The CAI Guide to FHA Certification

What is FHA?

The Federal Housing Administration (FHA) is a United States government agency created as part of the National Housing Act of 1934. It sets standards for construction and underwriting and insures loans made by banks and other private lenders for home building. The goals of this organization are to improve housing standards and conditions, provide an adequate home financing system through insurance of mortgage loans, and to stabilize the mortgage market.

What is an FHA Insured Loan?

An FHA insured loan is a US Federal Housing Administration mortgage insurance backed mortgage loan which is provided by an FHA-approved lender. FHA insured loans are a type of federal assistance and have historically allowed lower income Americans and first-time homebuyers to borrow money for the purchase of a home that they would not otherwise be able to afford or have the personal savings to put down a large enough down payment on the property. To obtain mortgage insurance from the Federal Housing Administration, an upfront mortgage insurance premium (UFMIP) equal to 1.75 percent of the base loan amount at closing is required, and is normally financed into the total loan amount by the lender and paid to FHA on the borrower's behalf. There is also a monthly mortgage insurance premium (MIP) which varies based on the amortization term and loan-to-value ratio.

What is FHA Certification?

FHA Certification for Condominiums is an approval process administered by the Department of Housing and Urban Development (HUD) to ensure that Condominium Associations meet established criteria to ensure that they are financially stable and managed properly. HUD uses the certification process as a management tool to assess the financial risk in insuring a homeowner's condominium loan. In practice, the certification process was created to reduce the rate of foreclosures on FHA insured loans. When FHA certifies a condominium association, loans on units within the project are eligible to be insured by FHA. FHA Certification does not mean that buyers obtain their loans from FHA. Eligible buyers of units in FHA certified associations obtain their loans from approved lenders and FHA guarantees the security of the loan.

Is the FHA Certification Process New?

Although FHA has been insuring mortgages for many years, the release of Mortgagee Letter (ML) 2009-19 on June 12, 2009 significantly changed the process by which FHA decided what communities and loans to certify. In February 2010, ML 2009-19 was implemented, eliminating the "spot loan" approval process. This process had previously assessed the homebuyer's financial viability in regards to an individual property. The elimination of the spot loan approval process was replaced with a certification requirement for the entire condominium development. In June 2011, FHA released the follow-up ML 2011-22, which effectively eliminated the Streamlined Recertification Process, making the certification process and recertification process for condominium approval identical.

Is FHA Certification Approval Important?

Although FHA Certification is not required for any condominium association, there are benefits for associations that secure FHA Certification:

● Increases the resale value of a home by broadening the pool of potential homebuyers.

● Reduces the interest rate on mortgage loans offered to potential homebuyers because of the reduced risk of foreclosure loss to the lender.

● Protects property values by increasing the overall marketability of project units in the community.

● Increases buyer pool as upwards of 60% of first-time homebuyers use an FHA loan.

● Reduces the number of vacant homes in a condominium project due to FHA loans having a lower foreclosure rate than conventional loans.

● Reduces the number of delinquent assessments in the community by factoring the ability to pay assessments into the total loan approval evaluation.

● Reduces the number of tenants in a community association because FHA insured loans require the owner to occupy the property.

● FHA loans are assumable, enabling new buyers to take over locked-in interest rates.

Does FHA Certification Expire?

Yes. FHA Certification is valid for a two-year period. Recertification may be started up to six months before the expiration date and may be completed up to six months after the expiration date. You can find out when your FHA Certification expires by visiting https://entp.hud.gov/idapp/html/condlook.cfm.

Common Misconceptions of FHA Certification

● Mortgage Insurance Premiums are not necessarily less affordable than private mortgage insurance. Although greater amount mortgages can be more expensive depending on the size of the down payment made by the borrower, on lower amount mortgages the cost differential is insignificant.

● FHA loans do not attract lower income homebuyers to a community. FHA loans were intended to help first-time homebuyers navigate the market and assist those homebuyers that have consistent income and healthy finances, but do not have a large amount set aside for a down payment. FHA is not an affordable housing program.

● FHA loans are not a reason for increases in foreclosure rates as statistics have shown that borrowers with an FHA-backed mortgage are actually less likely to default on their loan than non-FHA borrowers. FHA loans make up approximately 40% of the loan market and are an integral part of the U.S. mortgage market.

● Seeking FHA certification does not have to be a costly endeavor for an association. FHA itself charges nothing for the application. FHA certification specialists can be retained for assistance in the approval process, but fees are generally minimal.

Basic Eligibility Requirements

● **Owner Occupied** – At least 50% of the total number of units must be owner occupied.
● **Rentals** – At least one unit per complex must be available to be rented for more than 30 days.
● **Reserve Funds** – The Association must contribute at least 10% of their annual income assessments into a separate reserves account. Reserve can include capital expenditures and deferred maintenance and/or emergencies. (Approval doesn't require a specific balance, but rather the existence of a reserves account voted and documented in the Association's minutes.)
● **Special Assessments** – May be okay but application must be accompanied by a detailed explanation letter.
● **Pending Litigation** – May be okay but application must be accompanied by a detailed explanation letter and documentation from the court and/or attorney.
● **Master Insurance** – Must contain 100% replacement cost coverage and at least $1 million in liability protection for bodily injury and damages.
● **Fidelity Insurance** – Must be in place for complexes with 20 units or more. Minimum amount must equal 3X monthly income assessments + the current reserves balance.
● **Late HOA Fees** – No more than 15% of units can be 60 days late on their HOA fees.
● **Flood Zone** – If project is located in a flood zone, then they must carry flood insurance.
● **Maintenance** – All required maintenance for the year has been completed.
● **Common Areas and Recreational Facilities** – Completed and not subject to additional phasing, unless the project is considered a new construction project.
must be in control of the unit owners, unless the project is considered new construction project.
● **Commercial Space** – Complex must have less than 25% commercial space.
● **Ownership Percentage** – No single entity owns more than 50% of the total number of units.
● **Usage** – Complex cannot be a hotel, apartment, timeshare, nor have any weekly rentals. Also cannot have multiple units under one deed.
● **Loan Composition** – No more than 50% of loans in community may be FHA Loans.

Minimum Required Investment

● Seller-assisted down payment assistance programs are banned under FHA
● Minimum down payment by homeowner must be 3.5% of appraised value or sales price of property; whichever is less.
● Down payment may be made from borrower's own funds or be a gift from a family member or other acceptable secondary financing source such as a government or non-profit payment program.
● Maximum loan-to-value for borrower is 96.5% of sale price or appraised value; whichever is less.
● Maximum loan-to-value on the FHA insured mortgage may not exceed 100% with the Upfront Mortgage Insurance Premium financed.
● There are no minimum loan limits, but there are maximum loan amounts which differ based on location of the property.

Applying for Approval – HRAP v. DELRAP

● There are two primary ways to apply for FHA certification; either through the HUD Review and Approval Process (HRAP) or through the Direct Endorsement Lender Review and Approval Process (DELRAP)

● HRAP project approval applications, annexations and recertification submissions are reviewed and processed by FHA staff.
● DELRAP project approval applications, annexations and recertification submissions are reviewed and processed by qualified Direct Endorsement (DE) staff.

● HRAP processing time often takes between 30-60 days for a decision.
● DELRAP processing time is variable but a decision is generally reached faster.

● HRAP rejections may be appealed. 40% of applications are rejected, but 3 out of 4 rejection are approved after appeal.
● DELRAP rejections may not be appealed. Only 10% of DELRAP apllications are rejected, but if the applicant wishes to reapply within 12 months of denial, the submission must be through one of FHA's Homeownership Centers.

Projects Eligible for Certification

● Must exist in full compliance with applicable state laws of the jurisdiction and be in good standing with stated laws in which the project is located.
● Must be a single unit condo.
● Project must be primarily residential and must contain at least two dwelling units.
● Must allow up to a 30 year term loan for purchase or refinance.
● May be detached, semi-detached, row house, walk-up, mid-rise, high-rise, manufactured housing.

Master Association vs. Sub-association

● FHA does not approve master associations – In a community association that contains multiple association levels, homeowners will often belong to a master association and a sub-association. In a multi-association existence, the master association serves a role similar to the federal government. A sub-association in turn fulfills the role of a state government. While the association may consist of sub-associations that include different structures and styles of housing, the master is often the association that maintains the architectural conformity of the association and most of the common area.

● If a community association is composed of multiple sub-associations, all sub-associations must apply for and be approved by FHA individually. This is different from Fannie Mae, which will allow a master association to carry insurance for all of the sub-associations.

● Mandatory dues are not permissible under FHA guidelines. If a master association contains an entity such as a golf course, the master association cannot require homeowners to pay club dues. If dues payments are mandatory, FHA will decline an application.

● Pooled insurance policies are not permissible under FHA guidelines. A master association may not cover the sub-associations with a joint insurance policy. FHA requires each sub-association to carry its own insurance. FHA does not have the ability to determine the individual insurance coverage breakdown of each sub-association if the policy is carried by the master association because master associations are ineligible to apply for FHA approval. This is different from Fannie Mae, which will allow a master association to carry insurance for all of the sub-associations.

Documents and Information Required to Apply for Certification

Legal Documents

● Recorded covenants, conditions and restrictions (CC&Rs/Declaration/Master Deed).
● Signed and adopted bylaws; if State law does not require signed bylaws, provide copy of applicable State statute.
● Articles of Incorporation, Articles of Association or Condominium Trust filed with the State; if State law does not require incorporation, provide copy of applicable State statute.
● Recorded plat map indicating legal description.
● Recorded condominium site plans.

Financial Documents

● Current year's budget.
● Previous year's actual year-end results (Income and Expense Statement).
● Current balance sheet to support adequacy of Budget (current balance sheet to be dated within the last 90 days).
● Reserve Study is only required if budget is deemed inadequate to support project.

Insurance Documents

● Master Flood Insurance Policy (as applicable)
● Liability Insurance
● Hazard Insurance – Master Policy
● Fidelity Bond Insurance Policy
● Current Declaration pages for all policies provided

Miscellaneous Documents

● Management Agreement - signed (if applicable); in lieu of an executed agreement, an executed (signed/dated) document defining the terms and services provided by the management company on behalf of the homeowners association may be provided.
● FEMA Flood Map (must be official FEMA Flood Map; must identify location of project on FEMA Flood Map; flood certification is acceptable to augment the FEMA Flood Map but cannot replace it).
● LOMA, LOMR or an Elevation Certificate – an Elevation Certificate may not be used for proposed or under construction projects (if applicable)

Additionally Required Information

- The current balance (within 30 days of submission) in the reserve account.
- Total number of declared legal phases within the project.
- Total number of units in declared legal phases.
- Total number of planned units within project.
- Number of owner-occupied units.
- Number of tenant occupied units
- Number of tenant occupied units owned by the developer.
- Number of units vacant and unsold
- Number of bank-owned units (REO)
- Number of investor owned units within the project
- Number of units where HOA dues (all assessments for monthly dues including parking) are >60 days delinquent (Includes REO owned units).