

### News & Developments in Real Estate Law

Articles  
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## FANNIE MAE LENDING REQUIREMENTS IN THE CONTEXT OF CONDOMINIUM DEVELOPMENT

The downturn in the economy and the financial troubles of the nation's two largest mortgage finance lenders, the Federal Home Mortgage Association (Fannie Mae) and the Federal Home Mortgage Corporation (Freddie Mac), have had a significant impact on the residential real estate market. For many years, Fannie Mae has had restrictions in place governing the lending of federal funds to regional and community banks for mortgages on condominium units. However, the current real estate market, the changes in the condominium market, and Fannie Mae's recent problems have resulted in stricter requirements and enforcement. Ultimately, because a large majority of residential loans are backed by Fannie Mae, it is important that both developers and lenders of condominium projects be aware of the Fannie Mae requirements.

In November 2007, Fannie Mae shifted the obligation to internally review condominium unit loans to regional and community banks. This move proved to be problematic, as many regional or community banks were unfamiliar with the requirements or were otherwise unable to undertake such an extensive review of a particular condominium project. Initially, the delegation of the review process and the stricter requirements did not drastically affect the financing of condominium units. However, as Fannie Mae's financial problems worsened, they demanded that regional and community banks pay closer attention to the requirements. In turn, Fannie Mae's practice of backing loans that did not meet all of the requirements substantially lessened. In today's economic climate, a condominium project must meet the following Fannie Mae requirements in order for a unit purchaser to obtain the necessary Fannie Mae-backed financing:

- The project, or the subjected legal phase, must be "substantially complete," meaning that a certificate of occupancy has been issued for the project or subject phase and that all units in the building (not just the unit securing the mortgage) are complete.
- At least 70% of the total units in the project or subjected legal phase must be under a contract for purchase to owner-occupants (a 50% requirement is needed for an established project).
- Lenders must represent and warrant that the project meets applicable laws, rules, and regulations.
- Lenders must perform a review of the owners' association's budget.
- No more than 20% of the total square footage of the project may be used for nonresidential purposes.
- For existing projects, no more than 15% of the condominium/association fees may be delinquent.
- The units must be owned or leased, and the unit owners must be the sole owners of the project's facilities, common elements, and limited common elements.

The stricter enforcement of these requirements has made the securing of Fannie Mae-backed mortgages considerably more difficult and time-consuming. In a follow-up announcement issued December 16, 2008, Fannie Mae softened its position slightly and agreed to assist lenders with the review of condominium projects by introducing an in-house review service. One benefit of this new service is that once a project is approved it will be listed on Fannie Mae's website (eFannieMae.com) and can be relied on by future unit lenders. Moreover, the recent amendment clarified that Fannie Mae's owner-occupancy requirement could be met by the inclusion of lender-owned units that were purchased at foreclosure. It also provided that the owner-occupancy requirement could be waived in some instances.

While the introduction of the new review service shifts the review and approval process back to Fannie Mae, it is still very burdensome for lenders. A lender is required to submit specific information to Fannie Mae relating to the condominium's governing documents and the association's budget. Ultimately, lenders need to be certain that they have established appropriate procedures in order to comply with the Fannie Mae requirements and to ensure that appropriate and accurate information is delivered for review.

In addition to their impact on lending, the Fannie Mae requirements should be considered by developers when planning their projects. In order for units to be sold in a timely fashion, it is critical that developers comply with completion and occupancy rules on the front end. In the current market, developers should strongly consider structuring their projects in a form other than a condominium regime, or at the very least, should consider developing their project in small phases so that the Fannie Mae occupancy requirements are attainable.

## THE NEW TENNESSEE CONDOMINIUM ACT

As mentioned in a previous newsletter, on January 1, 2009, the Condominium Act ("the New Act") replaced the Horizontal Property Act ("the Old Act") with respect to the establishment and governance of condominium regimes in the State of Tennessee. Despite the change in the law, all condominiums built prior to the New Act will continue to be governed by the Old Act, unless all of the unit owners of a particular condominium project decide to be subject to the New Act. Certain provisions of the New Act, however, will apply to all condominium projects, even if the unit owners do not elect to be subject to the New Act. Therefore, it is important for developers and owners' associations to be familiar with the New Act to ensure compliance with its mandatory requirements. The relevant mandatory requirements include, but are not limited to, the following items that must be provided by the developer or association to a unit owner, purchaser, or lender within 10 days of request:

- A copy of the recorded master deed, association charter, and association bylaws
- A copy of the condominium's current rules and regulations
- The most recent balance sheet, income statement, and approved budget for the association
- Minutes of the association's meetings for the prior 24 months
- A statement of insurance coverage, including types of coverages, limits, and deductibles maintained by the association
- A statement as to whether the board of directors for the association is still under the control of the developer and, if so, when the control period expires.

While most developers and associations have always been able to provide copies of these documents to interested parties, it is now even more important that the developer and the association keep detailed accounting records and meeting minutes to ensure proper compliance.

## IN THE NEWS



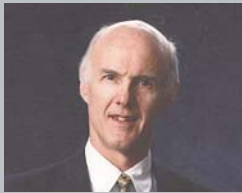
**Rachel Edwards** received a BV® Peer Review Rating from Martindale. The BV® rating indicates a high level of professional standards of conduct and ethics, reliability, diligence and other criteria relevant to the discharge of professional responsibilities. This is the highest rating a lawyer can receive who has been admitted to the Bar for 5-9 years.



**Rick Hitchcock** is listed in the *2009 Best Lawyers in America* for Energy Law. Rick is a member of the American Bar Association's Environment, Energy & Resources Section, as well as the Tennessee Bar Association's Environmental Law Section.



**Rick Hudson** is listed in the *2009 Best Lawyers in America* for Real Estate Law. Rick has been practicing law for 30 years and is a member of the American Bar Association's Real Estate Property, Probate and Trust Section.



**Nelson Irvine** is listed in the *2009 Best Lawyers in America* for Corporate Law. He has also been named the YMCA Volunteer of Year, as the recipient of the William D. Pettway Jr. Memorial Leadership Award.



**Mike St. Charles** is listed in the *2009 Best Lawyers in America* and in *Mid-South Super Lawyers* for real estate law. He recently received Chattanooga Bar Association's 2008 Albert L. Hodge Volunteer award and has been elected a Fellow of the Tennessee Bar Foundation.

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