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New FHA Condominium Mortgage Insurance Guidelines: Should Associations Care?

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The Federal Housing Administration ("FHA") is a government agency designed to help more people buy homes. FHA provides mortgage insurance on loans made by FHA-approved lenders throughout the United States and is a division of HUD. Mortgage insurance is a policy that protects lenders against some or all of the losses on a mortgage if the borrower defaults on the mortgage.

In general, more borrowers will qualify with FHA financing than with conventional financing. FHA insured mortgages generally have lower down payments, lower closing costs, looser credit standards, and mortgage rates are typically better. FHA insured mortgages are on the rise and increased to roughly 20% of all mortgage originations in 2008.

On December 7, 2009, new FHA condominium mortgage insurance guidelines went into effect. While most of these guidelines are currently in place, some will gradually be phased in through December 31, 2010.

Some of the more noteworthy guidelines are as follows:

- Spot Approval – New FHA regulations temporarily extend the spot approval process (a loan on a single unit in an unapproved condominium project) through February 1, 2010, after which it is eliminated completely.
- Comprehensive Approval – Once the spot approval process is eliminated on February 1, 2010, all condominiums must be approved through either a HUD Review and Approval Process (HRAP) that can be initiated by an association, or the Direct Endorsement Lender Review and Approval Process (DELRAP). Once approved, an association would have to be re-certified every two years.
- Owner Occupancy – At least 50% of the units of a project must be owner-occupied or sold to owners who intend to occupy the units. (Through December 31, 2010, bank-owned properties, vacant or tenant-occupied real estate-owned properties are excluded from this calculation).
- Delinquencies – No more than 15% of the total units can be in arrears (more than 30 days past due) of their condominium association fee payments.

- Budget Review – The review must determine that the association’s budget is adequate and includes: (1) line items to ensure sufficient funding for upkeep of amenities, (2) an annual contribution to the association’s reserves amounting to at least 10% of the association’s budget, and (3) adequate funding for insurance coverage and deductibles. If documents do not meet these standards, the mortgagee may request a reserve study. The reserve study cannot be more than 12 months old.

It is important for condominium associations to keep in mind that no Federal law or Arizona statute requires the association or management to comply with these FHA guidelines or otherwise facilitate lending. Seeking FHA approval or cooperating with lenders that seek approval is entirely a matter of choice. That choice, however, will be based largely on how one philosophically views the operation of a condominium association – either the association should do whatever it takes to preserve property value (by expanding the universe of potential buyers for member-sellers) or the association should not be concerned with how non-members obtain financing. Whatever that choice may be, it is important for an association to consciously decide whether or not to be involved. Determine the “pros” and “cons” of involvement and make your decision early on so that you have answers for homeowners and home buyers when they ask about why your association is or is not “FHA-approved”.

For more information regarding these FHA guidelines or assistance with FHA approval, contact your condominium association’s legal counsel for guidance.