

## The FHA Section 203(k) Rehab Loan Program

### **Loan Description**

The FHA Section 203(k) insurance program enables borrowers to finance the purchase or refinance of a home and the cost of its rehabilitation through a single mortgage.

### **Loan Purpose**

Rehabilitate an existing structure that has been completed for at least one year.

Purchase and rehabilitate an existing structure that has been completed for at least one year.

Rehabilitate a structure that has been completed for at least one year and refinance the outstanding indebtedness.

### **Occupancy**

Owner occupied only.

### **Eligible Properties**

Single Family Residences

FHA-approved Condos

Spot Condos

Attached /Detached PUDs

2-4 Units

REO properties.

### **Ineligible Properties**

Cooperatives

Log Homes

Geothermal Homes

Timeshares

Condotels

Geodesic Dome Homes

Commercial Property

Manufactured Housing or Mobile Homes

Non-warrantable condos

Properties with un-permitted additions

Working Farms, Ranches, Orchards

Homes that have never been completed.

Refinance transactions with properties listed for sale in the last 6 months from the application date.

Homes that have been completely demolished, including the foundation.

### **Maximum LTV**

Purchase: Maximum LTV is 96.50%.

Rate/Term Refinance: Maximum LTV is 97.75%. Maximum CLTV is 100%.

Cash Out Refinance: Not allowed

### **Eligible Improvements**

Examples of eligible improvements are listed below, however, this is not an all-inclusive list:

Repair/replacement of roofs, gutters and downspouts.

Repair/replacement/upgrade of existing heating, ventilation & air conditioning systems.

Repair/replacement of plumbing and electrical systems.

Repair/replacement of flooring.

Minor remodeling that does not involve structural repairs, such as kitchens

Exterior and interior painting. (continued on page 2)

Weatherization, including storm windows and doors, insulation, weather stripping, etc.

Purchase and installation of appliances, including free-standing ranges, refrigerators, washers and dryers, dishwashers and microwaves.

Improvements for accessibility for persons with disabilities.

Lead-based paint stabilization or abatement of lead-based paint hazards.

Repair/replacement/addition of exterior decks, patios, porches.

Basement waterproofing.

Replacement of window and doors and exterior wall re-siding.

Most improvements are eligible provided they add value and are permanently affixed to the foundation.

Improvements to detached structures and luxury items are not allowed.

Luxury items include: Swimming pools, hot tubs, tennis courts, gazebos, barbecue pits, etc. Repair work to these items is also not allowed.

### **Eligible Expenses**

Expenses eligible to be included in the cost of rehabilitation are material, labor, overhead and construction profit (noted in each work item), plus expenses related to the rehabilitation such as permits, fees, inspection fees by a qualified home inspector, licenses, inspection fees during construction by a HUD accepted inspector, lien protection fees, for title updates and architectural/engineering fees. The cost of rehabilitation may also include the supplemental origination fee and the discounts which the borrower will pay on that portion of the mortgage proceeds allocated to the rehabilitation.

### **Contractor(s) Requirements**

All loans require that all borrower-selected contractors sign the Homeowner/Contractor Agreement before closing. All contractors must be licensed if required by state. The lender must review the following items pursuant to the proposed contractor:

- Credentials
- Work experience
- Client references from contractor's prior work

### **Rehabilitation Period**

Rehabilitation construction must begin within 30 days of closing and all work must be completed within six months of closing.

### **Self-Help Requirements**

Self-help arrangements in which the borrower is performing some or all of the work items are strongly discouraged unless the borrower's ability to perform the work in a competent, timely, and workmanlike manner is self-evident and easily documented. The self-help option is not allowed for any project for which permits will be required, unless the borrower is a licensed contractor working in the specific field necessary for the rehabilitation.

### **Properties that require the following work items are not eligible for financing:**

Major rehabilitation or major remodeling, such as the relocation of a load-bearing wall;

New construction (including room additions);

Repair of structural damage;

Repairs requiring detailed drawings or architectural exhibits;

Landscaping or similar site amenity improvements;

Any repair or improvement requiring a work schedule longer than six (6) months; or

Rehabilitation activities that require more than two (2) payments per specialized contractor.

### **Appraisal Requirements**

All appraisals for FHA loans must be completed by a HUD-approved appraiser.

The loan-to-value is based on the lesser of:

- The sales price or “as is” appraised value plus borrower paid repairs minus sales concessions, or
- 110% of “as completed” appraised value.

The appraisal report must provide an “as completed” appraised value that estimates the value of the property after completion of the rehabilitation work. The borrower’s or cost consultant’s work write-up must be available for the appraiser to use in order to determine the “as completed” value.

### **Credit**

#### **Credit Scores**

The minimum credit score may not be lower than **620**.

**Valid Credit Score:** For a credit score to be considered valid, the score must be generated from a minimum of (3) trade lines that have been evaluated for at least 12 months. The trade lines do not need to be currently active but require some activity within the last 24 months.

**For borrowers with credit scores of 620 or higher that do not have at least 3 trade lines each with a 12 month history, the credit score will not be considered valid and the loan is ineligible for the 203(k) program.**

#### **Minimum Cash Investment**

The borrower must make a minimum cash investment of 3.5% of the lesser of the appraised or sales value. This amount is in addition to any borrower closing costs.

#### **Sales and Financing Contributions**

Sellers, or other interested parties such as real estate agents, builders, developers, etc., or a combination of parties are permitted to contribute up to 6% of the property sales price toward the buyer’s actual closing costs, prepaid expenses, discount points and other financing concessions. Closing costs normally paid by the borrower are considered contributions if paid by the seller.

#### **Cash Reserves**

Cash reserves are not a requirement for FHA loans except in the scenarios described below. Generally cash reserves are used as a Compensating Factor when approving an FHA loan with a debt ratio that exceeds guidelines. In this case, a minimum of 3 months PITI will be considered as a Compensating Factor. Gift funds, cash proceeds from the refinance and equity in another property are not acceptable sources for documenting cash reserves.

#### **Scenarios with Reserve Requirements (from above):**

**3-4 unit properties:** 3 months PITI after closing are required. Gifts are not an acceptable source.

#### **Temporary Buydowns**

Temporary buydowns are not eligible on the 203(k) program.