Outstanding Issues

FHA Condominium Rules

August 24, 2017

On September 13, 2012, HUD published Mortgagee Letter 2012-18 with temporary guidance on condominium sales. Further guidance was published on November 13, 2015 in Mortgage Letter 2015-27; and October 26, 2016 in Mortgagee Letter 2016-15. NAR had been working with HUD for years on these changes and will continue to encourage the following improvements to the rules so that more homebuyers have access to FHA if they want to buy a condo.

1) Owner-Occupancy Requirement

The owner-occupancy requirement is 50% with a temporary waiver for REOs.

Properties that can demonstrate reserve levels at 20% or higher, and less than 10% of units in arrears, HUD may approve an owner-occupancy level as low as 35%.

NAR recommends that HUD eliminate the occupancy ratio. Fannie Mae and Freddie Mac do not have an occupancy requirement. FHA's ratio greatly limits the number of condominium buildings available to credit-worthy borrowers who might want to live in a building closer to retail shops, work or public transportation options. Many of these potential homebuyers are not able to secure a conventional loan that would allow them access to homeownership in these properties. Potential homebuyers are forced to look at properties in locations or communities that don't meet their needs.

2) FHA Concentration

No more than 50% of units can be FHA insured.

NAR recommends expanding the concentration to 100%, especially for new construction. FHA is often the only financing available for many condominium buyers, especially first time or middle-income homebuyers who have limited resources for a downpayment. These are credit worthy borrowers who deserve to live in buildings and communities that meet their needs.

3) Certification Requirements

HUD softened certification language by acknowledging that associations may rely on attorney's advice for compliance with state and local condo laws. HUD also removed previous language from the project certification documents requiring associations to state whether they are aware of circumstances or conditions that may cause a mortgage to become delinquent. Penalties for false certification and/or failure to report remain at up to 30 years in prison and $1 million.

NAR recommends further easing restrictions. Thousands of condo boards still find the certification process much too complicated to even try, especially with the legal liability they face with fines and potential prison time.

4) **Delinquent HOA dues**

No more than 15% of units can be more than 60 days past due on HOA fees.

NAR recommends that no more than 15% of units be more than 90 days due, excluding REOs. REO dues are rarely received by associations in a timely fashion. Some state laws prohibit collection of delinquent assessments until 90 days past due and many association governing documents do not consider owners to be delinquent until 60-90 days.

Exceptions should also be provided when an association's budget has sufficient funds. Some associations may have compensated for delinquencies by building reserves or taking other steps to ensure that delinquencies are not impacting their financial stability.

5) **Pre-Sale Requirement**

Currently 30% of the units must be sold prior to FHA endorsement of any unit.

This can apply to each individual phase of a development, as opposed to the entire project. NAR recommends that FHA reduce or eliminate the presale requirement. With many homebuyers not being served by the private market, meeting the 30% requirement is a longer and more difficult process. Some condominium projects are at risk of remaining vacant or becoming rental properties.

6) **Investor Ownership**

A single investor can own up to 50% of the units at the time of project approval provided at least 50% of the units are conveyed or under contract as owner-occupied. Unoccupied and unsold units owned by a builder/developer are not included in the calculation of investor ownership.

NAR recommends that FHA increase the number of units a single investor can own. Builders should be exempted when renting out units prior to completion. Vacant units often deter potential buyers from purchasing in a project whereas occupied units, even as investor-owned rental units, can be a sign of strength for a project.

7) Commercial Space

Current law states that no more than 25% of a property's floor area can be commercial. Exceptions can be provided up to 50%. Requests for commercial space from 25-35% of floor area must be processed at the local level. Requests for commercial space from 35-50% must be approved by the Philadelphia HOC with significant additional documentation. Exceptions may also be made over 50%, but must be approved by the FHA Commissioner or her designee.

NAR recommends increasing allowable commercial space to 45% without requiring additional documentation and processing by the Philadelphia HOC. The current policy hinders efforts to build neighborhoods that have a mix of residential housing and businesses with access to public transit.