

How To Buy A Fixer-Upper With A Renovation Mortgage

The Ultimate Guide To Home Improvement Loans



Lending that has you covered.

The Richard Woodward Mortgage Team



THE ULTIMATE GUIDE TO HOME IMPROVEMENT LOANS

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WHAT IS A RENOVATION MORTGAGE?

Picture this scene: you're tired of renting and you want to find your own house. As you begin to explore the neighborhoods in which you'd like to live, you find many foreclosed homes up for sale. Many times, these homes are in disrepair. Sometimes they're missing things like appliances, the furnace or a water heater. But with prices what they are, it's hard to walk away from these properties. Enter home improvement loans – also known as the **Renovation Mortgage**. You can take advantage of one of these programs and roll the cost of repairs, renovation, rehabilitation and home improvements into the mortgage and pay just one monthly payment. The benefit to this is that you can then write off the interest on your taxes. You can't do that when you finance the work and supplies on a credit card or store credit line.

Disclaimer: Not intended as accounting or investment advice. Interest above the fair market value is not tax deductible for federal taxes. Contact your tax preparer for more information.

A renovation mortgage allows you to buy the house in its current condition and assume the responsibility of making the necessary repairs. So you can buy the house in "as-is" condition with a mortgage that takes into account the after-improved value once the work is completed. The cost of the work is amortized over the life of the mortgage, and stays with the home in the event that you decide to sell.

This is not a do-it-yourself home improvement loan. Renovation mortgages require licensed professionals for most of the work. This protects you and the lender in case the work does not get finished. Unfinished work devalues the home, and makes life difficult for all parties involved. Renovation mortgages can include several options. We'll explore those in this eBook. This guide is meant to help you better understand your options. Some of these programs can change without notice, since the ultimate funding comes from mortgage backers like Fannie Mae. Let this guide be your helper when it comes to buying a home in this housing market.

Renovation Mortgage Projects

Repair/replace roof, gutters & downspouts

Buy & install appliances including washer/dryer

Repair/replace/upgrade existing HVAC systems

Repair/replace septic systems and/or well

Repair/replace plumbing & electrical systems

Disability access like wheelchair ramps, elevator

Replace/repair flooring (carpet, tile, wood)

Abatement/stabilization of lead-based paint hazard

Minor renovations in kitchen or bathrooms

Build/repair/replace decks, porches & patios

Interior or exterior painting

Basement finishing & waterproofing (excluding structural)

Weatherization including storm doors or insulation

Replace windows, doors and siding

What is a HUD Consultant?

The role of the 203k Consultant is vital to the success of a FHA full 203k loan. The consultant is responsible for the onsite visit and the HUD work write up and is responsible for staying on during the project to facilitate draws and inspections. I like to think of this person as your own mini “project manager” and it adds a nice layer of comfort to the project. It is very important that you and your consultant have excellent communication at all times.

The overall objective/responsibility of the 203k HUD Consultant will be to insure [HUD’s minimum property standards](#) are met. In the work write up the consultant will cover the required repairs that will need to be done to the property. Also the consultant will make any recommendations for work that should be done. Then finally it will include desired work that the borrower would like to include.

The report will also stipulate if the home is habitable or not, the number of draws that will be allowed and the amount of contingency that will be required.

The HUD consultant is hired by the lender to inspect the property. The HUD consultant is normally a licensed property inspector. You may hire your own property inspector but in most cases, the HUD inspector would duplicate the service. If you would like to save money, the HUD inspector could also act as your inspector.

HUD Consultant Fees and Examples of Minimal Property Standards

Duties of HUD Consultant in Full Renovation Loan

- Provide the lender with a Specification of Repairs/Work Write Up which will be sent to the appraiser to use when arriving at “As Repaired” value.
- Provides expert opinion on whether the submitted bid by the contractor will be sufficient to complete the given repair items.
- Provides HUD Consultant expertise with interaction between Contractor and Borrower.
- Provides expertise for requested Change Orders; prepares the Change Order forms and submits to Lender for approval.
- Provides on-going Contractor interaction, inspections, and pictures of completed work with each Draw Request.
- Submits paperwork for each Draw Request to Lender for approval and processing.
- HUD Consultant Fees are set by FHA. These Fees may be financed into the loan, but usually the HUD Consultant will require a prior to close deposit on the fees to cover his losses if the loan does not close.

<u>Cost of Repairs (B1)</u>	<u>Fee</u>	<u>Cost of Repairs (B1)</u>	<u>Fee</u>
\$0 to \$7,500	\$400	\$50,001 to \$75,000	\$800
\$7,501 to \$15,000	\$500	\$75,001 to \$100,000	\$900
\$15,001 to \$30,000	\$600	\$100,000 and beyond	\$1,000
\$30,001 to \$50,000	\$700	Draw Inspection Fee	\$150

Section 2: Home Improvement Loan Options

HOME IMPROVEMENT LOAN OPTIONS

VA Renovation Loans

Now You Can Renovate Your Home the Benefits of a VA loan

Do you have a home in need of minor repairs no cash on-hand?
The VA renovation program could be your solution

The VA renovation program is designed to help men and women who serve our country repair or upgrade their home with the low rates VA lending programs offer. This program allows for minor renovation cost and the loan amount of home for purchase, or for repairs being done to an existing home with equity. This program is perfect for those looking to do small repairs such as repainting, fixture swaps, or assess ability upgrades such as ramps or rails.

The problem with home equity is that few homeowners in the United States have enough equity in their homes to qualify for equity loans or lines of credit.

Program Features

- Up to \$35,000 in renovation cost
- No minimum repair amount
- Includes minor and nonstructural repairs
- For purchase or refinance Homes
- Cosmetic repairs allowed
- No consultant required
- Primary residence only

Take charge of home improvements this one-of-a-kind product
to create the home you always dreamed of.



Disclaimer: Primary borrower must be an eligible veteran with a credit score of 620 or higher. Normal debt to income ratios and qualification requirements apply.

FHA 203K

The 203k section of FHA guidelines refers to borrowing additional funds to make repairs and improvements to your home. You can use the funds for simple upgrades to your home like a kitchen or bath improvement, or for more in-depth rehabilitation like rebuilding a house that is presently unlivable. You can even use a **203k rehabilitation loan** to tear down an existing structure and build a new one using some portion of the existing foundation. You can borrow up to 96.5% of the after-improved appraised value. You can only use the **203k** for primary, owner-occupied homes.

There are two **FHA 203k** options for you to consider: Standard 203k and the 203k Limited.

STANDARD 203K

The Standard 203k covers repairs of more than \$35,000 including structural work. This can include moving a load-bearing wall, adding a room or replacing the sill plate (due to insect damage). A Standard 203k requires a HUD-approved 203k consultant to help in the process.

Timelines, Disbursements and Inspections for the Standard 203k

Timeline: When the loan closes, the mortgage proceeds will be disbursed to pay off the seller of the existing property and the Rehabilitation Escrow Account will be established. Construction may begin. The homeowner has up to six (6) months to complete the work depending on the extent of work to be completed.

Disbursements (Draws): As construction progresses, funds are released after the work is inspected by a HUD-approved inspector. A maximum of 5 draws are allowed. Draw amounts may vary and are based on the work performed. Disbursements are made as each phase of the project is completed based on the draw paperwork provided by the consultant. Inspections are required prior to each disbursement. A ten (10) percent holdback is required on each disbursement released from the Rehabilitation Escrow Account.



The Holdback/Contingency Fee is:

1. Used as an incentive to insure all work is completed and to cover health, safety and unplanned issues that arise during construction.
2. Required on FHA 203k; recommended on Limited.
3. Required on properties older than 30 years and/or over \$7,500 in rehabilitation costs.
4. A minimum of 10% of the cost or rehabilitation and maximum of 20%.

If not used (after all construction is complete) the remaining amount will be applied to pay down the principal balance of the loan. The total of all holdbacks may be released only after a final inspection of the rehabilitation and issuance of the Final Release Notice.

Eligible Improvements for the Standard 203k

Homeowners can use the 203k program to finance “desired” repairs or upgrades such items as painting, room additions, decks and other items even if the home does not need any other improvements. Eligible improvements can range from relatively minor (though exceeding \$5,000 in cost) to virtual reconstruction: a home has been demolished or will be razed as part of rehabilitation is eligible, for example, provided that the existing foundation system remains in place.

The types of improvements borrowers may make using the Standard 203k include:

- All of the improvements listed below in the eligible improvements for a Limited 203k.
- Structural alterations and reconstruction, like room additions, repair of termite damage, major remodeling of kitchens and bathrooms, finishing an attic or basement, adding a second story to a home, etc.
- Major landscaping and site improvement including correction of grading and drainage problems, tree removal and repair of sidewalks and driveway, if they are a safety hazard to the property.

LIMITED 203K

When you need limited repairs of less than \$35,000 the Limited 203k comes into play. Replacing carpet, repainting the house or buying new appliances fall under the Limited 203k. You do not need to have a HUD consultant in a Limited 203k (although it's often a good idea to have one running the show for you).

Timelines and Disbursements for the Limited 203k

Timeline: When the loan closes, the mortgage proceeds will be disbursed to pay off the seller of the existing property and the Rehabilitation Escrow Account will be established. Construction may begin. Depending on the type of improvements the homeowner has up to six (6) months for completion.

Disbursements (Draws): No more than two payments may be made to each contractor. The first payment is intended to defray material costs and shall not be more than 50% of the estimated costs of all repairs and improvements. The Lender will allow the first payment at closing to cover for, and not exceed, actual required contractor deposits, building permits, and/or the cost of building materials incurred prior to construction. Before a final disbursement is made, the borrower must sign a statement acknowledging that the work has been completed in a workmanlike and satisfactory manner. A final inspection is required regardless of the improvement or repair, and must be done at completion before the final disbursement is released. Any leftover funds are applied to principal balance of the loan.



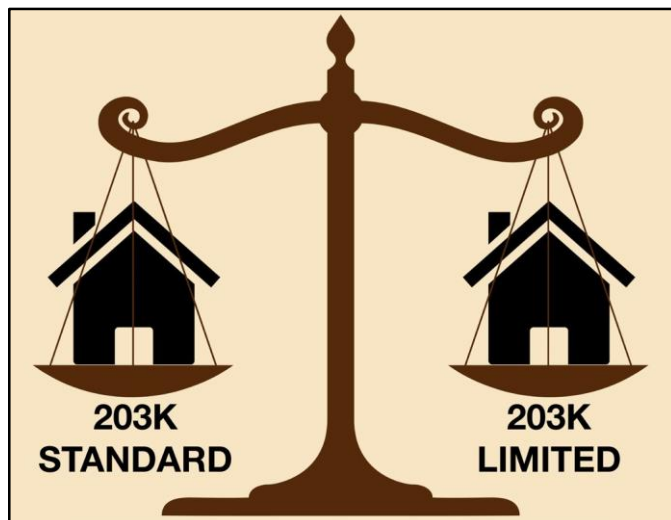
Eligible improvements include:

- Repair/Replacement of roofs, gutters and downspouts
- Repair/Replacement/upgrade of existing HVAC systems
- Repair/Replacement/upgrade of plumbing and electrical systems
- Repair/Replacement of flooring
- Minor renovation, such as kitchens & baths, which do not involve structural repairs
- Painting, both exterior and interior
- Weatherization, including storms windows and doors, insulation, weather stripping, etc.
- Purchase and installation of appliances, including free-standing ranges, refrigerators, washers/dryers, dishwashers and microwave ovens
- Septic system and/or well repair or replacement
- Accessibility improvements for persons with disabilities
- Lead-based paint stabilization or abatement of lead-based paint hazards
- Repair/replace/add exterior decks, patios, porches and swimming pools
- Basement finishing and renovation with does not involve structural repairs
- Basement waterproofing
- Window and door replacements and exterior wall re-siding

Ineligible Improvements include:

- Renovation involving structural changes, like moving a loadbearing wall, or new construction, like adding rooms
- Landscaping or Fencing
- Work that will not start within 15 days of loan closing or will cause the borrower to be displaced from the home for more than 15 days or renovations that will take more than 6 months to complete
- Luxury items like hot tubs, tennis courts, etc.

Learn more about Standard vs. Limited 203k in the Service First blog.



REFINANCE AND STAY WITH A 203K

The FHA 203k mortgage isn't just for new purchases. Home owners can refinance their mortgage into an FHA 203k and make the home improvements they desire, and stay in an "all-new home." In order to refinance, the home must meet these maximum amount stipulations.

Based on the lesser of:

1. The existing mortgage balance before rehabilitation, plus the estimated cost of rehabilitation and allowable closing costs or
2. The lesser of the As-Is value plus rehabilitation costs or 110% of the after-improved value multiplied by 97.75%



HOMESTYLE RENOVATION

The HomeStyle Renovation mortgage is another option for investors and home buyers alike. With the HomeStyle Renovation mortgage, you get to obtain a purchase transaction mortgage or a limited cash-out refinance mortgage and receive funds to cover the costs of repairs, remodeling, renovations or energy efficient improvements to the property.

There are no required improvements or restrictions on the types of repairs allowed or a minimum dollar amount for the repairs. Repairs or improvements, however, must be permanently affixed to the real property and add value to the property.

Essentially, HomeStyle Renovation is a solution to the current problem in housing that home buyers often see: finding houses that aren't yet "home." You can buy a house with potential and turn it into your home with your style, without breaking the bank. With a minimum of 5% down*, you can finance the purchase and remodeling of your dream home.

With as little as a 5% down payment you can add your taste & style to a house to make it your home with remodeling projects like a new kitchen, bathroom, room addition or energy efficient upgrades.

HomeStyle Renovation allows you to buy a home and fix it up, or refinance and remodel your current home.

- Purchase or refinance & remodel
- 5% minimum down payment for primary, single-family residences (10% for second homes)
- You can use gift funds for down payment & closing costs for owner occupied, primary residences after you contribute a minimum 3% down payment
- 3% seller contribution allowed
- Cosmetic and structural renovations allowed
- Allowable improvements can include landscaping, appliances, swimming pools and more



RENOVATION LOAN COMPARISON CHART

	FHA 203k (Consultant)	FHA 203k (Limited)	Fannie Mae HomeStyle®
Loan Type	Purchase or refinance		Purchase or refinance
Property Type	Purchase and renovate most residential properties		Purchase and renovate most residential properties
1-4 Unit Primary Residence	✓	✓	✓
1-Unit Second Home			✓
1-Unit Investment Properties			✓
Minimum Down Payment	3.5% of total acquisition cost (Sale price + renovation costs) or for refinancing (mortgage balance + renovation costs)	3.5% of total acquisition cost (Sale price + renovation costs) or for refinancing (mortgage balance + renovation costs)	10% for 1 - unit primary and second homes
			20% for 1 - unit investment only
Gift Funds	Allowed per FHA guidelines		Can be used on a case by case basis for down payment for owner occupied, primary residence and subject to MI guidelines
Mortgage Amount	Based on "as completed" appraisal value or total acquisition (Sales price + renovation costs) (lower of the two)		
Mortgage Insurance (MI) Required	✓	✓	Down payments less than 20% on a purchase and LTV's > 80% on refinance
Maximum Renovation Amounts	No maximum as long as mortgage amounts are within county guidelines for FHA loans	Up to \$35,000	50% of the as completed value
Allowable Repairs	From structural changes to landscaping, new appliances and more	From flooring to painting, remodeling kitchen/bath, appliances and more. No major remodeling, structural repairs or landscaping	From structural changes to landscaping, new appliances and more

*Down payment and other figures shown are for informational purposes only and are not intended as an advertisement or commitment to lend. Not all borrowers will qualify; contact us for an exact quote.

Section 3: Bonus Choices & More Resources

ENERGY EFFICIENT UPGRADES

Green is the “buzzword du jour” still. Energy efficiency is both Earth-friendly and good for the long term budget of the consumer. Longer-lasting light bulbs that use less energy, more efficient furnaces, and better windows help reduce pollution and save you money. These items are also covered under the various home improvement loans at your fingertips. These are different from the specific “energy efficient mortgages” you may have heard about, but these renovation mortgages solve the same basic issues.

The amount of money you might save with an energy efficient furnace will vary depending on several factors. However, one potential savings table we found showed a 2-story home of about 3,000 square foot can save around \$300-\$400 per year. That can add up when you also replace windows, weatherize the home and change the lighting. Making your home more energy efficient can save a lot of money over the course of several years.

Potential “green” items covered by home improvement loans:

- New windows
- New doors
- Furnace/duct work
- Air conditioner
- Weatherization
- New siding/insulation
- Efficient washer, dryer, refrigerator
- Water heater

A renovation mortgage allows you to buy the house in its current condition and assume the responsibility of making the necessary repairs.



Renovation Consumer Tips

Please review the important tips listed below about Renovation Mortgages and home improvement projects.

- For the Renovation Mortgage, you do not receive any cash at the loan closing. The funds provided for renovation are placed in an interest-bearing escrow account (Renovation Escrow Account).
- The lender may require that a contingency reserve be placed in the Renovation Escrow Account to cover unforeseen repairs or deficiencies during the renovation. If funds remain after the renovation is complete, they can be applied to additional elective repairs or improvements or can be used to reduce the principal balance. If you deposit funds into the account, the funds you deposited can be paid directly back to you at your option.
- When selecting a contractor always review the contractor's references, licensing, and financial background. Ask the lender for a Contractor Profile form to assist in your review
- You are responsible for negotiating any agreements or warranties with the contractor. The lender does not provide any warranty on the contractor's work.
- You are responsible for overseeing the renovation and ensuring that it is done as specified in the Construction Contract with the contractor. If work stops for an extended period of time, or there are problems with the work performed that may cause significant delays, you must contact the lender.
- If you are purchasing a home to renovate it, please note that the lender does not warrant or guarantee the condition of the property being purchased or the renovation.
- You are responsible for making the mortgage payment each month, even if the renovation is not satisfactorily completed.
- Funds for the renovation are paid in accordance with a schedule acceptable to you, the contractor, and the lender.

Funds are released to the contractor after an inspection of each phase of the renovation. The funds are provided in a check made payable jointly to both you and the contractor. You request these payments on a draw request form submitted to the lender.

- Do not approve funds be released to the contractor if you are not happy with the work. Do not accept unsatisfactory work.
- Do not pay the contractor "up front" out of your own funds before the renovation is satisfactorily completed.
- The lender may withhold some of the funds from each Draw Request. These funds are paid to the contractor when the work is completed. This helps to protect you from a contractor failing to complete the renovation
- If you would like to revise the original approved renovation, you must submit a Change Order Request to the lender for approval, and deposit any additional required funds (including contingency reserve) in the Renovation Escrow Account.
- When the renovation is completed, you and the contractor sign a Completion Certificate. The lender should provide you an accounting for all distribution of funds in the Renovation Escrow Account

Borrower Needs and Expectations FAQ's

What does the Renovation Department do for me?

Your Renovation Specialist will help you with getting the bids from your Contractor. They will, once you have chosen a Contractor, send out all Renovation forms to your Contractor. They will also will order and review the appraisal with the final bids from your Contractor. "AFTER" the Loan Closes, Your Renovation Specialist will then introduce you to your Renovation Coordinator. Your Renovation Coordinator will then Set Up and manage your Renovation Account. They will be with you throughout the entire Renovation period assisting you and your Contractor with all draws. When you do have questions, please call your Loan Officer and/or Renovation Specialist. So, you see you will not be left alone. You have a whole Renovation Team behind you all the way to completion.

How much can I borrow?

This depends on your repair and improvement needs. Also, it will depend on the Appraisal "As-Is" and "After Improved" value. Your Loan Officer and Renovation Specialist will help you choose the right program. For a better idea of how much you can borrow please take a moment to write down a list of wants, (Additional improvements wanted) and needs, (Property repairs immediately needed) this is called a "Scope of Work". Give this list to your Loan Officer.

What repairs can I do?

Depending on your "Needs" list, you can Repair/Replace and even add on to an existing home. Some Renovation Programs will also allow you to Repair/Replace or add "Outdoor" items such as decks and patios. Check with your Loan Officer to see which Renovation Program, "203k" or "HomeStyle" will work best for you.

Can I do any of the work myself?

Your home may be your biggest investment. All repairs need to be completed by a Professional, Licensed and Insured Contractor.

Can a Family member do the work?

If they are Licensed in the field that the repair is for and have Liability Insurance, yes, by exception only.

Where do I find a Contractor?

- Websites such as angieslist.com, homeadvisor.com, etc.
- Home improvement retailers such as Lowe's, Home Depot, etc.
- Word-of-mouth recommendations from family, friends and acquaintances.

How Long will the Renovation take?

All Renovations need to be done in a timely manner. When you have completed your "Scope of Work" you can discuss this with your Renovation Specialist for a better idea of time frame needed to complete Renovations. Note that all work must start within 30 days.

What if I am unhappy with the work completed?

Call your Renovation Specialist and Renovation Coordinator right away! They are there to help with any concerns that may arise between you and your Contractor. The Renovation Department will always try to help you in any way we can to solve problems.

What do I do when all repair/improvements have been completed?

Closing out the Renovation Escrow:

- Notify the Renovation Coordinator that all work has been completed.
- Renovation Coordinator will prepare the "Letter of Completion" and send to you with the final draw request.
- Final Appraisal and Title Work are ordered
- Contractor "Holdback" Draws are prepared and sent to the contractor.
- Renovation Escrow is finalized and a copy sent to the Borrower
- Renovation Escrow is Closed Out.
- Borrower is notified that the Renovation Escrow is Closed Out.

LET US KNOW HOW WE CAN HELP

For more than 20 years, Service First Mortgage has helped first time home buyers realize the dream of leaving that rental behind, and owning a house. Whether it's conventional lending, an FHA program, VA loan, USDA Rural Development or a 203k mortgage loan, the team at Service First is here to find the right mortgage for you.

WE'RE EASY TO FIND

The website: www.MortgageProsUs.com

We're on other social media sites as well.



Read the blog and keep up with the industry so you can be an informed borrower.

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