

FHA 203 (k) Rehab Loan



Help qualified borrowers purchase or refinance and make improvements—all with a single loan





Through the Federal Housing Administration (FHA) 203(k) mortgage insurance program, borrowers can purchase or refinance their home and include the costs to rehabilitate and repair it in the same loan. This program can help you expand homeownership opportunities while at the same time revitalizing the communities you serve.

FHA 203(k) can help you:

- Increase loan origination volume
- Expand your market reach
- Help borrowers find affordable financing and realize the dream of homeownership





There are borrowers who:

- Are interested in purchasing a property that needs repairs
- Are existing homeowners who need funds to rehabilitate their property
- Want to save time and money by financing the purchase or refinance with the cost of the repairs
- May not qualify for a conventional loan
- Have low-to-moderate incomes
- Are first-time homebuyers
- Live in disadvantaged neighborhoods
- Have credit blemishes or low credit scores
- Have limited cash for down payment or closing costs
- Want to improve their home and neighborhood





Provide borrowers an affordable, stable financing solution that combines the purchase or refinance of the home along with the costs of the improvements into a single loan:

- FHA guidelines apply
- Opportunity to borrow against the value of the home after improvements
- Low down payment requirements
- Flexible credit qualifying
- Fixed-rate and adjustable-rate mortgages up to 30-year terms
- Fully assumable loans to qualified borrowers
- Owner-occupied 1-4 unit properties, PUDs, condos and REO properties
- Lower initial monthly payments with optional temporary buydown





Your target market would be:

Borrowers purchasing a home in need of rehabilitation:

- May be REOs, short sales and foreclosures
- Incomplete renovations
- Out-dated kitchens, bathrooms, etc.

Borrowers refinancing existing home to make improvements:

- Improve instead of move
- Out-dated kitchens, bathrooms, etc.
- Expand to accommodate a growing family



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Types of mortgages

- 15-, 20-, 25- and 30-year fixed-rate terms
- 30- year only with FHA jumbo loan amounts
- 1-year adjustable-rate mortgage
- Not allowed with FHA jumbo loan amounts
- Optional temporary 2/1 buydown

Purchase and refinance of owner-occupied, primary residence

- Attached and detached single family residences, condos, and PUDs
- 2-4 unit properties
- REO properties

Eligible borrowers

- U.S. citizens
- Permanent and non-permanent resident aliens
- Non-occupant co-borrowers





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- **Investor handles draws**
 - Up to five releases allowed – two releases for Streamline
- **Work can be completed by contractor or borrower**
 - Borrower must be qualified and approved to do the work
 - Work must be completed within the agreed upon timeframe (no more than six months after closing)
- **Up to six months PITI can be included in the mortgage if the property is not occupied during construction**
- **Loan is fully assumable to qualified borrowers with no money down**



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Virtually any kind of improvement is eligible provided it becomes a permanent part of the real property and adds value, for instance:

- Additions to the structure
- Kitchen or bath remodels
- Finished basement or attic
- Patios, decks or terraces
- Roofing and landscaping
- Safety, energy efficiency and electrical upgrades
- Handicapped accessibility improvements

Luxury items are not eligible:

- Swimming pools, hot tubs, tennis courts, gazebos, barbecue pits, saunas or alterations to support commercial use





FHA guidelines apply

- **Manual underwriting**

- Minimum 580 credit score required on loans with FHA standard loan amounts
- Minimum 620 required on FHA jumbo loan amounts
- Non-traditional credit permitted

- **Bankruptcy (BK) and foreclosure**

- Chapter 7 allowed after 24 months after the discharge date, provided that good credit has been reestablished
 - Less than 24 months (but not less than 12 months) may be allowed provided the reason for the BK was due to extenuating circumstances and the borrower has exhibited an ability to manage financial affairs and the reason for the BK isn't likely to recur
- Chapter 13 allowed after 12 months of the pay-out period provided performance has been satisfactory and customer receives court approval to enter into the mortgage transaction
- Foreclosure or deed-in-lieu allowed after three years

- **Court ordered judgments and tax liens must be paid**

- Tax liens may be included in the refinance





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- **Full documentation only**
- **Miscellaneous income is acceptable, including child support, alimony or maintenance payments, and Note income**
 - Must show a 12-month history and evidence that the income will continue for three years
- **Self-employed income must be stable**
 - Two-year history required
- **Rental income acceptable with two-year history**
- **31/43% qualifying ratios** (higher ratios allowed with HUD approved compensating factors)





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- **Minimum \$5,000 rehabilitation amount**
- **3% minimum down payment required**
 - Checking, savings or other depository accounts
 - Proceeds from 401(k)
 - Gift from relative, fiancé/fiancée or domestic partner
 - Cash-on-hand
- **Interest party contributions allowed up to 6% toward closing costs**
- **Cash reserves are not required on 1-2 unit properties**



FHA 203 (k) Streamline

Allows borrowers to easily finance an additional \$35,000 into their mortgage to make improvements

- Cover improvements identified by home inspector or FHA appraiser
- Available for purchase and refinance transactions
- Allowed on limited improvement types, including:

Roofs, gutters, downspouts

Upgrade/repair plumbing, septic, well & electrical systems

Heating and air conditioning

Replacement of flooring, windows, doors, siding

Purchase and installation of appliances

Minor remodels that don't involve structural repairs

Handicapped accessibility improvements

Weatherization, painting, basement waterproofing

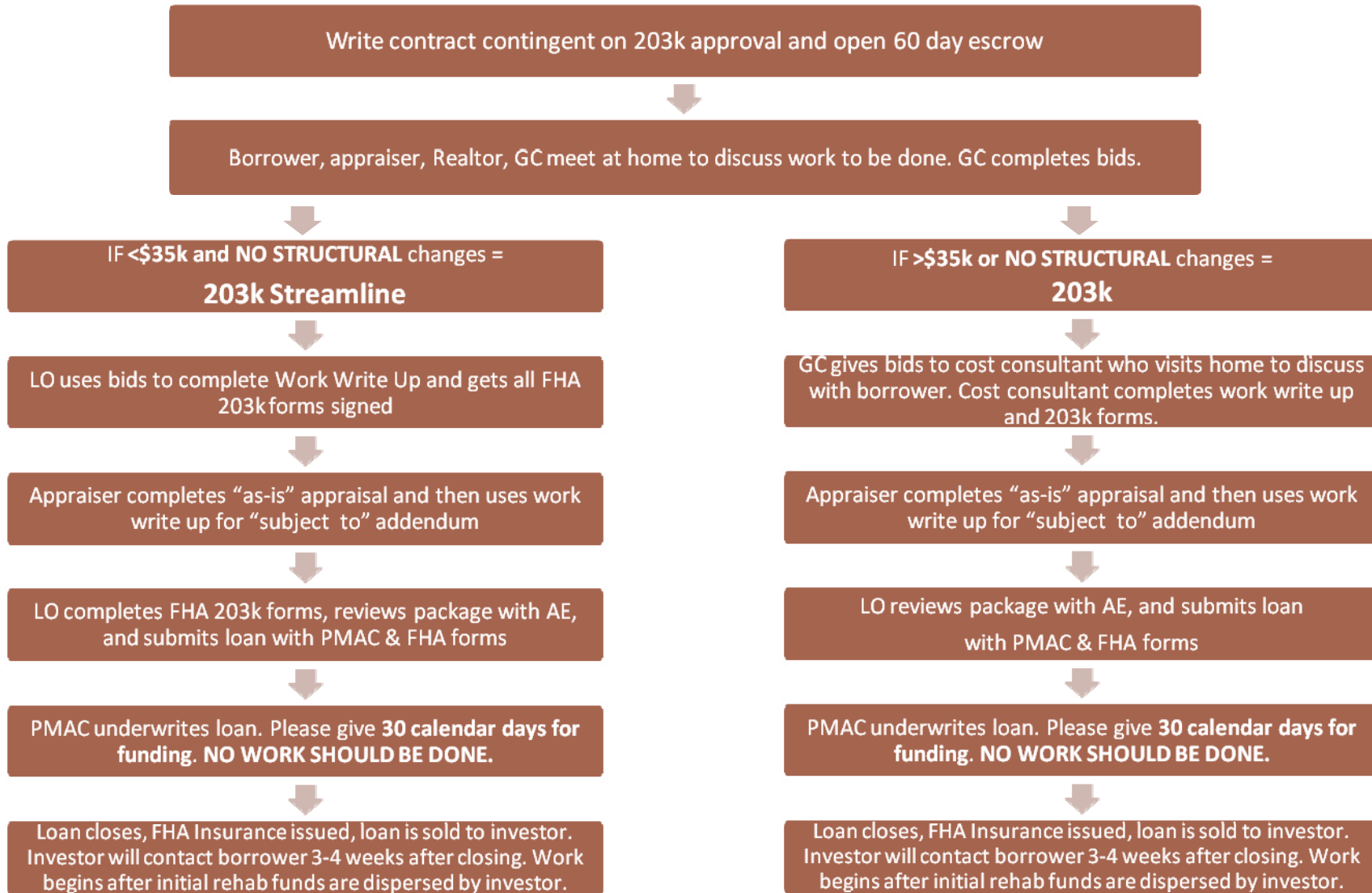
Streamlined 203(k) is subject to the same guidelines as FHA 203(k)

- It is the disbursements that are “streamlined”

PMAC Lending requires a HUD Consultant if the total repairs exceed \$20,000



203k and 203k Streamline Flow Chart





- **The loan-to-value is based on the lesser of:**
 - The sales price or “as is” appraised value plus cost of rehabilitation minus sales concessions or
 - 110% of “as completed” appraised value
- **When a 203(k) loan is coupled with an energy efficient mortgage, the base loan amount may exceed the county maximum up to \$8,000**



Determining the Maximum Loan Amount

EXAMPLE: purchase of a 1-unit property with 97/97% LTV – owner occupied only

Purchase and Renovation Costs

Sales Price (“as-is” appraised value)	\$	120,000
Labor/Material	\$	24,500
Soft Costs	\$	2,200
Contingency (utilities functioning – 10% required)	\$	2,670
Monthly PITI (Not required to vacate property during renovations)	\$	0
Total for Purchase and Renovation	\$	149,370

“As-completed” value (determined by appraiser) **\$ 160,000**

Value to use for determination of LTV must be the lesser of the sales price or “as-is” appraised value plus cost of rehabilitation minus sales concessions, or 110% of the “as-completed” appraised value. In this example, \$149,370 is less than 110% of the “as-completed” appraised value of \$176,000, therefore the value you must use when determining the maximum loan amount is \$149,370.

Maximum Loan Amount at 97% LTV **\$ 144,888**



Funding the Loan

\$200,000 Total Loan Amount

(\$175,000 purchase or refinance plus \$25,000 rehabilitation cost)*

	<u>Item</u>	<u>Amount</u>
	Amount for purchase or refinance	\$ 175,000
	Rehabilitation amount	\$ 25,000
	Total loan amount	\$ 200,000
	Total amount to be sent by Lender to the closing agent	\$ 200,000
Closing agent disburses funds (\$175,000 for purchase or refinance and \$25,000 to Lender) to deposit into an interest-bearing escrow account		\$ 200,000
	Investor wires Lender	\$ 175,000
Lender transfers rehabilitation funds from escrow account back to warehouse line		\$ 25,000

*This simplified example is for illustrative purposes only and does not include any fees associated with the transaction.





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After the loan is purchased

- Welcome package is sent to the borrower
- Signed W-9 form required from contractor before funds can be drawn
- Disbursements are made as each phase of the project is completed based on the draw paperwork provided by the cost consultant
- Exception is for the cost of flooring, roofing, cabinets and windows – 50% of the cost of these items can be disbursed upfront as part of a normal draw
- Inspections are required prior to each disbursement

A maximum of five draws allowed

- Draw amounts may vary and are based on the work performed
- A 10% reserve is withheld on each draw – a “holdback”
- “Holdback” funds are disbursed upon completion of all work





After the loan is purchased

- 50% of the rehabilitation funds are disbursed immediately
 - For borrowers doing the work themselves, a self-help agreement is required before any funds are disbursed – the check is made payable to the borrower
 - For borrowers working with a contractor, a W-9 must be provided to establish the contractor as approved – a two-party check is made payable to both the borrower and the contractor, the check will be sent to the borrower
- Included with the initial disbursement is an instruction letter detailing the receipt of the final disbursement
- The balance is disbursed upon completion of all work
- If the cost of the renovation is over \$15,000, an inspection by the original appraiser is required

Two disbursements are made

- One shortly after loan purchase
- Second and final disbursement once all work has been completed



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- Used to cover health, safety and unplanned issues that arise during construction
- Required on FHA 203(k); recommended on Streamline
- Required on properties older than 30 years and/or over \$7,500 in rehabilitation costs
- A minimum of 10% of the cost of rehabilitation and maximum of 20%
- If not used (after all construction is complete) the remaining amount can be
 - Applied to principal OR
 - Used to make other improvements (additional approval is required)





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- Used as an incentive to insure all work is completed
- Required on FHA 203(k) only – not Streamline 203(k)
- 10% of the cost is withheld from each draw
 - All payments are impacted by this requirement
 - For deposits on flooring, roofing, cabinets and windows there is no holdback on the deposit, but the final payment is subject to the holdback
 - Disbursed after all work has been completed and inspected
- Make sure all parties involved in the rehabilitation understand the holdback requirement





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- **Make sure all parties understand the draw process**
 - When the first and all subsequent draws are made
 - How many draws are allowed – maximum five for 203(k) and two for Streamline 203(k)
- **Title must be clear before final payment is made**
- **The most common cause for a delay in draw is a missing W-9**
- **Cost consultants can help make the process easier – they are listed by location** (search neighboring town to locate additional cost consultants)
- **Let Investor handle all draws**



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- **For area median home prices:**

<https://entp.hud.gov/idapp/html/hicostlook.cfm>

- **Cost consultants can be found on HUD's website:**

<https://entp.hud.gov/idapp/html/f17cnsldata.cfm>

- **For information on FHA mortgage insurance programs, visit:** <http://www.fha.gov/>

- **For information on U.S. Department of Housing and Urban Development, visit:**

<https://www.hud.gov/>

