



Condo Lending Best Practices

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Loan Officer and Realtor Best Practices

If you have a listing in a condo or a potential buyer purchasing in a condo:

- ▶ Provide the name of the association and city/state/zip so we can research **our internal CMG databases** and Fannie and Freddie's databases
- ▶ If possible, provide a condo questionnaire (does not need to be CMG version), budget and financials, master insurance
- ▶ If the docs above are not readily available, provide a resale disclosure, the budget and the master insurance. While a resale disclosure cannot be used in lieu of a condo questionnaire, most do have some high level information that might help (like information on special assessments, and litigation)
- ▶ We'll check the Fannie / Freddie approved/declined lists and our own internal CMG condo lists, and sometimes if the condo is approved by us or the agencies, we won't need a questionnaire or all the condo docs, other than insurance.

Guidelines on Deferred Maintenance, Critical Repairs and Special Assessments

On July 5th, Fannie Mae and Freddie Mac updated their guidelines to make what was “temporary guidelines” on deferred maintenance and special assessments permanent guidelines. The guidelines will go into effect and supersede the temporary guidelines effecting loan applications on or after 9/18/23. They did make some subtle changes to what was previously the temporary guidelines.

What’s changed:

- Fannie and Freddie now require lenders to obtain and review any structural and/or mechanical inspection report that has been completed within three years of Seller’s project review date, even if the HOA states there are no critical repairs, special assessments or code violations. **This is the biggest change.**
 - ▶ If a condo doesn’t have any structural and/or mechanical inspection report that has been completed within three years, that’s okay they don’t need to voluntarily get this type of inspection report
 - ▶ This is not to be confused with the borrower’s individual unit inspection; these inspection reports are ordered by the HOA and are project/building level reports that specifically are inspecting major structural or mechanical components
 - ▶ If the condo has an inspection report but the work was completed, the project still meets guidelines
 - ▶ If the condo has an inspection report and it shows some repairs are needed but they’re preventative in nature and the project is not suffering from any safety, structural soundness, or habitability concerns, the project still meets guidelines
 - ▶ If the condo has an inspection report and it shows some repairs are needed but they’re critical defects of major building components, the project would not meet guidelines until the repairs are 100% complete
- ▶ Ultimately, if there’s critical repairs (even if our unit is not affected) that affect safety, structural integrity, habitability, water intrusion, mold, wood rot that are not repaired, the project doesn’t meet agency guidelines.

Examples of Critical Repairs - Example 1

OBSERVATIONS

Seascape Towers condominium balconies and walkways are in in good condition overall, but the parking deck is in poor condition with frequent structural distress, even after considering the age of the structure and its location in an indisputably highly corrosive environment for over three decades. Previous structural repairs were found to remain serviceable in most instances, whereas others have failed most likely related to low quality craftsmanship or ingress of chlorides since the repair was completed. Nine Units exhibited no structural distress although unfortunately, twenty-nine Units were documented to have concrete spalling immediately adjacent to the sliding glass door opening that a high probability exists for encroachment. The balcony specific site maps denoting the observations will include an arrow pointing at the room where confirmed or suspected encroachment is anticipated to address spalling, but that disruptive intrusion will only occur if Keystone concludes the action as a necessity.

Dear Seascape Towers Owner(s):

Back in mid-2023 we became aware that a structural support beam in the SW corner of the garage was deflected and in distress. The discovery was made during the project to replace the sun deck railings, and the beam repair became a serious and urgent action item. We incorporated the cost of the beam repair into the Special Assessment that also included the repairs from Hurricanes Ian and Nicole from late 2022.

Parking Deck – A substantial amount of visible and acoustical spalling was documented at the parking deck horizontal surfaces that summed 3,212 square feet with most of it visible and the peripheries detected by sounding using the chain-drag technique. At least two generations of repairs exist with the more recent one found unsound resulting in calling them out for excavation and inspection. The quantities applied to the budget will be assigned to surface, full depth and edge repairs. Only one column spall was found at the southwest corner parapet wall, which is good news.

Examples of Critical Repairs - Example 2

some photographs to help identify and locate certain items.

BACKGROUND INFORMATION

Canal Corkran is a residential community that consists of eight, three story townhome style buildings that enclose a total of 51 units. The property was developed in 2003. The buildings consist of the following.

- 2-10 Wills Way
- 12-22 Wills Way
- 2-14 Hannah Loop
- 16-28 Hannah Loop
- 30-40 Hannah Loop
- 2-12 Nell Loop
- 14-26 Nell Loop
- 28-40 Nell Loop

Professional Relationships That Endure....Over 30 Years!

Water Intrusion ♦ Roofing ♦ Structural ♦ Architectural ♦ Pavement ♦ Warranty/Reserve Studies ♦ Litigation Support

The buildings are wood framed and faced with vinyl siding. The roofs are steeply sloped (approximately six inches per foot) and covered with architectural, fiberglass-reinforced asphalt shingles installed over nominal one-half inch thick plywood secured to wood trusses. A number of dormer roofs extend up above the main roofs and similarly feature asphalt shingle coverings.

As you know, the shingle roofs and gutters and downspouts were replaced in 2022 by Dirickson Roofing. Recent water infiltration has been experienced in several units and many of these are below the roofs, particularly around the areas where the main and dormers intersect. Repairs to the building exterior have been performed along the dormers to address the water infiltration issues; however, in some of these instances, the water infiltration has continued. We also understand that Dirickson was contacted, and they inspected the roofs and indicated that the leakage was not related to any noted roof problems.

The units with water infiltration issues are listed below.

Very helpful as to give this better understanding of what was observed by your firm.

- Could you let us know, for all units examined, is this just small surface level water intrusion with small traces of water entering through the windows and the two vent pipes noted?

THE WATER DAMAGE WE NOTED DURING OUR INSPECTIONS ASSOCIATED WITH THE ATTACHED REPORT WAS CONSIDERED MINOR TO MODERATE. IT TYPICALLY CONSISTED OF STAINS IN THE DRYWALL BELOW THE AREA OF INFILTRATION.

- And did there appear to be any further water intrusion damage?

WE DID NOT REMOVE ANY DRYWALL AS PART OF OUR WORK, SO WE CANNOT COMMENT WHETHER THERE WAS "FURTHER" WATER DAMAGE BEHIND THE DRYWALL.

Examples of Critical Repairs - Example 3

5.0 Conclusions

The balconies and stair landings at Country Lane Condominium Association, Inc. require some repairs and a consistent maintenance schedule. Many inspected balconies were found to have rotted or loose railing components, typically caused by prolonged exposure to moisture leading to decay of the wood fibers. It is recommended to replace rotted components and securely fasten loose ones to ensure the safety of the railing systems. Additionally, some balconies exhibited rotted and cracked deck boards, warranting replacement at this time. The framing components at all balconies were observed to be in good condition.

Most inspected stair landings showed signs of water intrusion at the underside of the substrate, with water stains observed on the substrate and/or framing. Cracks or gaps in the surface grout and flashing create pathways for moisture infiltration. Resealing landing surfaces with a waterproof sealant and properly sealing/flashing the edges is recommended to prevent further water intrusion. Loose or cracked stair treads were also noted at a couple of staircases, warranting repair or replacement.

Regular maintenance is crucial to preserve the balconies and stair landings from weather exposure over the years. Balcony surfaces should be resealed with a waterproof sealant every 2-3 years, and stair landing tile surfaces should also receive resealing every 2-3 years.

It should be noted that some inspected railings at the balconies did not meet current building code requirements for spacing, with the spacing between pickets and the top cap exceeding 4" in these cases. This is considered legal, non-conforming and some lenders and insurance companies are requiring that railings be brought up to code.

Following the repair recommendations listed in Section 3.0 soon will minimize the need for major repairs in the future. The next SB 326 inspection cycle should occur in 9 years.

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Overall Stair Landing



Landing surface



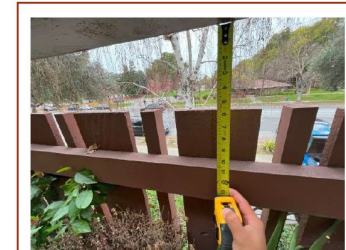
Railing is loose; repairs are recommended



Underside of landing substrate and framing show signs of water intrusion



Landing surface is not sloped to encourage drainage



Railing spacing does not meet current building code requirements

New Insurance Related Challenges

All property types have been facing more insurance related challenges based on what is available in the marketplace and the increased costs of insurance. More recently, certain markets have seen an increase of condo insurance related issues like:

- ▶ Actual Cash Value instead of Replacement Cost coverage, especially on roofs older than a certain age,
- ▶ Certain deductibles starting to exceed 5%,
- ▶ More co-insurance present,
- ▶ Limited coverage for certain perils like wind/hail or water sub-limits

Depending on the insurance issue, CMG has loan products or solutions that could still help close the transaction in projects with these characteristics.

Common Misconceptions

- ▶ We can review condo docs before we have a live loan, even pieces of the docs, before we have a live loan!
- ▶ FHA/VA approvals are free!
- ▶ Rental concentration:
 - ▶ Current Fannie/Freddie guidelines state that as long as the condo is NOT new construction or conversion, if our subject transaction is owner-occ/2nd homes, the condo can be > 50% rented (and investment property transactions are permitted at 75% LTV/CLTV or 70/75% if located in FL).
- ▶ Single Entity ownership:
 - ▶ No single entity (including developer rentals but not developer vacant units marketed for sale) can own:
 - ▶ > 2 units in a condo with 5-20 units
 - ▶ > 20% with Fannie or 25% with Freddie of the total units in a condo with 21+ units
 - ▶ Can own up to 49% IF: the subject unit is a purchase of one of the single entity owned units, there are no pending or active special assessments, the single entity is current on their HOA dues for the units they own, and the single entity confirms they do plan on selling units and retaining no more than 20% or 25% with Freddie (or retaining no more than 2 units if the condo is 5-20 units).
- ▶ Litigation:
 - ▶ Not all litigation is ineligible but if the litigation is involving repairs from defective work or insurance claims that are not 100% complete, the project is ineligible.
 - ▶ Even if the litigation is not formally filed, pre-litigation activity (like mediation or arbitration) still must be reviewed under the litigation guidelines
 - ▶ Other common litigation is personal injury lawsuits which are eligible with confirmation the insurance is defending and insurance will likely cover monetary damages should the HOA be found liable or settle
 - ▶ Or confirmation the damages will not exceed 10% of what is currently in the HOA's reserves

FHA/VA

- ▶ Detached condos do not need FHA approval but do need VA approval unless they're located in MI
- ▶ Most condos are eligible for a FHA Single Unit Approval and those approvals are slightly easier than getting a whole project approval (but we can do both)
 - ▶ FHA Single Unit Approvals are slightly easier than full project approvals within the guidelines
- ▶ VA must review the docs on all of their approval types and can take up to 30 days
- ▶ Most common issues are leasing restrictions, right of first refusal, large special assessments, budgets not contributing 10% to reserves/financials, 50% owner-occupancy on FHA only.
- ▶ Longer list of docs needed for FHA and VA approvals, we do try to set the expectation that these approvals could require a 30+ day closing.
- ▶ FHA/VA approvals are free of charge!
- ▶ They can be done on new construction condos as well, but come with more guideline requirements (conversions must go to HUD, 30% presale on FHA, 70% presale on VA but can request an exception).

New Construction/Conversions

▶ Presale

- ▶ Presale is the percentage of units sold or under contract to owner-occ/2nd home buyers.
- ▶ 50% is the requirement for conventional, FHA is only 30%
- ▶ Our non-warrantable products allow for as low as 25% and in some instances senior management can review and consider providing conventional financing at < 20% down before 50% presale is reached

▶ Phasing

- ▶ Legal phasing where the condo's CC&Rs (aka declarations and bylaws) or master deed and declaration of trust, phase an individual building or buildings can reduce the burden of presale and completion by only needing presale and completion of that phase instead of the whole project.

▶ Completion

- ▶ The entire project or phase must be substantially complete for conventional (meaning complete to drywall interior buyer selection items can be incomplete). FHA is wants a final CO

▶ Conversions

- ▶ Developer cannot be renting > 20% of the units, 50% presale (even for FHA), and project must have an engineer's report (or reserve study)

▶ PERS

- ▶ In some cases like high-rises, larger developments that cannot legally phase, or in conversions, PERS might be of value. This is a process where more documentation is submitted to Fannie Mae for review and it comes with a cost.