MORTGAGE BANKERS ASSOCIATION

November 28, 2016

Regulations Division
Office of General Counsel
Department of Housing and Urban Development
451 7th Street S.W., Room 10276
Washington D.C. 20410-0500

RE: FR-5715-P-01 Project Approval for Single-Family Condominiums

Dear Regulations Division:

The Mortgage Bankers Association (MBA)[1] thanks the Department of Housing and Urban Development (HUD) for its efforts to improve the Federal Housing Administration's (FHA) condominium program. This program enables FHA-approved lenders to extend insured mortgage financing to one-family units in multifamily projects as affordable options for first time- and low-to-moderate income homebuyers. MBA appreciates the opportunity to comment on FHA's revisions to the condominium program and welcomes the chance to contribute to the issuance of additional written guidance in the development of clear and consistent FHA policies.

I. Background

According to MBA data, the United States will see 15.9 million additional households over the next decade consisting of 10.3 million additional owner households and 5.6 million new renter households.[2] While this demand will increase the need for all types of housing over the next decade, condominium ownership will play a key role in providing first-time home-buying opportunities and affordable alternatives to single-family detached ownership in cities, as well as down-sizing opportunities for senior borrowers. MBA supports the intent of FHA's proposed rule on condominiums to ensure financial soundness and project viability while maintaining flexibility to retain the ability to be responsive to the changing market. To this end, MBA has worked with a cross-section of diverse lenders to identify the following comments regarding the provisions of the Proposed Rule.

[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,200 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, REITs, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

[2] Lynn Fisher and Jamie Woodwell, Housing Demand: Demographics and the Numbers Behind the Coming Multi-Million Increase in Households, Mortgage Bankers Association, July 2015.

II. Recommendations

MBA supports FHA's efforts to promote safe and sustainable financing for condominium loans and to increase the efficiency of current processes, such as the streamlining of private transfer fees and the expansion of the condominium project recertification period. MBA offers the following recommendations to further improve FHA's condominium program to make it more effective and viable. Enhancing this important program will encourage more lenders to participate in FHA condominium lending and will ensure direct benefits to first-time and low-to-moderate income homebuyers.

1. <u>Private Transfer Fees</u>

Under the *Housing Opportunity Through Modernization Act of 2016* that was enacted in July 2016, HUD was mandated to streamline its regulations on private transfer fees to be consistent with those of Fannie Mae and Freddie Mac (GSEs) as set by the Federal Housing Finance Agency (FHFA). Under FHFA's final rule, made effective in July 2012, the GSEs would be allowed to accept mortgages on properties subject to private transfer fee covenants so long as they provided a direct benefit to the encumbered property.

MBA is supportive of this mandate, believing that the immediate adoption of FHFA's rule will provide consistent guidelines for the industry and will allow for an expansion of eligible projects, so long as the private transfer fees are to the benefit of the borrower (i.e. maintenance fees). MBA believes that this change will create clearer and consistent guidelines across agencies, making it easier for lenders and FHA to serve the FHA borrower.

2. <u>Application for Condominium Project Approval and Renewal of Approval</u>

MBA strongly supports FHA's proposal in § 203.43b(g) to extend the approval period for a condominium project from two years to three years. This extension, in combination with the proposal to streamline the process for recertification requests, requiring only updates to previously submitted information rather than a resubmission of all information, will decrease submission burdens on lenders as well as review burdens on HUD. MBA appreciates FHA's consideration of industry concerns regarding the recertification process, and believes that this proposal will ultimately create a more efficient and effective recertification process.

To increase the clarity around this new requirement, MBA recommends that HUD further memorialize the lenders' obligation to report *known* changes in circumstance through explicit language in the final rule. This language should mirror current guidelines that require lenders to report any known litigation, budget deficiencies, changes to association documents that may not align with eligibility requirements, and *excessive* homeowners association delinquencies that place the property in financial distress as soon as they are made known to a lender throughout the three-year approval period. A clear provision of lender reporting requirements and reporting processes will contribute to decreased risks for both lenders and HUD.

3. <u>Phasing</u>

In § 203.43b(d)(x), FHA proposes to permit only legal phasing, while individual phases must contain a sufficient number of units to be separately sustainable as required by HUD so that the insurance fund is not placed at undue risk. MBA has significant concerns regarding this new proposal due to the potential implications that it would have on new construction projects and FHA borrowers seeking units in these buildings.

MBA believes that FHA's current phasing proposal would pose substantial difficulties for both builders and lenders in new construction projects, resulting in substantial closing delays. Without pre-approvals that are currently issued for "under-construction" or proposed construction projects, a lender would not be able to order a case number until a project is approved, subsequently delaying the processing of a loan application and resulting in significant closing delays of up to 60 days. This will ultimately limit the choices for low-to-moderate income borrowers, leaving them at a disadvantage if they are seeking new construction units. This issue is further complicated by the need for additional clarity on what criteria would make a legal phase eligible due to varying state law definitions of what constitutes a phase, whether one legal phase or all phases must be complete prior to approval, and what constitutes a sufficient number of units to be considered separately sustainable.

MBA recommends that the current phasing guidelines remain as-is, specifically for new construction projects to ensure optionality and choice for the FHA borrower. MBA also recommends that FHA limit the need for contiguous criteria to only vertical buildings, as requirements for builders to construct buildings in a specific order may limit the ability of a builder to make their projects available to borrowers in a timely manner.

4. Complete and Ready for Occupancy Requirement

In addition to the above-mentioned concerns, MBA is concerned that HUD's additional proposal to require that a project or legal phase be "complete and ready for occupancy," including the completion of the infrastructure of the project or legal phase under § 203.43b(d)(4), would represent a dramatic change in building plans for new construction projects. In many instances, this proposal would significantly impact current industry practices in place for the installation of building amenities and the timing of project eligibility and approval.

Currently under FHA guidelines, master association common elements need only be "substantially complete." While many local jurisdictions require larger amenities, such as pools and clubhouses to be installed at a certain point during the construction of a project, usually when 50 percent of the units have been constructed and closed, to ensure that there are enough owners to support the expenses to maintain those amenities. By requiring "completion," MBA believes that borrowers, lenders, and builders, would experience sizeable impacts due to delays in approvals and closings due to the feasibility of construction. This will ultimately make it more difficult for an FHA borrower to obtain a unit in a new construction project.

MBA recommends that HUD allow lenders to continue with the current practice of approving proposed or under construction projects, despite the possible need for additional environmental reviews, and maintain its current guidelines. Should HUD remain concerned regarding risk management issues related to projects with amenities in place, MBA recommends that HUD require a bond or letter of credit from the builder to assure completion.

5. Direct Endorsement Lender Review and Approval Process (DELRAP)

MBA appreciates FHA's efforts to enhance and codify its DELRAP authority under the condominium program. MBA offers the following recommendations on the codification of DELRAP below:

a. Indicia of appropriate experience

Under § 203.8, FHA's proposal would require staff with "at least one year of experience in underwriting mortgages on condominiums and/or condominium project approval" to approve condominium loans. However, without further guidance to assist lenders in identifying the qualifications of reviewers through the establishment of a formal documentation process for DELRAP lenders, MBA recommends that FHA maintain its current requirement. Current guidelines only require that a lender's staff have knowledge and expertise in reviewing condominium projects and FHA already oversees the risks of DELRAP authority through quality control (QC) reviews. These QC reviews are designed to monitor the quality of a reviewer's performance and are conducted by both the lender and FHA.

Further, a DELRAP lender is ultimately responsible for the management of their staff's individual performance as a responsibility under their delegated authority. Given this responsibility, MBA believes that lenders with DELRAP authority should be able to determine the appropriate experience criteria for their staff and be provided with the discretion to make staff qualification determinations.

b. Conditional DELRAP Authority

MBA also appreciates the availability of a grant for conditional DELRAP authority, however, MBA requests further clarification on the necessary procedures for the submission of all recommended Condominium Project approvals, denials, and recertifications. Lenders request clarification on whether these items must be submitted through FHA Connection, a Homeownership Center, or through another avenue. To streamline this process, MBA recommends the establishment of one centralized resource and staff to manage the conditional DELRAP authority.

6. <u>Commercial Space/Non-Residential Space</u>

MBA supports FHA's proposal under § 203.43b(d)(vii) to adjust and/or expand commercial space requirements for FHA approved condominium projects in response to the industry's feedback on the need for additional flexibility for non-residential space. While current guidelines only permit 25 percent of the property's total floor area to be used for commercial/non-residential purposes, FHA's proposal to expand the allowable commercial space range would allow for the accommodation of additional projects eligible for FHA approval.

MBA recommends that the commercial space requirement be set between 25-50 percent, with specific guidelines to allow exceptions for projects with up to 60 percent commercial space. MBA believes that special consideration is needed when a project seeks to use more than 50 percent of a property's total floor area for commercial space due to the potential impacts of this expanded presence on the characteristics of a residential project. MBA also recommends that FHA clarify that this requirement is not a minimum, but an allowable maximum for the addition of commercial space as well as the frequency with which FHA will reexamine the commercial space requirement, how much notice will be provided to lenders when a change is made, and what criteria will be used to determine recalculations. Finally, MBA suggests that FHA further define the items that may contribute to commercial space to ensure that lenders understand what features will fall into this category to aid in the completion of accurate commercial space calculations.

7. Acceptable Minimum Levels of Owner-Occupancy

MBA strongly supports the need to ensure a sufficient level of available condominium projects that are eligible for FHA financing. To this end, MBA appreciates FHA's efforts to adjust its owner-occupancy requirements under § 203.43b(d)(ix) with an expanded owner-occupancy range and through its recent publication of Mortgagee Letter (ML) 2016-15 that allows for a decrease in the owner-occupancy level from 50 percent to 35 percent in some instances, if the project satisfies certain additional criteria.

MBA strongly supports FHA's position that owner occupants serve to stabilize the financial viability of a project and are more incentivized to cooperate with other unit owners to ensure the successful operation of a project. MBA also understands the need to expand the supply of eligible condominium projects and units to increase purchase options for FHA borrowers. To this end, MBA supports a minimum level of owner-occupancy range between 25 and 50 percent, while certain exceptions could be made for lower percentages, or for extending the range to 75 percent, as proposed by HUD based on criteria dictated in ML 2016-15. MBA also requests additional clarity regarding the frequency with which it will reexamine the owner-occupancy level, and what criteria will be used to determine recalculations.

Finally, MBA recommends that FHA establish a revised owner-occupancy calculation based on the number of the minimum allowable investment units rather than based on a subdivision of classifications for owner-occupied units, investor units, vacation homes, etc. This revised grouping would make it easier for lenders to distinguish and track the number of primary, secondary, and investor held units. Currently, lenders face significant challenges in distinguishing secondary residences from vacation homes and investor-owned units, and struggle to accurately validate and monitor these units in approved projects. By classifying units as (1) primary residences; (2) secondary residences; or (3) investor units, in line with GSE industry standards and removing the need to distinguish vacation homes from secondary residences, which most associations are not equipped to track, lenders will be able to more accurately track owner-occupancy levels and FHA will be able to better manage default risk in approved projects.

8. Single-Unit Approvals

MBA appreciates FHA's efforts to reintroduce parameters for single-unit approvals in projects that are not otherwise approved to participate in FHA financing under § 203.43b(h). We believe that this is a step in the right direction towards providing more avenues of credit access and purchase options for first-time and low-to-moderate income borrowers seeking homeownership.

However, MBA is concerned that there are not enough systemic safeguards in place to ensure that these approvals are limited to already existing projects and to minimize misuse of this program. Without further guidance and clarity regarding lender obligations, the criteria that will be used for unit approval verification, and the processes that will be in place to monitor and track these unit approvals, this program may result in unintended risk to the Mutual Mortgage Insurance (MMI) Fund, and may pose risks to borrowers seeking sustainable homeownership.

MBA recommends that FHA implement a limited review process for single-unit approvals and a screen within FHA Connection (FHAC) to collect data for FHA on spot approvals to help FHA monitor and manage these risks. Based on the current proposal, a condominium identification number would not be available for a single-unit, and without effective monitoring systems, both FHA and participating lenders will have significant difficulties determining approved unit percentages in an otherwise ineligible building.

9. Acceptable Maximum Percentages of Units with FHA-insured Mortgages

MBA appreciates FHA's efforts to adjust the acceptable minimum percentages of units with FHA-insured mortgages under § 203.43b(d)(viii) through the proposal of a range between 25 and 75 percent of the total number of units in the project. However, MBA believes that additional clarity is needed on the frequency with which HUD will adjust the allowable maximum and minimum percentages and the amount of notice that lenders will be given prior to a change in the range.

In the alternative, MBA recommends that FHA maintain its current guidelines to allow for 50 percent of the total number of units in a project with some leniency to allow for potential cancellations. In many circumstances HUD has already allowed for up to 75 percent FHA financed units in established projects based on individual project conditions and the associated risks of this flexibility are monitored and mitigated through the recertification process. MBA believes that the flexibility provided under current guidelines along with the sufficient risk mitigation provided through the recertification process remains the most effective approach to this calculation for both lenders and FHA.

III. Conclusion

FHA plays a critical role in creating access to affordable mortgage credit for many homebuyers with limited financial options. MBA values the importance of FHA's condominium program as condominium purchasing trends continue to increase. We welcome the opportunity to work with FHA to further improve its program to ensure loan quality and the development of clear standards to promote safe and sustainable financing.

MBA greatly appreciates the efforts HUD has put into developing and maintaining FHA's condominium program and urges HUD to consider the above recommendations. Should you have questions or wish to discuss these comments, please contact Tamara King, Vice President of Residential Policy and Member Engagement, at (202) 557-2758 or TKing@mba.org, or Katherine Tung, Policy Advisor of Residential Policy at (202) 557-2870 or KTung@mba.org.

Sincerely,

Stephen A. O'C

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