

## CHAPTER 6. CONVERSION TO THE CONDOMINIUM PROGRAM

- 6-1. REHABILITATION OF PROPERTIES CONTAINING 11 OR LESS UNITS.  
Section 234 of the National Housing Act makes it possible to insure mortgages in a condominium development of 11 or less units without the need for the development to have been previously insured as a project under Section 234(d) or other eligible Sections of the Act. Conventionally financed developments are thereby eligible for mortgage insurance under Section 234(c). Conventionally financed developments that have in excess of 11 units (12 or more) are ineligible for insurance under Section 234(c) unless they are substantially rehabilitated under the provisions of Section 234(d).
- a. There are many properties that could readily be converted to condominium ownership with appropriate consumer safeguards. However, it should be kept in mind that there are some speculative operators who may be attracted to the condominium concept because of its consumer characteristics, and who may attempt to use it as a "dumping ground" for undesirable properties that can no longer be found marketable for rental or investment purposes.
  - b. While there is no statutory requirement that the structures in a development with 11 or less units be rehabilitated, there is a consumer protection requirement in Section 234 that makes it necessary to require that HUD-FHA not approve a unit for consumer ownership in any development where the consumer would be exposed to extraordinary costs of repair and replacement.
  - c. The appraisal of a development, whether or not it has been previously insured by HUD-FHA, must contain an engineering report indicating which structural, electrical or mechanical components must be repaired or replaced as a condition precedent to insurance. In the event that a boiler or some other "mechanical" equipment has substantial useful life remaining, cash representing the used portion of its expected life may be escrowed for deposit in the future condominium replacement reserve in lieu of replacement. The balance of the amount necessary would be generated through the normal funding of the replacement reserve as reflected in the Annual Budget (HM 93240).

- d. In multifamily complexes, emphasis must be placed on replacement of inadequate components or systems that are buried in walls and other common areas. After the individual loans are closed all owners must sign for any loan necessary to accomplish

a repair or replacement because the security for such a loan is in their names (the Condominium Association owns no property). Painting and decoration of the interior of a unit may be passed on to the buyer as a HUD-FHA approved self-help participation plan, provided the Purchase and Sale Agreement fully discloses the fact that it is not included in the sales price and further discloses what the anticipated cost will be.

- e. Two classifications have been set up for processing purposes "Operating" condominiums and "Non-operating" condominiums. (see paragraphs 6-2. and 6-3.)

6-2. OPERATING CONDOMINIUMS (11 OR LESS UNITS).

- a. Definition. An operating condominium project is one which has been substantially filled with occupants who have title to the units they occupy, for sufficient time to demonstrate the common expense experienced in the last accounting year. The operating condominium may or may not have been previously approved for HUD-FHA mortgage insurance.

- (1) When a request is received to insure a mortgage on a unit located in an operating condominium of 11 or less units, which was not constructed with a HUD-FHA insured project mortgage, application for appraisal will be made on FHA Form 2800-1.
- (2) Legal documents for organizing the condominium (e.g. Enabling Declaration, FHA Form 3276-A, By-Laws, FHA Form 3277, Regulatory Agreement, FHA Form 3278, etc.) are to be reviewed and a determination of acceptability made before processing is begun. Amendments thereof may be necessary for these operating condominiums to be eligible.
- (3) If it is found that the condominium owners are unwilling to be subjected to a Regulatory Agreement or required amendments cannot be made, for instance, because of the inability to obtain approval of all present unit owners, further processing of the case will not be made.

7/73

Page 6-2

HUD-Wash., D. C.

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4265. 1

- b. Refer to Valuation Processing (Chapter 10) for Valuation Analysis of:

- (1) Operating Condominiums (11 or less units).
- (2) Non-operating Condominiums (11 or less units).

6-3. NON-OPERATING CONDOMINIUM (11 OR LESS UNITS).

- a. General. When an owner of a multifamily development consisting of 11 or less units, which was not constructed with a HUD-FHA insured project mortgage and it is not an operating condominium, wishes to convert the project to a condominium form of ownership, it will be necessary that an appraisal be made of the entire project, in order to arrive at a value for the single unit.
- b. Request For Appraisal. The request for an appraisal will be initiated by the owner (sponsor), or mortgagee, utilizing FHA Form 3201, "Application for Mortgage Insurance." It will not be necessary to complete Sections F, G, H, J, and K, nor are the exhibits listed in Section L necessary. Required attachments will be:
  - (1) Two copies of the proposed Master Deed or Enabling Declaration, if any available at application stage.
  - (2) Plat and Plans of the Project.
  - (3) Two copies of the By-Laws of the Association of Owners, if any available at this stage.
  - (4) Schedule of Units, FHA Form 3280-A, with Columns 1, 2, and 3 completed by the applicant.
  - (5) Two copies of proposed Regulatory Agreement, FHA Form 3278.
  - (6) The applicant will be required to pay an application fee of \$40.00 per family unit.

Upon receipt of the abbreviated FHA Form 3201, and attachments, processing will follow multifamily procedures for condominiums as described in Reference (1) of the Foreword.

7/73

Page 6-3

HUD-Wash., D. C.

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4265.1

- c. Feasibility. When the appraisal has been completed, and it has been determined that the units in the project are eligible for HUD-FHA mortgage insurance from a valuation standpoint, a feasibility letter shall be issued, conditioned upon HUD-FHA review and acceptance of the necessary legal documents establishing the condominium regime. If such documents did not accompany the application, the sponsor will be required to submit them to the field office before continuing processing of the case.
- d. Review and Approval of Condominium Documents. Upon receipt of the organizational documents (or upon completion of approval, if the organizational documents were attached to the

application) a copy of each will be referred to the HUD Area Counsel. He will compare these instruments with corresponding FHA Model Forms, and submit to the field office his comments thereon, from a legal standpoint, setting forth any amendments necessary to conform them to HUD-FHA requirements. Concurrently with the Area Counsel's review, the field office will conduct its review of the forms for their administrative acceptability. (See Paragraph 5-5, "Review of Condominium Documents" in Reference (1) of the Foreword.)

- 6-4. PROJECTS WHERE CONSTRUCTION WAS COMMENCED PRIOR TO AUGUST 1, 1968. In the case of a project comprising in excess of 11 units where construction was commenced prior to August 1, 1968, without HUD-FHA insured financing, a proposal to convert 11 or less of the units to a condominium form of ownership is acceptable where the units are so constructed as to permit such a separation into condominium ownership to be logically and feasibly made. (This would preclude hi-rise or other single structures containing in excess of 11 units)) Subsequent condominiums of 11 or less units will likewise be acceptable even though they may be a part of the same over-all housing development. Where subdivision of the property results in areas (such as parking lots) that are common to more than one separately constituted condominium, an off-site nonprofit corporation must be organized to hold title to those areas.
- 6-5. PROJECTS WHERE CONSTRUCTION WAS COMMENCED ON OR AFTER AUGUST 1 1968. Where a builder contemplates from the start the construction of a condominium development consisting of more than 11 units, but proposes to develop it on a piecemeal basis (composed of small projects of 11 or less units) he will be required to

7/73

Page 6-4

HUD-Wash., D. C.

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4265.1

proceed on a multifamily basis under Section 234(d). He would otherwise be improperly avoiding the usual HUD-FHA project conditions, such as prevailing wage requirements, cost certification, HUD-FHA construction inspections, etc. In other words, the processing will be on the basis of 12 units or more.

- 6-6. CONDITIONING THE BLANKET COMMITMENT FOR INSURANCE OF INDIVIDUAL MORTGAGES. Upon approval of the condominium organizational documents, or upon modification of appropriate instruments made necessary by the foregoing review to conform to HUD-FHA requirements, "Blanket Commitment for Insurance of Individual Mortgages," FHA Form 3275-A, conditioned for any necessary rehabilitation or repair, will be issued to the mortgagee. Thereafter, application for individual commitments will be made in the usual manner on FHA Form 2900.

Page 6-5 (and 6)

7/73

HUD-Wash., D. C.