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## Private Transfer Taxes: A New Buyer's Burden

### ***Private Transfer Taxes: A New Buyer's Burden*** »

An emerging type of transfer fee can add thousands of dollars to closing costs.

SEPTEMBER 2007 | BY KELLY QUIGLEY

Alex Creel, senior vice president of government affairs for the CALIFORNIA ASSOCIATION OF REALTORS®, first heard of private transfer taxes a few years ago when he took a phone call from one of the state's local boards. The Placer County Association of REALTORS® was keeping a concerned eye on a new-home development called Fiddymment Farm in Roseville, Calif. The builders had agreed to impose private transfer fees, effective for 20 years, as part of a deal to satisfy demands from two environmental groups, the Sierra Club and the Audubon Society.

Today, Creel and others around the country are fighting an increasingly pitched battle to keep these fees from becoming commonplace as environmental groups, affordable housing organizations, and private companies become aggressive in their use of the fees as a source of revenue.

These so-called "private transfer taxes" — which are most common in California but are beginning to crop up in other states — help builders win support from organizations that otherwise would stand in the way of new developments.

It works like this: Builders agree to add a covenant to the deed of each new home that requires future buyers of the property to pay a percentage of the selling price to a designated land trust or charity.

The transfer fee rule is attached to the deed, so there's no way to reverse the requirement once it's in place. Buyer after buyer will have to fork over the appropriate amount of cash, usually about 1 percent of the home's price.

Builders are happy because it relieves them of having to spend out-of-pocket money to meet environmentalists' demands for

preserving open space, Creel says. Plus, the builder often gives the first buyer an exemption from paying the fee, making new homes easier to sell.

"I see it as legalized extortion," Creel says. "But builders are OK with the extortion because they're not paying for it—the future home buyers are."

#### **Unlikely Allies**

The Fiddymt Farm development raised fundamental questions about the appropriateness of the fees. "Our first question was: Is this legal?" says Dean Anderson, executive vice president of the Placer County Association of REALTORS®. "At its most basic level, it doesn't seem fair."

But even after learning that no laws prevented such a maneuver, Anderson couldn't rest easy. "The biggest risk is simply that there's no regulation. I could put a transfer tax on my property to benefit my retirement fund, and there's nothing anyone can do about it."

CAR began collaborating with lawmakers on a bill to regulate the fees: capping them at 1 percent of the home price, requiring funds to be used locally for public benefit, and limiting the duration of fees to 30 years, among other things.

But lawmakers faced pressure from environmentalists and builders, who said the bill's demands were unreasonably stringent. They countered CAR's efforts with a bill that offered more liberal regulations. The California association successfully fought back against that legislation, although it likely will resurface next year.

In the meantime, there continues to be no oversight on where or how proceeds can be spent, on how long a private transfer tax may be imposed, or on how the fees should be disclosed to home buyers.

#### **Cost of Doing Business?**

To understand the argument in favor of private transfer taxes, you also must understand how tough — and costly — it has become in many parts of the country for developers to get their projects approved.

In areas around Lake Tahoe, Calif., where nature reigns supreme, it's not uncommon for a builder to get hit with lawsuits claiming their developments could harm the environment and be forced to pay hefty impact fees imposed by local governments.

If builders weren't allowed to pass along those costs in a transfer fee, they'd have to make up for it by adding thousands of dollars to their homes' initial selling price, shutting out buyers, says Kimberley Dellinger, legislative advocate for the California Building Industry Association in Sacramento. "Why shouldn't the second and third buyers share the costs?" she says.

Builders claim that real estate practitioners are really just worried about preserving their commission. "REALTORS® never complain that a house is too expensive," and that's precisely what happens when builders lump all of their costs into the price of the first home, Dellinger says.

That's not the case, says Rindy Merrifield, president of the Placer County association. "Our commission on \$5,000 or \$10,000 is nothing," she says. "Our concern is that this hurts our buyers and sellers."

Merrifield doesn't argue with the fact that builders must contend with very high developer fees. "I feel for them," she says. "But at the same time, they're making a lot of money, and we don't think buyers should be covering their costs."

Supporters of private transfer fees also contend that public benefits far outweigh the extra costs for buyers. The Fiddymt Farm development will use a modest transfer fee of 0.5 percent (\$2,500 for a \$500,000 house) to raise an anticipated \$85 million. Those funds will go to a trust for preserving open land.

#### **Future Risks**

Some of those arguments may have substance, but without any oversight there are too many risks, critics say. For example, what's to stop builders from charging sky-high fees? Already, Creel is aware of fees in California that are as high as 1.75 percent, or \$8,750 for a \$500,000 house. Then there are concerns over disclosure: Is it the real estate practitioner's responsibility to investigate and disclose such fees to buyers? Will these fees show up in a title search, or will buyers be surprised at closing?

"Any time you require buyers and sellers to bring money to the closing table, you make housing less affordable," says Trey Goldman, legislative counsel for the Florida Association of REALTORS®.

Goldman says private transfer fees haven't yet become common in Florida. Nonetheless, the association is opposed to the practice

and is involved in efforts to pass legislation that would make the fees illegal or highly restricted.

Likewise, the Texas Association of REALTORS® recently helped to add an amendment to a bill that will keep private transfer fees at bay.

The fear of many REALTOR® associations is that because there's no oversight of private transfer fees, the practice will become unruly, with no centralized way to find out which properties have fees and where the funds are going.

Already, one company has sprouted in Florida to help private property owners place 1 percent transfer fees on their own homes, with the revenues from future sales serving as extra income to the household.

Controversial? "Only to people who don't know how to use a calculator," says RJon Robins, principal of Fort Lauderdale-based Freehold Licensing LLC. He says home owners with a transfer-fee covenant on their property are more likely to reduce their selling price to compensate for the fee. That reduces the debt load for the next buyer and makes the home easier to sell.

Whether the fees are imposed by developers or by home owners themselves, one thing remains true, says Merrifield of the Placer County association: "Without being regulated, private transfer fees will spread through the country like wildfire."

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