a useful tool in determining where they are but also whether the price of the property has been discounted as Freehold says it has.

Brian: Thank you.

Alan: Go ahead Paul.

Paul: Are the developers required to disclose to give a discount?

Justin: Not to my knowledge.

Paul: You don't know of any body...there is no restriction out there on it being 1%, correct. It could be some other dollar amount.

Justin: Our sense of why these covenant fees are listed at 1% and why they expire after a period of 99 years and why they are designed to be assessed when a property transfer occurs is so that the incentive to oppose payment of the fee is so low that no one will oppose it. Our sense is that the 1% has been designed to skirt the legal requirements for a burden on property for an unreasonable restraint on alienation and in a court Freehold might argue that 1% is 1%, it is not an unreasonable restraint on alienation.

Paul: Is it sort of like airline baggage fees? They just get bigger and bigger over time?

Justin: If I am paying a \$500 airline ticket and I am also required to pay a \$50 baggage handling fee, you might say that. At the same time you might say that an airline baggage handling fee I am paying is for a service to be provided to me. That might be a difference in this.

Paul: Once last question. Once again, this is Paul Hanson of Minnesota. I have heard discussion by the other parties that are here about how things are going to take longer, the search is going to have to be greater. Isn't that also going to include or raise transactional costs for the title industry and hence to the consumer?

Justin: We're concerned about these fees as they exist today but what is especially concerning is that up to 99 years from now, these fees might be considered enforceable. As you know, a title search most often occurs for a marketable period of time. If title searchers would be required to go back 99 years in order to identify a Freehold covenant there might be additional costs in doing that but especially having the people trained not just to search the record, but to examine the record for 99 years, that is what is most concerning in terms of costs to the industry that would have to be passed on in some way to someone.

Alan: Yes?

Brian: One last question. Justin, have you seen anything where these fees come into play that you know of if someone passes away and then that land is inherited by the children. When does that occur? Does it occur when the children sell the property? How does that work?

Justin: That is a good question Brian. I would like to have the opportunity to follow up in writing to answer that so that I can make sure I am doing it accurately. My sense is that what our written response to that question is that a covenant fee is applied when property changes ownership. So, when a consumer

refinances their mortgage, they would not be required to pay the fee. But, when ownership of the property is transferred from one descendant to another that fee would be applied.

Alan: That last question was from Brian Gaudiose of Virginia. Any other members of the Task Force have questions for Justin?

Al: I have one question. Al Bottalico, California. I mean if, I think it was mentioned...FHA already disallows this but if Fannie and Freddie also follow suit, isn't it going to become very difficult for a perspective buyer to get financing down the road and it is going to make the property very hard to sell potentially, I would think if you know what is going to happen in the future but it seems like that puts a real cloud on a title.

Justin: Fortunately there is an out. Anyone who puts a covenant onto a property has the right to remove the covenant from the property. Joe Alderman, the CEO of Freehold Capital Partners, in fact did that to his own home. You will note that in a Forbes article they reported that fact. So, if FHFA were to pass a rule banning Fannie Mae and Freddy Mac from purchasing, insuring, guaranteeing mortgages for properties that have covenants attached to them, there would be an extraordinary incentive for builders to remove them from the properties where they have been places. In fact, in Utah a builder did that after a tv investigative report went and knocked on the doors of consumers and said you know you have to pay one of these things when you sell your home. The public pressure forced the developer to file a release on that covenant. We think there is an opportunity for this to get worked out.

Let me also mention that whether FHFA passes a rule or not, and we do expect that they will by the end of the year, we are not entirely clear what the future organizational structure of Fannie Mae and Freddie Mac will be. So, regardless of if there is federal action on this, it will be necessary for state legislatures to take action to ban these fees as well so that we can be sure that consumers won't be affected by them whether Fannie Mae or Freddie Mac are in existence or not.

Alan: Okay, any other questions? Seeing, none, thank you again Justin for your presentation. The next three items that are on our agenda are written materials for which I don't think we have speakers. The first are comments submitted by Professor Wilson Freyermuth of the University of Missouri School of Law. The second is a bill from the U.S. House Financial Services Subcommittee on Housing and Community Opportunity called the Homeowner Equity Protection Act of 2010 which deals with this issue. That bill or its inclusion here was prepared by NAIC staff. Lastly is the aforementioned press release from Freehold regarding its agreement with Fidelity. Let me ask, is there anyone in this room who wants to comment on any of these written materials that are in our packet? Yes, Bill

Bill Lacy: I don't want to comment on them. I have a question. I would assume Freehold was invited?

Alan: Yes.

Joe Bieniek: Yes, Freehold was invited to be here and I also had reached out a couple of weeks ago to two other entities asking them if they wanted to because they were not on our original list so I did some research and got in contact with them and have not heard from them.

Tamara Kopp: This is Tamara Kopp with Missouri. Was Fidelity invited to offer comments on the press release?

Alan: Not to my knowledge. Joe? Yes, Justin?

Justin: I had attempted to respond on Freehold's behalf in my testimony about the agreement that was entered in to many months ago before this was issued. If there are any questions about that, I would be happy to respond.

Bill Lacy: Yes, This is Bill Lacy. You said Freehold, did you mean...

Justin: Sorry, Fidelity. Thank you, Bill.

Alan: Now, we do have a gentleman in our audience who introduced himself to me at the start of this meeting, Jeff Moseley. Jeff, I know you are hoarse from laryngitis right now and you also potentially have materials for the Task Force. Not to embarrass you, would you be willing to just go to the mike and tell us what you want to have presented to us.

Jeff: I appreciate you giving me a few minutes. First of all, I am not an attorney. I think everybody who spoke today was. I am a developer from Georgia. I am a savvy businessman I feel. I don't feel like Freehold came to me trying to sell me snake oil. I truly believe this is a solution to a serious problem that we have currently in the economy. But just to give you more, I was not prepared to speak today so I am going to go over some notes I put together for you all.

Currently there is an estimated ten to twelve million homes in the U.S. that have these transfer fees already on them. Lennar is the biggest builder in the country that has them currently, from California to Florida. Despite decades of use, there is no evidence of harm from them being used. The critics today and I have heard it from a couple of the speakers claim that you know, the capital recovery fee is hidden. It isn't. It is always filed as a stand-alone instrument and it is easily identifiable in public records. The transfer fee appears on Schedule B of the Title commitment, exceptions to coverage, which is the exact same method of revealing HOA dues, encumbrances, etc. Another thing the critics have suggested is that the capital fees do not run with the land. If this would true, courts would reject these covenants. In reality, assessing a fee to recover a capital cost for infrastructure clearly establishes a nexus between the benefit and the burden. Another thing I heard was regarding the 99 years, critics were suggesting today that they have to look back 99 years. In the modern era this presents no problem. Ground leases and other encumbrances run for 99 years. In addition in many states the Marketable Title Act requires an abstract to be filed or the encumbrances will terminate.

I want to give you a real world example from a developer's standpoint. Everybody was up here going... First of all as far as disclosure; the title commitment would not be the first time this would show up. I myself use licensed realtors for all my transactions and that would show up on the property disclosure form that the realtor files on the property and the consumer would know that before it even gets to the closing table. Secondly, I will give you a real world example. One of my subdivisions up in Georgia, I have starter homes, roughly \$135,000. If I am able to acquire this funding through the Freehold initiative, those homes will be lowered by about \$11,000. Now, run the numbers. A consumer has a choice. You put two houses next to each other, one at \$135,000 and one \$11,000 less. Which one do you buy? You buy one without the covenant on it for \$135,000 or you can save \$11,000 in my case and these are real world numbers. I come to you here not a representative of Freehold; again, I am a developer trying to get through this real estate debacle we are in. They have a choice. Save \$11,000 now, think of the money that saves them on the real estate commission, the title insurance, the interest they are going to pay on this mortgage over the seven to ten years they are going to own this home but when they sell that home they know they have to relinquish 1% when they sell that home. It's a choice you know, that the consumer has and I have talked to hundreds of developers that are doing this. Every

one of them things this is a very good way to spread the archaic way of charging the infrastructure costs for somebody up front whereas now it is spread out over 99 years. Again, I come to you not as an attorney or representing Freehold. I am a businessman developer. I appreciate your time and will answer any questions I could.

Alan: Yes, Brian.

Brian: Brian Gaudiose with Virginia. First of all, thank you so much for coming before us. We do appreciate that. In the real world example that you used, and I have no reason to doubt you, who sets the price? You set the price, correct.

Jeff: I do.

Brian: So, it could be \$135,000 but with the covenant fees you could reduce it by \$11,000.

Jeff: Yes, sir.

Brian: But, somebody could arguably just set it at \$135,000 and still have the covenant fees.

Jeff: Well, I guess as a comparative way to look at it, let's assume you have identical subdivisions or right next to each other. All else being equal, let's say this house is \$135,000 in the competing subdivision that does not have the covenants and in my subdivision it is \$11,000 cheaper but I do have that 1% re-conveyance fee on the covenants. I guess that is the best way to compare it if I am answering your question correctly.

Brian: Yes. But I guess I am saying we just have one sub-development. One developer might say okay, I think I can reduce it by \$11,000. But another developer with that same subdivision could say "You know what? I don't think I am going to reduce by \$11,000; I am just going to keep it at \$135,000. In other words, there is nothing that prevents you from setting the price where you think you need to set the price or where you want to set the price.

Jeff: You are exactly right. But, the free market in the end is going to take over. If that developer is... Again, if we are talking about similar product, why would somebody buy his when, again, similar product, why would he buy out there with a developer that has not reduced his price by a developer that has reduced his price, wouldn't you go buy there?

Brian: Yes, but what I am trying to say is it is up to each individual developer. So, if I am building a subdivision and I want to charge covenant fees, I may not do what you are saying and say well, I can sell it for \$11,000 less because the market will still bear \$135,000.

Jeff: Yes, sir.

Brian: So, I don't have to reduce it. There is nothing that makes me reduce it. I could have both. I could sell the property for the highest value that it will do and still have the covenant fees and there is nothing that stops that from occurring.

Jeff: If the market allows it, then you are correct in that situation, yes sir.

Brian: Okay, thank you.

Alan: Thank you. Are there any other questions for Mr. Moseley from the Task Force? Yes, Bill Lacy.

Bill: Yes, just one. What I gathered implicit in your argument was the premise that these two subdivisions are in essence the same as commodities. There is a lot that goes into a house, not only location, workmanship, craftsmanship, design, access to shopping, schools and all of that. At least in the part of the country I am from in Arkansas we seldom see identical subdivisions anywhere.

Jeff: I do agree. When you have a competing subdivision, one guy may, I am just using an example, on guy may put granite and nicer trim in the house whereas the other guy doesn't. I understand that point. I guess to simplify that and in the real world you can't do that but let's put the houses next to each other. Is the consumer willing to pay? The house with the transfer fee on it is going to have to sell for less. The free market is going to dictate that. Am I making myself clear? Am I in a drowsy state from the medicine I am on here?

Bill: As you say though, we are in the real world and we unfortunately do not have the luxury of simplifying these types of situations.

Jeff: Yes, sir.

Alan: Any other questions for Mr. Moseley? Yes, Jim?

Jim: Jim Odiorne from the state of Washington. Did I understand you to say that you are able to accept these covenants with the idea that it is going to reduce your cost in some way?

Jeff: Yes sir.

Jim: And, is there also a part of the covenant fee that goes to someone besides you?

Jeff: Yes, sir, it does go to Freehold. It does go to charitable organizations. I might add that it is my understanding; I am not from Freehold, but the 5% that goes to charity goes to a local charity which they set up boards in each state to dictate where that goes, not knowing the name of it.

Jim: Okay. I think I heard you say that the benefit of the covenant and the transfer fee to the purchaser from you was that they got lower costs up front. Is that correct:

Jeff: Yes sir.

Jim: What is the benefit to the next person that sells it and the next and the next?

Jeff: That house is going to have to sell for less than that comparable house on the market so, if comparably in a different neighborhood that house is \$200,000, it is going to have to stay lower because it does have that transfer fee associated with it. The free market will take affect there.

Jim: I am sorry. I did not follow the benefit to the next seller.

Jeff: If the first homeowner, let's say they bought my house for \$11,000 less. They sell that house seven years from now. They are going to have to charge less for that house than a competing product that does not have that transfer fee associated with it unless the market does not, the free market does not in the

end does not worry about these fees in the future. I can't make that prediction but the second person will have to reap the benefit of that lower price house as well and the third and the fourth.

Jim: Okay, but you benefit every time it is sold.

Jeff: Do I benefit every time it is sold? Yes.

Jim: And Freehold benefits every time it is sold.

Jeff: The whole premise that Freehold has addressed to the developers that are in this pool is that they can securitize these things and the developer can sell off his portion of these instruments and get some very needed capital right now. I don't know anybody in the real world here... There is no capital available for developers right now. It doesn't exist. That would help the struggling real estate market and create jobs. The ripple effect would be amazing with what it would do. But, as far as the developer, my interest is selling that to Freehold, assuming Freehold does do that. They have not done that yet.

Jim: Thank you.

Bill: Just a couple more. Bill Lacy. I want to make sure I understood. You said something during your presentation about infrastructure costs being spread out over 99 years. So, in essence, how does that work, exactly? How do you... Do you not borrow as much money to pay those? Or...

Jeff: Well, if the developer's strip can be securitized as Freehold is attempting to do... Again, I am a developer, I am not Freehold. I want to be clear. Then, I will be able to reduce the price of everything in my development because that helps pay for the infrastructure cost. Right now when I have \$40,000 in a lot, for instance, I have to charge that on the first homeowner, period. That is the way it works. Whereas, if I got that income stream, I can reduce the price of that home and then each person through that 99 years is paying a little bit of that infrastructure cost, not that first person.

Bill: So, you take that, you sell it at a discount but then what you have is a future obligation that somebody has figured out the house is going to change hands every seven years over 99 years and there has got to be a projection of appreciation of the home and interest rate, they discount it all back and that is what they put in your pocket for the whole subdivision.

Jeff: I do have documentation I'd be happy to email or send to the board that shows that.

Bill: Yeah, okay but that is what you are talking about?

Jeff: Yes.

Bill: One other question in response to that. Did I hear you correctly when you said it actually saves you some cost to do this? Could you identify what those costs are? That was your question. I thought you said yes. I was just wondering what those were. You still have to pay the labor, you still have to buy the land, and you still have to service the debt. There is...

Jeff: I don't recall how I answered that question. I apologize

Bill: Okay. But, I mean there is no cost item in construction and developing and selling that you are able to forego by doing this?

Jeff: No. It still cost the same to do it. You are just getting additional funding that you are able to reduce the sales price of that product.

Bill: Okay. Thank you.

Alan: Okay, thank you. Actually we have run out of time. Mr. Moseley, I want to thank you for coming up and giving an impromptu talk. A couple of things; one, if you have a business card, give it to Joe or me. Secondly, do you have materials that you want us to share with the Task Force before it meets Tuesday morning?

Jeff: Yes, I do.

Alan: Great we will be happy to take those from you. Thank you. Next thing on our list is next steps for the Title Insurance Task Force on this matter. When we meet Tuesday morning, our time has been extended to two hours. We ill meet from 8 a.m. until 10 a.m. and on that agenda is what steps, if any, this Task Force wants to take on this matter. All that being said, I know we have another two hour meeting in this room very shortly. Is okay with everybody if I can this meeting adjourned? So be it, adjourned. Thank you all.

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