



Updated FHA Guidelines: Condo Approval Process for Single Family Housing

Legislative Update Compliments of Kipcon Inc.



In June of 2009, the Federal Housing Administration (FHA) placed Mortgagee Letter 2009-19 into effect. These regulations required community associations to have a current reserve study in order to receive FHA financing. Specifically, all condominium associations would have to have a reserve study that was no more than 12 months old and included all recent events and market conditions in order to obtain approval for lenders to issue FHA backed mortgages.

In November, Mortgagee letter 2009-46B replaced the previous regulations further updating the condominium approval process. Though less stringent, these new guidelines serve the same purpose of ensuring that adequate monies are available for the funding of capital reserves before the FHA offers financial aid.

For all case numbers dated December 7, 2009 or later, the FHA will now allow lenders to determine project eligibility. Mortgagees must review the homeowners' association budget to determine that the budget is "adequate." In addition, there are three specific requirements which must be included that relate to maintenance, replacement and insurance costs. The wording used in the document in Article 11, is as follows, "The budget must determine that the budget is adequate and:"

- Includes allocations/line items to ensure sufficient funds are available to maintain and preserve all amenities and features unique to the condominium project,
- Provides for the funding of replacement reserves for capital expenditures and deferred maintenance in an account representing at least 10% of the budget; and
- Provides adequate funding for insurance coverage and deductibles (see Section VI, Insurance Requirements).

The only FHA definition of "adequate" is that 10% of the budget be set aside for maintenance and reserves. Should the budget documents not meet these standards, the document explains that, "the mortgagee may request a reserve study to assess the financial stability of the project. The reserve study cannot be more than 12 months old. When reviewing the reserve study, consideration must be given to items that have been replaced after the time that the reserve study was completed"

In lieu of the actual budget documents, the mortgagee may rely on Fannie Mae for their Analysis of Annual Income and Expenses Operating Budget using Form 1073a. The form must be executed by a representative of the seller/servicer, owners association or management agent. Much like a reserve study, this form collects similar maintenance schedule and budgetary information.

Although there is no reference to any of the national standards for the development of a Reserve Study, the mortgagee may request a reserve study to assess the financial stability of the project. A comprehensive report of all the major common element components that will require maintenance and/or replacement, a reserve study acts as a road map for planning a community association's budget and clearly meets these FHA loan requirements.

A reserve study consists of two parts: a physical analysis and a financial analysis. The physical analysis is a component study that determines an objective forecast of building component replacements or repairs — including cost estimates that incorporate inflation. The financial analysis uses information from the component study to create a budget for your community association, anticipating future expenditures, establishing funding goals and identifying annual funding requirements.

Although the FHA is not requiring that community associations have a current reserve study, an adequate budget must be established. An association could show that its budget accounts for ongoing common area maintenance, future reserve replacements and community insurance costs, but a professional prepared reserve study will undoubtedly fulfill the budget review requirements of FHA qualification. In light of the FHA's technical budget requirements, an updated reserve study is recommended for associations looking to comply with the new regulations.

If you would like a full copy of these FHA guidelines, please contact Kipcon, Inc. at your convenience or use the following link: <http://www.hud.gov/offices/adm/hudclips/letters/mortgagee/files/09-46bml.pdf>.