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Community Associations Newsletter

Congress Makes Lending in Condominium Market Easier

H.R. 3700 became law on July 29, 2016

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On July 29, 2016, President Obama signed the *Housing Opportunity Through Modernization Act of 2016* (H.R. 3700), a law which relaxes some of the existing requirements previously imposed by the Federal Housing Administration (FHA) for condominium eligibility.

In 2009, FHA and the Federal National Mortgage Association (FNMA, aka "FannieMae") announced new guidelines for approving mortgage loans involving the purchase of condominium units. These regulations significantly impacted how boards of condominium associations set policy on owner-occupancy ratios, finances, insurance, and governance. Previously, FHA and FNMA evaluated purchase loans on a unit-by-unit basis, but, in 2009, both agencies began requiring condominium associations to be approved in order for any owner in that project to refinance with FHA or FannieMae financing or to sell to a purchaser with that type of financing.

From 2009-2015, FHA loosened the guidelines in various ways, but many condominium associations still did not meet the standards.

This situation should change, at least to a degree, with the new law. While some of the provisions that were implemented previously by FHA remain the same, several of the more burdensome requirements affecting

condominium associations have been relaxed, thus allowing more condominium units to be eligible for FHA financing.

Commercial Space

Under the previous rules, no more than 25% of the total floor area could be used for commercial purposes, although FHA would consider a project with up to 35% commercial space on a case-by-case basis and up to 50% if the applicant provided additional information outlined by FHA.

Now, under the new law, the same rules still apply, but FHA is required to take into consideration factors relating to the economy of the locality where the condominium is located.

Transfer Fees

Under the previous FHA rules, transfer fees, such as a working capital contribution that a buyer of a condominium unit is required to pay to the association upon purchase, rendered the condominium ineligible due to the National Housing Act's prohibition on rules and policies that restrict the free transfer of the unit.

However, the Federal Housing Finance Agency (FHFA, the overseer of FannieMae and FreddieMac) came out a few years ago permitting transfer fees in instances where the fees are paid directly to the homeowners

association or condominium association to benefit the property.

The new law now requires FHA to adopt the same standards with respect to transfer fees as FHFA. In other words, FHA is now required to accept for eligibility condominiums that have transfer fees that directly benefit the condominium property. This change essentially enables associations to amend governing documents to require new owners to provide a capital contribution upon purchase.

Investor Ownership

Under FHA's previous rules, at least 50% of the condominium units must be owner-occupied for the condominium to be eligible for FHA certification.

Under the new law, FHA has until the end of October 2016 to issue guidance regarding the percentage of units that must be occupied by owners as a principal residence or a secondary residence for condominium eligibility. If FHA fails to meet that deadline, then the required owner-occupancy ratio is reduced from the current 50% threshold to 35% owner-occupied. While our office was preparing this memo, on September 27, 2016, FHA released proposed regulations in response to the new law. While the regulations are not in effect yet and still open for public comment, some of FHA's proposals include allowing commercial space between 25% and 60%; allowing an owner occupancy range between 25% and 75%, and allowing some condominiums to receive an exemption on a case-by-case basis. We will continue to

monitor the status of the proposed regulations.

There are still many important requirements that are unchanged by this law. For example, associations still cannot have more than 15% of their members more than 60 days delinquent in assessments. At this time, at least 10 percent of the association budget must be placed into a reserve account. The association cannot be involved in a construction defect lawsuit and must have fidelity insurance in place.

Even now, 7 years after the initiation of the federal lending requirements on associations, most condominium associations are not FHA/FNMA approved for loans. Many condominium associations cannot qualify, while other condominium associations have boards that do not view approval as a priority. Although approval is beneficial, condominium associations are not legally obligated to meet the FHA/FNMA requirements, and boards are not required to pursue FHA/FNMA approval.

The board's basic responsibilities are to maintain and preserve common areas and comply with the law and governing documents. Making sure association members have the most financing options is not the board's obligation, but it is certainly an exercise that helps the membership.

We will continue to monitor FHA's actions and report any additional changes to our clients and industry professionals.