

US APPROVALS

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HUD/FHA • VA • Project Review
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January, 2010 (Updated)

To: US Approvals' Clients

Re: HUD Mortgagee Letters 2009-46A & 46B.

There is no substitute for reading the ML's. Information herein is provided as a courtesy only and is subject to changes in agency policies without notice, and that interested parties will retain qualified advice of **legal counsel, property management, reserve preparer, insurance agent and lender-underwriter**.

US Approvals will continue to offer application services to clients under HRAP (HUD Review and Approval Process). The following changes will apply to US Approvals' client applications which are submitted to HUD under HRAP effective 12/7/09.

Detached (Site) Condos: Projects comprised of detached "site" condominiums no longer require HUD approval; however, VA currently continues to require VA review and approval of site condos.

VA & Fannie Mae Acceptance: Although HUD has relaxed some requirements (i.e. reserves, working capital, etal), these could have a negative consequence on the project's acceptability by VA, Fannie Mae and/or Freddie Mac.

Update:

Effective 12/7/09, VA discontinued acceptance of HUD approval.

Effective 2/1/2010, Fannie Mae will discontinue acceptance of HUD approval per the following:

This change is effective for conventional loan applications dated on or after February 1, 2010.

All conventional mortgage loans for which the lender's project acceptance was based solely on FHA-project approval must be purchased as whole loans or delivered in MBS on or before May 31, 2010.

Completion: All common elements / facilities / amenities (i.e. pool, clubhouse, parking, etc.) must be completed.

Pre-Sales: In the case of **new construction**, the pre-sale requirement defined in ML 2009-46B will be reduced temporarily to **30 percent** (from 50%). Per ML 2009-46B, the pre-sale percentage must be documented as follows:

- Copies of sales agreements and evidence that a mortgagee is willing to make the loan;
 - Evidence that units have closed and are occupied; OR
 - Information from a developer/builder that lists all of the units already sold, under contract, or closed (e.g. a spreadsheet, chart, or listing used for the company's own tracking purposes) that is accompanied by a signed certification from the developer.
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Owner-occupancy Ratios: At least 50 percent of the units of a project must be owner-occupied or sold to owners who intend to occupy the units. For proposed, under construction or projects still in their initial marketing phase, FHA will allow a minimum owner occupancy amount equal to 50 percent of the number of presold units (the minimum presales requirement of 50 percent still applies).

Vacant or tenant-occupied real estate owned (REOs), including properties that are bank owned, may be excluded from the calculation of the required owner-occupancy percentage (should be removed from both the numerator and denominator).

Owner-Occupied, Second Home, and Rentals:

Per HUD FAQ's to ML 2009-46B:

15. Can secondary residences be rented out at all during the course of the year and still be considered as secondary residences as noted in 2009-46 B?

Yes, FHA does not prohibit renting of secondary residences.

16. Can second homes (secondary residences) be included in the calculation of owner- occupancy or presale percentages?

For the purpose of calculating presale and owner-occupancy percentage only, second homes can be included as long as they are:

- not investment properties;
 - occupied by the owner for some portion of the year; and
 - meet the requirements of a valid presale as stated in ML 2009-46 B.
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24 CFR 203 § 203.18

(f) Definitions. As used in this section:

(1) **Principal residence** means the dwelling where the mortgagor maintains (or will maintain) his or her permanent place of abode, and typically spends (or will spend) the majority of the calendar year. A person may have only one principal residence at any one time.

(2) **Secondary residence** means a dwelling: (i) Where the mortgagor maintains or will maintain a part-time place of abode and typically spends (or will spend) less than a majority of the calendar year; (ii) which is not a vacation home; and (iii) which the Commissioner has determined to be eligible for insurance in order to avoid undue hardship to the mortgagor. A person may have only one secondary residence at a time.

(6) **Vacation home** means a dwelling that is used primarily for recreational purposes and enjoyment, and that is not a primary or secondary residence.

Concentration Requirements: The FHA 30% maximum concentration requirement defined in ML 2009-46B will be increased temporarily to 50 percent through 12/31/2010 (per ML 2009-46A).

Exceptions to 50 percent Concentration Level. The FHA concentration may be increased up to 100 percent if the project meets all of the basic condominium standards plus the additional items stated below:

- The project is 100 percent complete and construction has been completed for at least one year, as evidenced by issuance of the final or temporary/conditional certificate of occupancy for last unit conveyed;
- 100 percent of the units have been sold and no entity owns more than 10 percent of the units in the project (for projects with fewer than 10 units, single entity may own no more than 1 unit);
- The project's budget provides for the funding of replacement reserves for capital expenditures and deferred maintenance in an account representing at least 10% of the budget;
- Control of the Homeowners Association has transferred to the owners; and
- The owner-occupancy ratio is at least 50 percent.

Note: **New construction and conversions are not eligible for this exception.**

Delinquent Home Owners Association (HOA) Dues: No more than 15 percent of the total units can be in arrears (more than 30 days past due) of their condominium association fee payments.

Transfer of control of the Homeowners Association shall pass to the unit owners within the project no later than the latest of the following:

1. 120 days after the date by which 75 percent of the units have been conveyed to the unit purchasers;
 2. Three years after completion of the project evidenced by the first conveyance to a unit purchaser; OR
 3. The time frame established under state or local condominium laws if specific provisions regarding transfer of control exist.
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Attorney Certification: Although an Attorney Certification will no longer be required by HUD, it is advised that the Declarant obtain one, as the Declarant must certify to HUD that the project meets all requirements of 24CFR203, state and local laws.

Reserves for Replacements: The budget must include reserves equal to at least 10% of the budget. Although a reserve study may not be required by HUD, and although US Approvals will review the HOA financials, the Declarant must certify to HUD that the project meets all requirements of HUD ... “the Developer/Builder has no knowledge of circumstances or conditions that might have an adverse effect on the project or cause a mortgage secured by a unit in the project to become delinquent (including but not limited to: defects in construction; substantial disputes or dissatisfaction among unit owners about the operation of the project or the owners association; and disputes concerning unit owners; rights privileges, and obligations).”

Insurance: The insurance deductible(s) must be adequately funded to be evidenced in the HOA financials. Insurance coverage on individual units can be “walls in” coverage provided by the unit owner. HUD no longer requires the HOA to maintain blanket coverage to include the unit interiors. However, VA indicates that if the unit owners are required to maintain walls in coverage, the legal documents should affirm this.

Investor owned units: No more than ten percent (10%) of the units may be owned by one investor. This will apply to developers/builders that subsequently rent vacant and unsold units.

Right of First Refusal: Right of first refusal is permitted unless it violates discriminatory conduct under the Fair Housing Act regulation at 24 CFR part100.

Completion: All common elements / facilities / amenities (i.e. pool, clubhouse, parking, etc.) must be completed.

Legal Phasing: Legal phasing is permitted for condominium processing. It is recommended that developers submit all known phases for initial project approval. FHA will not accept market phasing in lieu of legal phasing.

For **vertical buildings**, legal phasing is acceptable if:

- a. The floors are legally phased in groupings of no less than five floors;
 - b. At least a temporary certificate of occupancy has been obtained and all common areas and amenities have been completed; AND
 - c. A third party completion bond has been obtained.
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Hazard Insurance: For forward mortgages, in cases where the master policy *does not* include interior unit coverage, including replacement of interior improvements and betterment coverage to insure improvements that the borrower may have made to the unit, the borrower must obtain a “walls-in” coverage policy (HO-6 policy).

Condominium Conversions: Conversion to condominiums occurs in those projects which involve changing the title of an existing structure generally under one title, to property that is separated into units so that the title to most units can be held separately. Changes to condominium conversion requirements are defined below:

1. The one-year waiting period requirement for conversions is eliminated;
2. In the event that FHA is insuring a mortgage on a unit and an undivided interest in the common elements on a project undergoing remodeling or rehabilitation, the entire condominium project, including the common facilities, must be 100 percent completely built before any mortgage may be endorsed. Escrow provisions will be permitted for weather related delays for common areas only.
3. Conversions of properties from non-residential or from rental, whether tenant-occupied or vacant, will be treated as new construction.

Ten-Year Warranty: In cases where a building permit and a certificate of occupancy (or its equivalent) are issued by a local jurisdiction that performs a minimum of three inspections (typically the footing, framing and final) neither an Early Start Letter nor a HUD approved ten year warranty plan is required. For those jurisdictions that do not issue a building permit (or its equivalent) prior to construction and a Certificate of Occupancy (or its equivalent) upon completion of construction, a condominium unit that is one year old or less must have either an Early Start Letter (with a minimum of three inspections by an FHA Roster Inspector) or be covered by a HUD-approved ten-year warranty plan (with a final inspection by a FHA Roster Inspector) to be eligible for high-ratio mortgage insurance. Projects are still required to be on the FHA-approved condominium list.

Recertification of Project Approvals: Condominium Project approvals will expire two years from the date of placement on the list of approved condominiums. Further participation in the program after this two-year period has expired will require recertification to determine that the project is still in compliance with HUD's owner-occupancy requirement and that no conditions currently exist which would present an unacceptable risk to FHA. In addition to the HOA financials, items that must be given consideration are:

1. Pending special assessments,
 2. Pending legal action against the condominium association, or its officers or directors, and
 3. Adequate hazard, liability insurance, and when applicable, flood insurance coverage.
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Transition Strategy: FHA will move all currently approved condominium projects to the new approval list and FHA Connection database. The following requirements are applicable based on the date of the initial project approval. Additional guidance on new data entry requirements will be issued in a separate ML.

- Projects that received approval prior to October 1, 2008, will require recertification on or before December 7, 2010.
- Projects that received approval between October 1, 2008 through December 7, 2009, will follow the recertification requirements defined in the Project Approval Section, XIII.

False Certifications: Title 18 U.S.C. 1014, provides in part that whoever knowingly and willfully makes or uses a document containing any false, fictitious, or fraudulent statement or entry, in any matter in the jurisdiction of any department or agency of the United States, shall be fined not more than \$1,000,000 or imprisoned for not more than 30 years or both. In addition, violation of this or others may result in debarment and civil liability for damages suffered by the Department.
