

Rees Broome Client Alert

Federal Housing Administration Issues New Condominium Approval Regulations

By: Leslie Brown and Kristen Buck
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The Federal Housing Administration (FHA) finally published long-awaited regulations regarding condominium eligibility for FHA-insured loans. The new rules follow the proposed rules published on September 28, 2016 which arose out of the adoption of the *Housing Opportunity Through Modernization Act of 2016* (H.R. 3700) earlier that year. These new rules take effect October 15, 2019.

Overall, the new regulations loosen requirements for condominium eligibility, making access to FHA-insured financing easier for prospective purchasers.

Single-Unit Approval

Similar to the prior “spot-loan” process, the regulations allow for individual units to be eligible for FHA-insured financing in instances where the overall condominium itself is not FHA approved. In order to be eligible for single-unit approval, the unit must be completed (not under construction), must be located in a condominium with at least 5 dwelling units, and no more than 10% of the units within the condominium may already utilize FHA-insured financing in projects with 10 or more units (projects with less than 10 units, the number of FHA-insured mortgages cannot exceed 2). FHA

will be publishing guidance on how such single-unit approvals will be identified in FHA’s system.

Owner Occupancy

The new regulations reassert the acceptable owner-occupancy ratio of at least 50% of units within the condominium, while also maintaining the exception for condominiums that have been between 35% and 50% owner-occupancy when additional criteria is met.

The regulations also clarify what is meant by a “secondary residence” with respect to calculating owner occupancy. A unit that is occupied by an owner as a place of residence for any portion of the calendar year, other than as a principal residence, and such unit is not rented for a majority of a calendar year, will count towards calculating the total number of owner-occupied units.

Reserve Study

Under the current rules, annual budgets must allocate at least 10% of the budget for reserve funding. If the budget does not do so, FHA can require the association to provide a copy of a reserve study, no less

than 12 months old, to verify the status of the association's reserve funding.

Under the new regulations, FHA will accept a reserve study prepared by an independent third party that is up to 36 months old if the 10% reserve budgeting allocation is not met.

Commercial Space

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

Under the new regulations, FHA will accept a condominium with up to 35% commercial space, and will consider a project with up to 50% commercial space so long as the residential character of the condominium is maintained and additional economic criteria are met.

Recertification Time-Frame

Under the current rules, FHA's certification of a condominium project lasts for 2 years.

Under the new regulations, the recertification time period is extended to 3 years.

Other Factors

FHA still continues to require that no more than 15% of the units be delinquent in the payment of assessments and that each condominium maintain adequate fidelity and flood insurance (if the property is located within a flood zone). FHA also requires that additional information be provided if the condominium has an outstanding loan, pending litigation, or an active special assessment.

Lastly, FHA has been scrutinizing the financial health of the condominium. FHA wants to see a stable income stream over the past 2 years, with decreases no higher than 15%, and that the condominium has the ability to cover the cost of insurance premiums and deductibles. Additionally, the condominium must have financial controls in place, such as separate operating and reserve accounts, and restricting the management company from drawing or transferring funds from the reserve accounts without association approval.

If you have questions about the effects of FHA's regulations on your condominium association, please contact one of our community association attorneys.