FHA Approval Process

As is evident from the ENews articles in May (Special Assessments... Are they Special Part I and II), I am and we are (Sentry Management) huge proponents of appropriate budgeting and building reserves.

Recently, I received part of a questionnaire from a community that is applying for or looking to renew their FHA approval. The questions that were being asked by FHA are going to be very difficult to answer because the responses are going to have a very negative effect on the outcome. The community is in a state that does not have statutory requirements for funding reserves. As a mature community, it had not planned nor budgeted for replacement of a major component in their community with a definable useful life. This component affects every owner, every owner's equity, every future sale that requires financing and puts the entire community at risk, if the component is not replaced. Because there were no reserves set aside for this component, a loan had to be obtained. In addition to the loan, additional capital was required and came from a small pool of reserves and a special assessment had to be levied to pay the difference as well as pay the principal of the loan, as the budget was not increased for the repayment of it. As part of the FHA approval process, FHA asked the following questions:

- How old is the loan?
- What was the purpose of the loan?
- What is the remaining term?
- What is the payment history of the loan?
  - Provide a 12 month payment history from the lending institution
  - Provide a copy of the current loan statement

•Has the HOA been adjusting the yearly assessment (read budget) to include the yearly loan repayment amounts?

•Has the HOA been paying for replacement or repair costs with loans?

If you had to answer these questions - especially 2, 5, and 6 - would your community pass the test?

While I am not advocating for or against FHA approval, many communities would benefit by being approved. There will be situations in buildings and communities where loans are not the norm. But in most instances, homes in your building or your community will have some type of lender involved in the transaction. These lenders will and should look at the financial situation of the association when placing a loan. Financial soundness based on adequate budget, strict collections and reserve funding are an integral part of the loan process.

If the Association is looking to be FHA approved, additional guidelines would also have to be met in order to comply with FHA requirements. They are:

•No more than 15% of your units can be delinquent for more than 30 days

•At least 50% of the units must be owner occupied

•At least 10% of the association's budget must be allocated for reserve funding

•The association must have adequate insurance coverage

•There can be no pending litigation other than routine collection activity

Whether or not your community is looking to obtain or renew their FHA Approval, the questions and guidelines stated above provide a pretty good thermometer for looking at your community to see if it could make muster. They are hard questions, but their answers may point a direction the association needs to take in order to be healthy.