New FHA condo financing rules squeeze sellers

Some real estate projects face resale challenges

BY **STEVE BERGSMAN**, FRIDAY, JANUARY 28, 2011.
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Back around the beginning of December 2010, there were a number of notifications in the press exclaiming Federal Housing Administration condominium requirements for recertifying projects were going to expire, which did nothing but cause a lot of people, including me, to scratch our collective heads, wondering what that was all about.

That deadline was to be Dec. 7, 2010; except when that date rolled around the FHA decided to **extend the various recertification deadlines** on a rolling basis through the end of 2010, most of 2011 and even into 2012.

Those who understood what was going on -- a group that admittedly didn't include me -- breathed a sigh of relief; everyone else was still picking at their scalps with their fingernails.

"There were 26,000 condominium developments that would have had to have been recertified by Dec. 7, 2010, and, in fact, my office sent out letters to almost every single one of these developments across the country telling them they were going to lose their approval. Most of them didn't even know," said Orest Tomaselli, CEO of White Plains, N.Y.-based National Condo Advisors LLC.

As I was also to learn, this is an important bit of knowledge for condominium managers and HOA (homeowners association) boards because it could affect individual condo sales going forward.

Condominium projects can be FHA-approved for the purposes of making FHA financing easier. Unfortunately, the process has always been a wee bit paper-intensive, and because, up until 2007, private lenders were throwing money at condo purchasers, many projects eschewed the FHA's offerings.

However, if you as a purchaser did want or need FHA financing there was something called a spot loan, which was a way to get FHA approval for the one condominium unit targeted for purchase.

Then as the mortgage crisis/economic recession rippled through the land and mortgages became more difficult to obtain, spot loans began to rain down on the condominium market and the FHA felt it was losing control of the process as it was its old certification program, so at the start of 2010 changes were implemented.

"With a spot loan, a letter went out from the mortgage company or lender to the homeowners association, and the HOA would fill out the basic information and send it back. If everything was compliant, a lender could give someone an FHA mortgage," Tomaselli explained.

"In February 2010, the FHA ended the spot loan -- replacing it was a process where every single condominium development had to have project approval, which was to be given by HUD (the U.S. Department of Housing and Urban Development), which administers the FHA, and lenders that were delegated FHA lenders."

There was another key change. In the old days, FHA approval was pretty much forever, but then it concluded projects checkmarked many years ago were probably not up-to-date in regard to compliance and needed to be recertified.

"What HUD effectively declared was the projects it approved 10 or 15 years ago were no longer compliant so it was going to rip away the approvals (any project approved before 2008 was stripped) and force the developments to go through a recertification process," Tomaselli said.

All of the condo projects that ever received FHA approval were going to have to have those certifications expire as of Dec. 7, 2010, but there were so many projects seeking recertification that it created a crush on FHA's resources to deal with it," said Kevin Britt, a Seattle attorney specializing in condo and homeowners association representation.

"The FHA extended the deadline based on when the projects originally received approval. The earliest projects were circa 1972 and had to be recertified by Dec. 31, 2010; the other projects (using five-year increments) had longer deadlines."

Now, here's the catch for homeowners associations.

"In the old days, all you had to do to was get your project approved once and it was good for life," Britt said. "What the FHA has since said was it wants to keep a closer tab on these associations. 'We want to look at you right now -- the recertification process -- and again every two years.' It's an ongoing obligation that the association has to be willing to sign up for.

"Every two years the HOA will have to go through this and the question is: Does it want to take on the obligation and ongoing expense?"

The onus had always been on the development to be compliant with FHA requirements, but in the past those necessities were minimal. Guidelines have since been considerably augmented.

For example, condo developments now have to have a reserve in the budget for maintenance and repairs equal to 10 percent of the budget. Also, new or established projects with more than 20 units are required to carry fidelity bonds/insurance for all officers, directors and employees of the association and all other persons handling funds.

There are some developments where it would cost too much money to be approved just because of the due diligence that would have to be performed in order to be compliant, said Tomaselli.

FHA-insured loans were not a huge factor in the condo market until relatively recently -- and then they became "the" major factor, Britt said. "Associations were not used to thinking about the FHA as being the only game in town. If you aren't FHA-certified, it's now something that makes your condo less attractive in terms of individual owners trying to sell a unit."

Look at this way: If you have two condo developments next door to each other and one is FHA-approved and the other isn't, the latter is at a severe disadvantage as far as marketing (and, by extension, value).

"When those condo owners want to sell their units and no one can finance," said Tomaselli, "when buyers can't get a mortgage because the development is not FHA- or Fannie Mae-compliant, that's when the pain will rise and everyone will start to scramble to become compliant."

*Steve Bergsman is a freelance writer in Arizona and author of several books. His latest book, "**After the Fall: Opportunities and Strategies for Real Estate Investing in the Coming Decade**," has been ranked as a top-selling real estate investment book for the Amazon Kindle e-reader.*