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Cornerstone FIRST MORTGAGE

BUYING A UNIT IN A CONDOMINIUM

ARE UNITS IN A CONDOMINIUM TREATED DIFFERENTLY FOR FINANCING THAN A SINGLE-FAMILY HOME?

The short answer is yes.

WHY?

Lenders (Banks, credit unions, mortgage bankers and brokers) SELL most of their 30 and 15 year fixed rate loans to Fannie Mae or Freddie Mac. By selling the loans lenders receive cash which they use to engage in further lending. In order to sell the loans, the loans must meet Fannie Mae and Freddie Mac standards.

WHAT IS FANNIE MAE? WHAT IS FREDDIE MAC?

Fannie and Freddie are government sponsored enterprises created by Congress. Fannie and Freddie BUY mortgage loans from lenders provided the loans “conform” to their standards. In purchasing mortgage loans, these two mortgage giants perform an important role in the nation’s housing finance system – they provide liquidity, affordability and stability to the U.S. mortgage market.

WHY DO FANNIE MAE AND FREDDIE MAC TREAT CONDOS DIFFERENTLY THAN A SINGLE-FAMILY HOME?

To Fannie Mae and Freddie Mac, units located in a condominium project present risks that are distinct from the risks associated with a single-family home. Some of the documents which must be analyzed in order to evaluate risk:

INSURANCE: To evaluate insurance risks, FNMA will look at the insurance master policy for the Association which includes but is not limited to: [1]:

- Coverage is adequate to protect the project from unexpected losses due to
    - Sufficient coverage (replacement cost) for damages due to wind, fire etc.
    - Sufficient flood insurance coverage if the property is in a flood zone
    - Coverage to protect the Association against Lawsuits against (requirement is for $1M minimum),
    - Law or Ordinance Coverage (in case condo property is damaged and needs to be rebuilt to current existing building code)
    - Fidelity Bond Insurance (to protect the association against fraudulent acts by members of the Board of Directors and association employees[1]
- BUDGET- The budget must demonstrate that the association allocates at least 10% of the annual operating budget towards reserves for replacements of major capital improvements such as building’s air conditioning system, elevators, structural repairs etc.[2]
- HOA DELINQUENCIES: A high percentage of unit owner’s delinquent in their assessments (resulting in deficient operating budgets, and higher HOA dues or sub-par maintenance)
- Associations where fraud is committed by officers
- EXISTING LITIGATION: Litigation by or against the association – resulting in unanticipated and unbudgeted costs.
- LEGAL CONDO DOCUMENTS: Inability to cure mortgage default due to restrictions in the project documents.

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[1] Not required if the condo being purchase will be the primary residence of the borrower and the down payment is 25% or greater. (Higher down payment requirements if property will be a second home or investment property)

[2] [2] Not required if the condo being purchase will be the primary residence of the borrower and the down payment is 25% or greater. (Higher down payment requirements if property will be a second home or investment property)

HOW DO I KNOW IF THE CONDO I AM PURCHASING MEETS FANNIE MAE / FREDDIE MAC'S CRITERIA?

In order to assess their risk and evaluate if the condominium project is demonstrably well managed, a standardized “Condominium Project Questionnaire” must be sent to and be filled out by the condominium association’s property manager or a member of its Board of Directors. In addition to the questionnaire, the lender will require a copy of the budget of the Association and a certificate of insurance.

Based on the information received, the project will either meet or not meet Fannie or Freddie's standards. Mortgage loans in condominium projects which do not meet their standards will not be purchased by them.

WHO PAYS FOR THE "CONDOMINIUM QUESTIONNAIRE"?

The borrower is responsible for the fee charged by the homeowner’s association to fill out the questionnaire. The fee must be paid up front and is not refundable.

I'M PUTTING A LOT OF MONEY DOWN - IS ALL OF THIS STILL NECESSARY?

Short answer is, possibly. Condominium project approvals fall under two categories:

1. <u>“Full Review”</u> (Which allows you to purchase with less down payment).
2. <u>“Limited Review”</u> (Which allows you to purchase but with higher down payment requirements”

WHAT IS THE DIFFERENCE BETWEEN THESE “REVIEWS”

<u>FULL REVIEW</u>: Project undergoes a thorough review by analyzing an extensive questionnaire, copy of most recent budget, financial statement and insurance policies . *If the project qualifies under full review, you will need less down payment to purchase (making the project more marketable).*

<u>LIMITED REVIEW:</u> In exchange for higher down payment requirements, the project undergoes a more streamlined review with fewer requirements and documentation.

WHAT DIFFERENCE IN DOWN PAYMENT REQUIREMENTS ARE WE TALKING ABOUT?

Here is a side by side comparison of down payment requirements in the State of Florida under each scenario

	FULL REVIEW Minimum Down Payment Requirement	**LIMITED REVIEW** Minimum Down Payment Requirement
PRIMARY RESIDENCE	5% 3% Low Income Programs	25%
SECOND HOME	10%	30%
INVESTOR	15%	30%

You can go directly to the Fannie Mae website to confirm https://www.fanniemae.com/content/guide/selling/b4/2.2/04.html

WHAT HAPPENS IF THE CONDO PROJECT DOESN’T MEET THE CRITERIA FOR EITHER FULL OR LIMITED REVIEW?

Condominium Projects which do not meet either of the eligibility requirements are known in the industry as “non-warrantable” meaning neither Fannie Mae nor Freddie Mac will buy the loan.

ARE THERE A LOT OF CONDOS THAT DON’T MEET THE REQUIREMENTS?

The “Full Review” approval data in South Florida is pretty abysmal – roughly 80% of the condominium projects in South Florida FAIL TO MEET the “Full Review” requirements (usually because there aren’t sufficient reserves and/or because the insurance coverage is insufficient and/or because the Association is involved in litigation). See “tips” section below.

WHAT IS A NON-WARRANTABLE CONDOMINIUM

It is the name given in the lending industry to condominium projects which do not meet Fannie or Freddie's Guidelines.
https://www.fanniemae.com/content/guide/selling/b4/2.2/04.html

Pioneer Mortgage Funding works with lenders who will do mortgages in "non warrantable" type projects. These lenders will charge higher rates of interest than Fannie Mae and Freddie Mac to compensate for the added layer of risk that they're absorbing. Alternatively, you could apply for a second mortgage to bring the first mortgage down to 75% loan to value thereby bypassing the "Full Review" requirements. Talk to your loan officer.

TIPS FOR BORROWERS LOOKING TO PURCHASE A UNIT IN A CONDO - DO THIS BEFORE YOU MAKE AN OFFER

There are things you can do at no cost to you which will help to determine if the condominium project meets guidelines**:**

1. Check Fannie Mae's website to see a list of approved condominiums: https://www.fanniemae.com/content/datagrid/condo_pud/condo_approved_projects_report-fl.pdf

2. If the condominium you are interested in is not on the list, **before you make an offer** ask your realtor to obtain and provide you with the following from the listing agent:
   a) A copy of the association's approved budget *(to see if Association has sufficient reserves)*
   b) Copies of all certificates of insurance for the association *(to see if the Association has sufficient coverage)*
   c) If there is any litigation pending – *request that your realtor obtain from the listing agent copies of any pending litigation the Association is involved in.*

[1] For a complete list of what makes a project ineligible go to: https://www.fanniemae.com/content/fact_sheet/ineligible-condo-project-characterisitics.pdf and https://www.fanniemae.com/content/fact_sheet/condo-project-review.pdf

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