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By Mary Ellen Podmolik

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Chicago Tribune

CHICAGO — Buying a condominium is getting trickier for anyone who wants to put down only 3.5 percent and have the government insure their mortgage.

The issue isn't just the borrower's financial wherewithal. It's the building's, and plenty of condos no longer get a thumbs-up from the Federal Housing Administration.

Since Feb. 1, 2010, condo buyers haven't been able to secure unit-by-unit "spot" approval for FHA-backed mortgages if an entire building was not certified. Instead, the federal government set criteria to determine the financial viability of an entire building before deeming the project as FHA-approved, even if it had previously been certified. An approval lasts two years.

The number of rejected buildings is adding up, due to bad paperwork and bad balance sheets as an increasing number of condo associations struggle with rentals, short sales and foreclosures. It is jeopardizing the plans of condo sellers who rely on the FHA's stamp of approval as a marketing tool and condo buyers who either want or need an FHA-approved building.

The effects of those rejected buildings are likely to linger, particularly if more stringent down-payment requirements take effect for homebuyers, and could hamper any recovery of the housing market.

For the first nine months of 2011, the FHA's share of the overall home-purchase market was 37.4 percent nationally, but the share for condos would have been higher because FHA-insured loans are popular with condo purchasers, said Guy Cecala, CEO and publisher of Inside Mortgage Finance. "They have the most-used program out there," he said.

Since Oct. 1, 38 percent of condominium communities that have gone through the certification process have been rejected by the FHA.

"It's a critical year for buildings," said David Hartwell, a Chicago attorney who represents condo and homeowner associations. "This is a whole new world that we live in now. I see more rejections than acceptances, and the reasons I see clients rejected aren't quickly curable."

For buyers like Kristy Fender, of Chicago, FHA certification is a must-have on her list, and not just because it lets Fender and her fiancé, Dan Harvey, make a smaller down payment on a home purchase. She also figures that in approving buildings the FHA is doing the due diligence that she would otherwise have to do.

But the process has been much more complicated than Fender imagined, and she's wasted a fair amount of her time. "It's been very frustrating," Fender said. "There's a lot of wishy-washy information out there."

Fender and Harvey now plan to make an offer on a South Loop condo, but the offer will be contingent on the association getting the building certified for FHA financing. Bleeker has spoken with the building's management company.

"If sellers were aware of it, they would certainly be more proactive with their management companies and not let their certification lapse," Bleeker said. "There's a whole education curve that needs to be done here, at the buyer level and the seller level."

Many times, particularly in smaller buildings, it is a real-estate agent or lender that informs an association that its certification has expired.

In addition to not knowing about the process, a lack of knowledge of the rules and the many gray areas

within them is compounding issues for condo buildings. So, too, is not submitting all the required documentation. Many buildings are denied simply for missing or incomplete paperwork, which has led to the creation of a cottage industry of companies and attorneys that help shepherd associations through the process.

"It seems like there's always something additional that (the FHA) wants," said Steve Stenger, president of Condo Approval Professionals. "Once it expires, FHA lending stops. Lenders can't get case numbers; the FHA won't insure them. That whole section of financing dries up."

Among the specifics that the FHA looks at is that a building is 50 percent owner occupied, that no more than 10 percent of units are owned by one investor or entity, that no more than 15 percent of the units are 30 days past due on their monthly assessments, and that at least 10 percent of the association budget be set aside for capital expenditures and deferred maintenance. But some of those rules also come with a little wiggle room.

The FHA also looks at special assessments and pending litigation, two areas that can raise red flags.

The Community Association Institute believes the FHA's requirements are having a "chilling" effect on the market, and the trade group has asked for flexibility in the guidelines.

"When it comes to the condo market, that is the gateway to affordable housing, and FHA should play a critical role in that," said Andrew Fortin, a vice president at the trade group.

The FHA hopes to publish its condo-certification rules in the Federal Register this year for public comment. Among the areas that may be open to additional flexibility is the requirement that no single entity can own more than 10 percent of a building's units, a spokeswoman said.

But in the meantime, associations continue to grapple with the rules.

"There are new, more onerous guidelines to comply with, and there are definitely challenges," said Jason Will, national condominium sales manager for Wells Fargo Home Mortgage. "The smaller or self-managed homeowners association might not be aware of the guidelines changes until they have a buyer. You actually have a real transaction in jeopardy."

Some associations are deciding that the effort and the expenses tied to the application process, which can run into the thousands of dollars, aren't worth the payoff and are letting their certifications lapse. In some instances, that position reflects a bias against what are thought to be lower-caliber buyers who need the FHA's backing.

"It's the owners that are trying to sell their units versus the owners that want to live in their units," said Jonathan Bierman, a property manager at Forth Group, a condo association management company.

Many in the housing industry say that position is shortsighted, given consumer demand for FHA-backed mortgages.

"In an economy where it's difficult to sell your condo, (FHA approval) is almost imperative," said Kerry Bartell, a Buffalo Grove, Ill., attorney who represents homeowners associations. But, she noted, "We have a lot of clients that say they want to do FHA certification, and we say, 'Don't spend the money, because you're not going to make it.' "