

# Renovate your Real Estate Business

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## Renovation Lending

This class is to help real estate agents better serve their clients by understanding how renovation loans work to solve problems. Sellers do not have to address health and safety issues and save additional funds in preparation to sale a home. Buyers can avoid costly bills after making a large purchase and tailor a house into a home they love. This option becomes a solution to help build the community by fixing distressed homes.

## Renovate your business

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- I. Identifying a property
- II. What are Renovation Loans
- III. Renovation Process
- IV. Writing the offer
- V. Developing a team approach?



### Part I: Identify the Property

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## Challenges?

1. Have you turned down listing due to property condition?
2. Have you missed listings due to seller wanting to do repairs?
3. Buyer can not find what they are looking for?
4. Found a property that had functional obsolescence?

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## Issues with Property

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- **Functional Obsolescence**
- **Structural**
- **Roof**
- **HVAC**
- **Room Additions**
- **Plumbing**
- **Eliminate Health + Safety Issues**
- **Paint – Interior/ Exterior**
- **Cosmetic Repairs**
- **Remodeling**
- **Appliances**
- **Windows**
- **Mold and Rot**
- **Landscaping**

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## Before & After Exterior



## Eligible Improvements

- Repair Well/ Septic
- Repair/ Remove Pool
- Roof/ Gutters
- Flooring
- Appliances
- Windows/ Doors
- Appliances
- Modifications for disable
- Fencing
- Tree Removal
- Oil tank removal
- Landscaping

## Before & After Interior



## NOT Eligible

- Finance costs associated to purchase
- No luxury (gazebos, tennis courts, spa, ect.)
- Improvements that solely benefit commercial
- Satellite dishes



## How the Renovation can be used?

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- ✓ To purchase a dwelling and the land and rehabilitate.
- ✓ To purchase a stick built home on one site, move it onto a new foundation and rehabilitate.
- ✓ To refinance existing liens secured against the subject property and rehabilitate.
- ✓ Prepare a property to be placed on the market

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## Benefits of Renovation

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- Buyers can purchase and make approved improvements after closing
- Current owners can refinance, stay in their homes, and make approved changes after closing.
- Increases property value and builds equity.
- Combines the cost of the home and renovation into one

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## Part II: What is Renovation Loan

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### What is a Renovation Home Loan?

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- A renovation loan allows you to finance a home AND include the costs associated with repairs, remodeling and/or additions into your loan.
- Three different types: **FHA 203k, Construction and Conventional Renovation.**
- Can be used for primary residences 1-4 unit, vacation homes and investment properties.
- The renovation loan is based on the **AFTER-IMPROVED** value of the home.



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## What is a Renovation Home Loan?

- Purchase-
  - Increase property value
  - Customize to buyer specification

**Acquisition + Renovation  
= Loan Amount**

  - Avoid Alternative Financing After Close
- Refinance
  - Address health and safety concern
  - Grow equity to maximize sales price



## Advantages of the Renovation Loan

- One loan covers the entire process – including an amount set aside in case of exceeding costs (contingency reserve).
- Borrower will know the repair costs for the subject property by obtaining estimates from a licensed contractor of the borrowers choice.
- Renovation fees can be financed into the total acquisition of the loan
- Low rates
- **6 months of payments can be rolled into the loan**





## Advantages of the Renovation Loan

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- Renovation loans **do not cause a delay** in settlement time frames
- Down payment assistance programs are permitted from government entities in accordance with guidelines \*\*\* VHDA does not allow 01/2018
- Repairs are to be completed within a specific timeframe based on the loan program.
- A renovation loan is ideal for fixer-upper homes or foreclosed properties because the loan closes BEFORE repairs begin and is based on the home's value AFTER improvements have been made.



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## Part II: Different Types of Renovation Loans

## FHA 203k **Streamline** Renovation Loan

- Home purchase or refinance and must be used for primary residence
- **Maximum of \$35,000 minimum of \$5,000**
- Minor/non-structural repairs, remodeling kitchens and bath, HVAC replacement/repairs
- 2 to 4 months time frame for work to be completed
- FHA minimum required down payment: typically 3.5% of total loan
- Fixed terms
- One settlement
- 1 to 4 unit homes - townhomes and condos
- Disbursement of funds are up to 50% of the contractor's estimate after closing – the remaining funds when work is completed and inspected
- Two party checks are issued payable to the customer and the contractor
- Only one contractor can be used
- Credit scores typically around 620 (can vary by lending institute)

## FHA 203k **Full** Renovation Loan

- Follows normal FHA guidelines ( lower scores, higher dti, and UFMIP)
- **No Renovation price limit- Loan limits per county apply**
- **Major renovations, structural changes and repairs - no tear downs**
- **6 months or less time frame for work to be completed**
- FHA minimum required down payment (3.5% of total loan)
- Fixed terms
- One settlement
- 1 to 4 unit homes - townhomes and condos
- **Disbursement of funds are after the HUD approved consultant's inspect, for each phase, and the contractor and home owner have signed the request**
- Two party checks are issued payable to the customer and the contractor
- Only one contractor can be used
- Credit scores typically around 620 (can vary by lending institute)

- FORMS: Hud 9746-A Draw Request (203k)
- FORMS: Hud 92577 Change order request (203k)

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## 203(k) Consultant Fee

example

- Consultant may charge the fees listed for the preparation of the Work Write-Up and review of architectural exhibits.
- Mileage Fee may be charged at the current IRS mileage rate when the Consultant's place of business is more than 15 miles from the property.

<u>Cost of Improvements</u>	<u>Fees</u>
< \$7,500	\$400
\$7,501 - \$15,000	\$500
\$15,001 - \$30,000	\$600
\$30,001 - \$50,000	\$700
\$50,001 - \$75,000	\$800
\$75,001 - \$100,000	\$900
> \$100,000	\$1,000
\$25 per additional Dwelling Unit	

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## Conventional Homestyle Renovation Loan

- **Home purchase or refinance and can be used for primary residence or investment/vacation homes**
- **Up to 50% of the after improved appraised value limit for renovation cost**
- Major renovations, structural changes and repairs - no tear downs
- **6 months or less time frame for work to be completed**
- Fannie Mae's required down payment- Loan limits apply per county
- Fixed terms
- One settlement
- 1 to 4 unit homes - townhomes and condos
- Disbursement of funds are after the HUD approved consultant's inspect, for each phase, and the contractor and home owner have signed the request
- Two party checks are issued payable to the customer and the contractor
- Only one contractor can be used

## Example of Loan Limits 2018

Can vary by county and is meant for illustration only\*

FHA	Standard	High Cost Areas
1 UNIT Owner Occupied 3.5% down	\$ 294,515	\$ 679,650
2 UNIT Owner Occupied 3.5% down	\$ 337,075	\$ 870,225
3 UNIT Owner Occupied 3.5% down	\$ 445,800	\$ 1,051,875
4 UNIT Owner Occupied 3.5% down	\$ 566,425	\$1,307,175

Conventional 2017	Standard	High Cost Areas
1 UNIT 5% down owner occupied	\$ 453,100	\$ 679,650
2 UNIT 15% down owner occupied	\$ 580,150	\$ 870,225
3 UNIT 25% down owner occupied	\$ 701,250	\$ 1,051,875
4 UNIT 25% down owner occupied	\$ 871,450	\$1,307,175
1 unit 15% down Investment Property	\$ 453,100	\$ 679,650

<https://www.fanniemae.com/singlefamily/loan-limits>  
[https://www.fanniemae.com/content/eligibility\\_information/eligibility-matrix.pdf](https://www.fanniemae.com/content/eligibility_information/eligibility-matrix.pdf)  
<https://www.fhfa.gov/DataTools/Tools/Pages/Conforming-Loan-Limits-Map.aspx>

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## Construction Loan

- **Home purchase or refinance and can be used for primary and vacation homes**
- **No price limit**
- Major renovations, structural changes and repairs – **tear downs available**
- 12 months or less time frame for work to be completed
- Larger down payment required than other options listed
- **Fixed and adjustable terms (permanent finance)**
- **Option of One settlement or Two depending on the construction**
- **Single family attached and detached homes – no condos**
- **Disbursement of funds are after a draw inspection by appraiser**
- **Checks or wires are issued payable to the contractor**
- Only one contractor can be used
- **Only available in certain areas**

## Conversion and Property Types

### Eligible Properties: Condominiums

Question: Would this condo unit be eligible for 203(k) financing? It has three stories with two units on each floor.



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## Part III: Renovation Process

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## The Renovation Process

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1. Pre Qualify & Identify Property
2. Closing time 40-45 days
3. Offer to purchase
4. General contractor and or consultant ( 2 -4 weeks)
  1. Work write up (material and labor)
5. Appraisal (**subject to**)
  1. Change project by scaling back or change plan
  2. FHA allows 110% of after improved appraised value
6. Close
7. Work begins after closing with a draw schedule
8. GC disbursements

## The Renovation Process

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- Borrower chooses a licensed **contractor** who will perform the work and will obtain a consultant's work write-up report and/or contractor's estimate to determine the cost and the scope of work involved.
- The **after-improved appraisal** is ordered based on the work write-up or the contractor's bid.
  - Please note: we cannot order an appraisal without the finalized and signed bid
- The contractor delivers their insurance forms and disclosures along with a copy of their license. \*contractor must be licensed in the state of the property location

## The Renovation Process continued

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- Once a **final approval** is obtained, **closing** is scheduled and the funds for the draws are set aside. Funds will be disbursed on a draw basis after settlement.
- **Repairs are to begin** within 30 days of closing and are to be completed within a specific timeframe agreed upon in advance between the borrower and contractor and approved by the lender (not to exceed 6 months)
- The funds are mailed to the borrower in the form of a **two party check** and made payable to the borrower and the contractor.
- Borrower is required to make mortgage payments as scheduled after closing

## Contractors NOTES

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- Required for all renovation loans
- The borrower selects the contractor
- The lender cannot provide recommendations

The contractors MUST:

- be licensed in the state that the renovation work will be completed in
- have liability insurance
- be able to provide 3 quality references for past projects
- provide a detailed bid for renovation work broken down by labor and material
- Have three years minimum experience







## How the HUD consultants work

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### I. Consultant meets with the borrower at the site.

- A general examination of the work to be done determines if the project is feasible.
- If feasible, Client signs Consultant Agreement and pays the Consultant fee (can be financed into loan) \*however, most require a deposit

### II. Consultant prepares a detailed **Work Write-Up** which contains:

- Clear, concise project specifications
- Construction cost analysis
- HUD required draw request forms
- Preparation of contractor bid packages
- Preparation of lender packages

### III. Consultant delivers the Work Write-Up Packages to the:

- Borrower
- Lender
- Contractor

**\*HUD Consultants WWU and contractors BID must match\***

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## Part III: The Renovation Process (cont)

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## Contingency Reserves

- A **contingency reserve equal to 10% and up to 20%** of the total costs of the repairs and renovation work must be established and funded to cover required unforeseen repairs or deficiencies that are discovered during the renovation.
- The contingency reserve may be considered as part of the total renovation costs or the borrower may fund it separately.
- The contingency reserve may be released only if required, necessary, and unforeseen repairs or deficiencies are discovered during the renovation.
- **Unused** contingency funds, unless they were received directly from the borrower, must be used to **reduce the outstanding balance** of the renovation mortgage after all of the renovation work has been completed and the certification of completion has been obtained.



## Renovation Work Requirements

- All improvements required by the appraiser on the property must be included in the **Work Write-Up/Contractor Bid**.
- Renovation work must start within 30 days of settlement.
- Work may not stop for more than 30 days.
- All improvements completed on the property must be based on the Work Write-Up.
- Work must be completed within 6 months.



## Draw Procedure

- Funds are released from the escrow account as work is completed
- A draw request form will show all parties the amount of each item or category for the draw
- An inspection must be performed by the consultant or appraiser to sign a draw request for funds to be released
- Draw requests must be signed by the customer, contractor and consultant which will ensure that all parties involved have inspected the work and approved completion



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## Draw Procedure

- There is a standard 10% hold back on each draw (for total renovation costs >\$35,000 or when structural work is required)
- If there is a change in the work being performed, a change order request must be made in writing along with a new estimate for the item which must be reviewed and accepted by George Mason Mortgage
- Checks will be made payable to both the customer and the contractor
- Final Draw request close out is complete when the contractor finalizes the project and all draw documents are submitted and approved



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## Common Mistakes or Delays

- Contract timeframe – to allow for appraisal completion
- Finding a contractor that is licensed, experienced and available- it is recommended that the borrower research the contractor through Better Business Bureau and their states licensing website
- Not meeting required timeframes
- Under estimating the required work amounts \*example starting at 30 and bid comes in at 80



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## Part VI: How to Write a Purchase Contract for a Renovation Loan

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## Suggested Contract Language & Instructions

- Write the Contract for purchase in **“AS-IS” condition.** – The seller does not need to do any work to the property prior to closing the loan
- The math portion of the contract is just like any other contract, based completely on negotiated sales price for the property
- Seller contribution limits apply:
  - For conventional & construction: above 90% LTV is a 3% max seller contribution and below 90% LTV is a 6% max.

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## Suggested Contract Language & Instructions


- Select the financing type- then **write in renovation.** This tells the LO they can work on the renovation portion of the financing

*The following is suggested language to be placed in the contingency section or other terms of the contract:*

- The seller will allow full access to the property after contract ratification for Rehab/Renovation Construction Estimating (performed by the consultant and Contractor). The report completed by the HUD consultant is called the Specification of Repairs.
- This contract is contingent on loan approval and buyers acceptance of Specification of Repairs.

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## Suggested Contract Language & Instructions



**CONTRACT LANGUAGE \*FHA Loan**

- Purchase contract needs to disclose the buyer will be utilizing the FHA 203(k) to acquire the property.
- FHA does not require the amendatory clause for any 203k renovation
- Seller contribution limits apply:
  - For FHA 203k there is a max of 6% seller contribution.

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FHA's Office of Single Family Housing Training Module

## Sample HUD REO Sales Contract

EXAMPLE: FHA INSURED 203(k) FINANCING


**Sales Contract**

**U.S. Department of Housing and Urban Development**

Office of Housing  
Federal Housing Commissioner

**Property Disposition Program**

1. I (We) \_\_\_\_\_ (Purchaser(s)) agree to purchase on the terms set forth herein, the following property, as more particularly described in the deed conveying the property to the Secretary of Housing and Urban Development:  
(street number, street name, unit number, if applicable, city, county, State)
2. The Secretary of Housing and Urban Development (Seller) agrees to sell the property at the price and terms set forth herein, and to prepare a deed containing a covenant which warrants against the acts of the Seller and all claiming by, through or under him. Title will be taken in the following name(s) and style \_\_\_\_\_
3. The agreed purchase price of the property is \_\_\_\_\_ 3. \$ 125,000  
Purchaser has paid \$ 1,000 as earnest money to be applied on the purchase price, and agrees to pay the balance of the purchase price, plus or minus prorations, at the time of closing, in cash to Seller. The earnest money deposit shall be held by \_\_\_\_\_
4.  Purchaser is applying for FHA insured financing  203(b),  203(b) repair escrow,  203(k) with a cash down payment of \$ \_\_\_\_\_ due at closing and the balance secured by a mortgage in the amount of \$ \_\_\_\_\_ for \_\_\_\_\_ months (does not include FHA Mortgage Insurance Premium, prepaid expenses or closing costs Seller has agreed to fund into mortgage).  
 Said mortgage involves a repair escrow amounting to \$ \_\_\_\_\_  
 Purchaser is paying cash or applying for conventional or other financing not involving FHA.
5. Seller will pay reasonable and customary costs, but not more than actual costs, nor more than paid by a typical Seller in the area, of obtaining financing and/or closing (excluding broker's commission) in an amount not to exceed \_\_\_\_\_ 5. \$ 3,750
- 6a. Upon sales closing, Seller agrees to pay to the broker identified below a commission (including selling bonus, if offered by seller) of \_\_\_\_\_ 6a. \$ 6,250
- 6b. If broker identified below is not the broad listing broker, broad listing broker will receive a commission of \_\_\_\_\_ 6b. \$ 0
7. The net amount due Seller is (Purchase price [Item 3] less Items 5 and 6) \_\_\_\_\_ 7. \$ 115,000
8. Purchaser is:  owner-occupant (will occupy this property as primary residence)  investor  
 nonprofit organization  public housing agency  other government agency. Discount at closing: \_\_\_\_\_ %  
Discount will reduced by amounts, if any, listed on Line Items 5 and 6.



## HUD REOs

- HUD REOs are eligible for 203(k) loans if they are listed as uninsurable or insurable with repairs.
- HUD REOs that are listed as uninsurable can only be an FHA loan as a 203(k).
- “Good Neighbor Next Door” and \$100 down programs can be used with 203(k).
- Sales Contract must reflect 203(k) financing.

*FHA Training Module*

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## Part VII: Develop your Team

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## TEAM to Referrals

- Home Inspector
- General Contractor
  - Sub contractors (introduction)
  - HVAC, Roofer, Plumber, Electrician
- Interior decorator (HGTV)
- Architect / Virtual Rendering
- Landscaper/ Nursery
- Moving Company

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### SHAWN BARSNESS

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