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To: All Agents Authorized to Conduct Business in the District of Columbia and First American Employees

From: Elisabeth C. Zajic, Vice President, District Manager & Senior Counsel

Subject: **DISTRICT OF COLUMBIA TENANTS' FIRST RIGHT OF PURCHASE UNDER TOPA: A NEW LAW AND UNDERWRITING GUIDELINES**

On February 16, 2005, Councilmember Jim Graham introduced Bill 16-50 in the D.C. City Council and the TOPA wars, previously confined primarily to the courts, escalated and moved into the streets of D.C., with pitched battles being waged over the sale of almost every residential building with rental accommodations located in the District of Columbia.

As a result, we now have a new law and new rules of engagement for TOPA transactions. "95/5 deals", much vilified in the Council chambers, are not often seen. The Department of Consumer and Regulatory Affairs is prohibited by the D.C. City Council from issuing any advisory opinions on TOPA issues, particularly on what may constitute a "sale" requiring TOPA notice.

Tenants and tenant organizations have a greatly increased appreciation of their own bargaining power, and outside third-party investors are proactively seeking out tenants and tenant associations to purchase assignments of tenants' rights and match existing third party contracts and/or otherwise compete for the deal. The result is that, in many TOPA deals, there are two or more claims of "matching" contracts, with all prospective purchasers claiming superior rights.

The new amendment to the existing TOPA statute, due to become effective around July 25, 2005, avoids any bright-line rule as to what constitutes a sale under TOPA, instead directing that transactions be judged in accordance with an "economic substance test" in terms of meeting the definition of sale.

As a result, we have a highly volatile business environment, and a new law which will add layers of complexity to an already complicated statute. Accordingly, we now require that you obtain written approval from this office before insuring any TOPA transaction, i.e. any transaction for the sale of improved residential real property with one or more rental accommodations.

I. TITLE INSURANCE IN TOPA TRANSACTIONS

The Tenant Opportunity to Purchase Act ("TOPA") is codified in Title IV of D.C. Act 3-86, the Rental Housing Conversion and Sale Act of 1980, as amended (the "Act"). It gives a tenant or tenants' association a first right of purchase in connection with any sale of residential real property, as "sale" is defined by the Act ("TOPA sale"). The applicable D.C. Code section is 42-3404.02.

Generally, title insurance protects against loss arising from real property interests, constructive notice of which is imparted through recording. TOPA rights are not a matter of record, and traditionally, title insurance would not provide protection against loss or damage arising from their exercise. However, under TOPA, a tenant or tenant organization claiming non-compliance with the Act will seek to set aside the transaction. If the tenant or tenant association is successful, the result will be a total failure of title. Purchasers and lenders look to the title insurance industry for protection from this risk, and we have endeavored to meet this need, on a "special risk" basis only.

All commitments for purchase transactions for property located in the District of Columbia must include the following Schedule B I requirement:

"This Company must be furnished with satisfactory proof that caption property is owner occupied, occupied by the proposed purchaser, or vacant. In the event of sale or lease of caption property, and if tenant occupied, further proof is required that the requirements of Title IV and V of D.C. Law 3-86, "Rental Housing Conversion and Sale Act of 1980" and as amended, have been complied with."

All commitments for purchase transactions for property located in the District of Columbia must include the following exception:

"Rights of tenants under the Rental Housing Conversion and Sale Act of 1980, as amended, and regulations adopted thereunder."

The same exception should appear in both owner's and lender's final policies unless you have documented your file with proof that the property is owner-occupied residential or commercial use only, or you have written authorization from this office for its deletion.

II. THE NEW LAW: THE RENTAL HOUSING CONVERSION AND SALE AMENDMENT ACT OF 2005

A. GENERAL CONSIDERATIONS

- The definition of TOPA sale shall include the transfer of an ownership interest in a corporation, partnership, limited liability company, association, trust, or other entity which owns an accommodation as its sole or principal asset, which, in effect, results in a transfer of the accommodation.
- The applicability of the Act, and the rights created thereunder, shall be determined by examining the substance of the transaction or series of transactions. A step transaction or other device entered into for the purpose of avoiding the obligation to comply with the requirements of the Act shall be construed in accordance with the substance of the transaction.

B. EXEMPT TRANSACTIONS AND “TIME-CERTAIN NOTICES”

In connection with the sale of a residential rental accommodation, if a TOPA Notice of Sale and Tenant Opportunity to Purchase is not provided to tenant(s), on the grounds that a proposed transfer is not a TOPA sale, a Notice of Transfer must be provided to each tenant in the housing accommodation and to the Mayor (DCRA). The Notice of Transfer must be sent by certified mail, overnight delivery by commercial carrier or by personal service, at least 90 days prior to the proposed date of transfer. It must contain, at a minimum, a statement of the tenant or tenant organization's rights under the Act, an accurate description of the transfer containing all material facts, the date of the proposed transfer, and the reason, if any, why the owner contends that the transfer is not a TOPA sale.

The failure to provide a Notice of Transfer or the provision of a Notice of Transfer that contains material or fraudulent misrepresentations or omissions shall create a rebuttable presumption that the transfer is a TOPA sale.

The following transactions are specifically made exempt from the definition of TOPA sale, and no Notice of Transfer is required to be given to tenants:

- Transfers by a decedent's estate, even though for consideration, to members of the decedents family, including lineal descendants of the decedent, surviving spouses or domestic partners or their lineal descendants, or trusts for the benefit of or business entities controlled by those family members, if the consideration for the transfer will pass from the decedent's estate to or solely for the benefit of charity.

- Transfers to a trustee under a bona fide deed of trust or mortgage, and foreclosure sale deeds and deeds in lieu of foreclosure.
- Transfers pursuant to tax sale or tax foreclosure.
- Bankruptcy sales.
- A transaction contemplated by a registration statement filed with the SEC prior to February 22, 1994.
- Transfers of title to an LLC pursuant to D.C. Code Section 29-1013.
- Transfers into a revocable trust, without consideration, when the transferor is the current beneficiary.
- Transfers by the trustee of a revocable trust to the beneficiary upon the death of the grantor of the trust.
- Transfers by the trustee of a revocable trust when the transfer would otherwise be exempted if made by the grantor of the trust.
- Transfers pursuant to court order or court-approved settlement.
- Transfers by eminent domain or threat thereof.

The following transactions are also exempt but nevertheless require a Notice of Transfer Pursuant to an Exemption to tenants or a tenant organization:

- Inter-vivos transfers, even though for consideration, between husband and wife, parent and child, siblings, grandparent and grandchild, or domestic partners.
- Transfers of property caused directly by a change in the form of the entity owning the property, without consideration, including transfers of interests in an entity to an LLC as contemplated by D.C. Code Section 29-1013.
- Entity interest transfers in tax credits transactions.

A tenant or duly organized tenant association has 45 days from the time the Notice of Transfer is filed with the Mayor to file a notice evidencing an intent to file a petition for relief under D.C. Code Section 42-3405.03 or 42-3405.03(a) ("Notice of Intent to File Petition"). Failure to do so timely will prevent the tenant or tenant association from asserting any TOPA rights relative to the transfer which is the subject of the Notice of Transfer. If the notice is a Notice of Transfer Pursuant to an Exemption, the time period in which a Notice of Intent to File Petition is shortened to 30 days.

A tenant or duly organized tenant organization has 30 days from the date the Notice of Intent to File Petition is filed with the Mayor to file a petition for relief. Failure to do so will preclude the tenant or tenant organization from asserting any TOPA rights relative to the transfer.

Conclusive proof of termination of a tenant or tenant organization's TOPA rights shall be constituted by the following, taken together:

- Certifications from DCRA setting forth the date of receipt of the Notice of Transfer and indicating that no Time Certain Notices from a tenant or tenant organization were received within the prescribed periods;

- An affidavit from the owner attesting to the date, content and manner of issuance of the Notice of Transfer; and
- An affidavit from the owner in compliance with the Servicemembers Civil Relief Act as to any tenant whose rights are affected by this Act.

For notice purposes, the term "tenant" shall mean the person or persons who, under the terms of the lease or any amendment or consent executed thereto, are entitled to occupy the rental unit.

Upon 5 days of request by any person, the Mayor shall provide written certifications of all notices received or not received, and copies of the notices. The certifications may be filed at the Office of the Recorder of Deeds.

Tenant organizations may form and register with the Mayor at any time, not only upon receipt of a tenant notice.

The Mayor shall issue a declaratory order within 30 days from receipt of a petition for relief. A declaratory order issued pursuant to D.C. Code sections 42-3405.03 and 42-3405.03(a) shall be the sole binding determination of TOPA rights.

A Rental Housing Conversion and Sale Act Task Force shall be established to examine all aspects of TOPA transactions.

III. CONCLUSION

Are you confused? You don't want to have to figure out what constitutes TOPA compliance, and, fortunately for you, we don't want you to. So, if you have a TOPA transaction, just phone, fax or email....we'll be here.