

Renovation Lending

FHA 203(k)
Standard and Streamlined
May 30, 2007

What is a 203(k)

- **203(k) mortgage adds the cost of repairs and home improvements to the purchase or refinance a home.**
- **The new first mortgage includes the purchase price or refinanced amount PLUS the renovation costs and fees.**
- **The appraisal is based on the future value of the home after renovation.**

Benefits to the Borrower

- **Choice of location**
- **Create the home they want rather without the seller's involvement**
- **One closing with one set of closing costs**
- **The most inexpensive way to borrow for home improvements**
- **Create equity**

Benefits for Origination



- **Increase average loan size 30% or more**
- **Average escrow = \$36,100/\$43,100**
- **Focus moves to payment and value, away from interest rate**
- **Eliminate the competition**
- **Something new to talk about**

Benefits to Company

- **Create satisfied customers and referrals**
- **Differentiate yourself in marketplace**
- **Help Realtors sell more homes – resolve the issues with no additional work for them**
- **Close more loans**
- **Profitability**

How to Begin?

- **Take a credit application**
- **Evaluate the project**
- **Determine which 203(k) product is appropriate**

- **Credit Package**
 - » **Traditional FHA Credit**
 - » **Same rules for ARM's and REO**

Evaluating the Project

- **Questions to Ask**
 - » **Scope of the work**
 - » **Time required?**
 - » **Total cost of project and fees**

Selecting the Product

- **Clear choices**
- **Not so clear options**
 - **General Contractor vs Contractor**
 - **Generalist – “Jack of all Trades”**

What is different about 203(k)?



- **Consultant (n/a for Streamlined (k))**
 - Selected by Lender
 - Prepares the work write-up
- **Contractor(s) – General or Specialized**
 - Selected by Borrower and does the construction work
 - Provides cost estimates and contracts
- **Draw Administration**
 - Release of the escrow funds after closing until the project is complete

All FHA 203(k)

- **Owner occupied only**
- **HUD REO**
- **Good Neighbor Next Door**
- **Energy Efficient Mortgage (EEM)**
- **Manufactured housing**
- **Mixed-use properties**
- **Assumable**

Standard 203(k)

- **Minimum of \$5,000 in repairs**
- **No maximum for remodeling and fees**
- **Mortgage Payments can be financed**
- **Additions and structural changes**
- **Six months to complete but extensions allowed**
- **Mixed-use properties**

Streamlined 203(k)

- **Up to \$35,000 remodeling & fees (B14)**
 - **Repair, replace, upgrade work**
 - **Minor remodeling only – no plans or drawings**
 - **Appliances including free standing**
 - **Lead based paint abatement**
- **Contingency Reserve & Inspections**
 - **Lender's options & requirements**
- **Consultant is not required**
 - **Work items are added to appraisal**
 - **Work is completed after closing**
- **Maximum of two draws for each specialized contractor**

Special Documents for 203(k)?



- **Maximum Mortgage Worksheet (2/06)**
- **Cost Estimates – Work Write-up - Plans**
- **As Completed Appraisal**
- **Homeowner/Contractor Agreement(s)**
- **Borrowers Acknowledgement**
- **Identity of Interest**
- **Draw Request**
- **Rehabilitation Loan Agreement**
- **Rehabilitation Rider**

Maximum Mortgage Worksheet



- **A Maximum Mortgage Worksheet (MMWS) is required for every Renovation Mortgage**
- **The MMWS is used to calculate the correct mortgage amount**
- **The MMWS establishes the renovation escrow**
- **A MMWS may need to be updated several times between origination and underwriting**
- **No changes after final underwriting**

General Loan Information

- **Borrower information**
- **Loan Parameters**
- **Details about property**
- **Closing costs borrower will actually pay**

Total Renovation Escrow Account

- Total cost of repairs from work write-up
- Contingency reserve
- Inspection Fees and Title Updates
- Mortgage Payments Financed
- Costs that can be released at closing
- Supplemental Origination Fee
- Financed Discount Points

Section C – Purchase

- **Lesser of Sales Price plus Total Renovation Cost OR 110% of “as completed” appraised value**
- **Test for the minimum 3% statutory investment**
- **Use applicable LTV factor to calculate Maximum Mortgage Amount**
- **Adjust for allowable down payment if HUD REO**

Section D - Refinance

- **Sum of Existing Debt plus Total Renovation Costs**
- **Can add borrower paid closing costs, prepaids and discount points paid in cash if the as-is value supports the cost**
- **Use the LTV factors defined in 4155.1 Rev-5**

Work Write-up or Plans

- **Streamlined**
 - **Descriptive bid**
 - **Includes materials, labor and profit for the contractor**
- **Standard**
 - **Specifications of Repairs prepared by Consultant**
 - **Architectural drawings as needed**

- **After-improved appraisal**
 - **Current property plus “project”**

- **HUD REO – As-Is Appraisal**
 - **Property issues identified**

Borrower's Acknowledgement



- **Information for the Borrower**
 - » **Interest on Escrow Account**
 - » **Permits**
 - » **Draw Request process**
 - » **Contractor selection and changes**
 - » **Starting, changing and finishing the project**
 - » **Use of funds and holdbacks**

Loan Agreement and Rider

- **Formal Terms and Conditions**
 - » **Mortgage payments**
 - » **Escrow Account & Contingency Reserve**
 - » **Changes to plans and project**
 - » **30 day rule**
 - » **Liens and Notices**
 - » **Completion and/or Pay down**
- **Rider incorporates RLA and makes it part of the Security Agreement**

Underwriting 203(k)

- **Consultant**
- **Contractor – General or Specialized**
- **Project Plan and Appraisals**
- **Renovation Documents**
- **Draw Administration**

- **Consultant (n/a for Streamlined (k))**
 - **Selected by Lender**
 - **Prepares the work write-up**
- **Selection and Screening**
- **Benefits**
- **Fee Schedule**

- **Contractor(s) – General or Specialized**
 - Selected by Borrower
 - Does the construction work
- **Role**
- **Key information**

Project Plans and Appraisal



- **Documentation given to the appraiser describes clearly the work to be done**
- **Incorporates all aspects of the proposed changes**
- **Blueprints, drawings, sketches, minimum property requirements, HUD As-Is Appraisal**
- **One appraisal of the property as it will be when completed is needed**

Draw Administration

- **Permits**
- **Inspections**
- **Release of funds – Accounting Form**
- **Contingency Funds**
- **Holdbacks and Final Release**
- **Pay down and Interest on Escrow**
- **Close-out**

Reference Materials

- **4240.4 Rev. 2 - Handbook**
- **ML 94-11 - Key 203(k) Issues**
- **ML 95-40 - Key 203(k) Issues**
- **ML 00-25 - Consultants and Contractors**
- **ML 05-50 - Streamlined 203(k)**

Renovation versus Rehab

**Is this the only
time you think
of renovation?**



Time to revive FHA and 203(k)



**Thank you for your
interest!**

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