WILL LEGISLATORS FIND A WAY TO SAVE OUR FAILING CONDOMINIUMS, HOA-GOVERNED COMMON INTEREST DEVELOPMENTS?

April 26, 2022 deborahgoonan Deferred or Indadequate Maintenance, HOA legislation, HOA, Common Interest Dysfunction & Distress, Housing Policy / Real Estate News & Trends Comments Offon Will Legislators find a way to save our failing condominiums, HOA-governed common interest developments?

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This year, several states have considered new legislation to help — or force — condominium association and HOA-governed common interest developments (CID) to better manage and finance their long-term maintenance, using reserve studies as a tool.

In Florida, Legislators attempted to enact a building safety bill requiring more frequent inspections and reserve studies, but failed, when they could not agree on the most appropriate level for reserve funding. A Colorado Legislator just dropped a reserve study bill, late into the current session. And Maryland's Legislature just enacted a new law requiring reserve studies every five years, for all homeowners, condominium, and cooperative associations in the state.

However, the rest of the states have remained relatively silent on this hot button issue. Why?

CIDs didn't plan for the future

The fact is, saving for the future and long-term sustainability of various common interest developments — condominiums, housing cooperatives, and planned communities — was never part of the plan. When these CIDs were approved, neither local governments, lenders, nor insurers required community developers or their future homeowner boards to provide documentation of a long-term maintenance plan. And efforts to ensure HOAs are doing their job have been minimal and ineffective.

And, let's be honest. CID developers often don't give a hoot about the long term viability of the CIDs they build. Their goal is short term profit on new construction sales — and perhaps slightly longer term revenue from holding onto a portion of units or amenities, generated by rental income. Most of the time, by the time multifamily buildings and private community infrastructure starts to wear out, the developer is long gone.

This leaves millions of homeowners saddled with the cost of repair and replacement, or a worse alternative — living in a deteriorating building and/or common interest development (CID).

The second piece of the puzzle, in my opinion, is the fact that common ownership of property isn't the same thing as individual ownership of one's own home, managed by local government. In CIDs, there's no "pride of ownership," because the HOA doesn't allow owners to modify or update their homes to their personal needs and tastes.

And the condominium association cannot ever seem to get all its unit owner members in agreement as to repair and replacement projects. It's like herding cats — each unit owner prefers to go in a different direction, and many of them plan to live in their condo only for a short period of time. There's little potential for condo owners to increase the value of their *building*, no matter how nice they fix up the interior of their units.

Planned obsolescence?

I want to emphasize: The HOA industry, local and state government, were never truly interested in a long-term future for condominiums and CIDs. And, for decades, the banking and finance industries didn't care either. If long-term viability and safety had been the goal, these institutions would have required a 30-year reserve and asset depreciation plan to be in place *at the time that construction was approved and permitted*.

As I have explained in a previous post, it's way too late for most HOAs to start planning for the future, because the 'future' is already here, and it's not looking good at all. Condominiums and planned communities are aging, and much of their common property and infrastructure is deteriorating. The super majority of condominium and homeowners associations have inadequate reserve accounts, and most property owners are either unable or unwilling to come up with the cash to pay for construction projects and make expensive repairs.

Many knowledgeable experts agree: there is no way to solve this problem. Therefor, the ultimate resolution will be either redevelopment OR condemnation and demolition.
But, lo and behold, the demise of run down CIDs creates potentially lucrative construction and renovation opportunities for the HOA industry. It begs a serious question that no one dares to ask. Could it be that the original creators of CIDs always contemplated their planned obsolescence?

Trade group pushing for HUD to allow FHA financing for major condo rehabs

At least since the 1970s, the era of financial institution deregulation, the real estate industry has been built on churning new construction, sales, and lease opportunities — not necessarily on building housing with pride and craftsmanship, meant to last for generations.

The leading HOA-industry trade group, CAI (Community Associations Institute) knows darn well that condo associations (and HOAs) won't be able to fund their reserve accounts and/or pay for necessary repairs. That's why they are now lobbying Congressional Legislators to allow condo owners to obtain FHA loans to help pay for the work that needs to be done. (See Twitter link)

In my opinion, there are several problems with this lame-brained idea.

First of all, very few condominiums are FHA approved. (only 6.5%, according to this article on NerdWallet) That's because FHA won't certify associations with 51% or more rental units, or with high assessment delinquency rates. They also won't back loans for uninsurable buildings. That pretty much describes the majority of condominium associations in the U.S.

Then there's the fact that some condo association members attach a negative stigma to FHA loan recipients, assuming most of them cannot afford to make regular mortgage payments, let alone HOA payments. Some say that's an unfair assumption, but others point to the mortgage foreclosure crisis of 2008, and note that many FHA borrowers defaulted on their loans. In 2020, the FHA default rate hit 11.7%.

Heaping loan payments on owners, especially seniors, will make matters worse

Even if CAI were able to convince Congress tapping FHA loans to pay for years of deferred maintenance is a good idea, it would mean that millions of owners (some of them living on fixed incomes) would have an immediate substantial increase in HOA fees and assessments. That would render the condos unaffordable, which would trigger more numerous HOA foreclosures.

My hunch is that CAI is hoping to give seniors the ability to take out a Reverse Mortgage (HECM), to help them stay in their homes, while also continuing to feed the HOA gravy train of new construction and renovation projects.

But a Reverse Mortgage under duress is a bad idea for seniors. According to the National Council on Aging (NCOA): "Reverse mortgages are best used as part of an overall retirement plan, and not when there is a pending crisis." I'd define a huge condo or HOA special assessment as a 'pending crisis,' wouldn't you?

Even if an owner manages to stay current on taxes and insurance, and to avoid foreclosure when defaulting on the HECM (reverse mortgage agreement), that owner is basically throwing away their equity and potential generational wealth, for the benefit of the condo association.

Greed driven by investors

And, let's not ignore the truth. The condo association that pushes for huge special assessments is almost always dominated by *investors*, not owner occupants. Essentially, any condo or HOA (residential or commercial) project is attractive to investors or developers, because the stakeholders can rely on a sizable portion of emotionally-attached (or economically trapped) owners to help finance their de facto rental apartment business or redevelopment project!

When the investors eventually succeed at bleeding the owners dry, the HOA will either foreclose or force a buyout upon condominium termination.

A similar tragedy is now unfolding nationwide, as investors buy up mobile home parks, proceed to hike up the rent on the land, and essentially force out low-income homeowners. The ultimate goal of real estate investors is to get a higher return on investment on the land — that can be accomplished by either selling or leasing to consumers who are able and willing to pay higher prices/rents, or, alternatively, simply bulldozing the whole place and starting anew.

Unfortunately, condominium and townhouse associations that are not built upon valuable land in a desirable location will simply continue to deteriorate to the point where they become insolvent. Then, after years of delaying the inevitable, the local government will have to step in and condemn the place.

Hopefully, residents of unsafe buildings or communities will be forced to move out before a major calamity, such as a fire or building collapse. Legislators and policy makers need more realistic goals for the millions of owners and residents of rapidly declining HOA-governed CIDs. Those goals should be to minimize overall financial distress, prevent severe loss of home equity, while also taking effective measures to avoid preventable injury and unexpected death.

Are Legislators up to the task?

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