

Fannie Mae HomeStyle Renovation Program

Guidelines and Procedures

Towne Family of Companies

Fannie Mae HomeStyle Renovation Program Overview

The Fannie Mae HomeStyle Renovation Mortgage provides a way for borrowers to make renovation, repairs, or improvements totaling up to fifty percent (50%) of the as-completed value of the property with a first mortgage, rather than a second mortgage or home equity line of credit. The funds can be used for any repairs or renovations that are permanently affixed and add value to the property.

Loan Purpose:

1. Refinance and renovate an existing residential property – limited cash out refinance ONLY
2. Purchase and rehabilitate an existing structure.

Key Features:

Allows a borrower to finance both the acquisition of a property (or pay off of existing mortgage debt) plus the rehabilitation of a property in need of repair all in one mortgage loan. Other key features of this program are:

1. No minimum dollar amount requirement for the eligible improvements to the existing structure on the property;
2. All health, safety, and energy conservation items must be addressed prior to completing general home improvements;
3. The scope of work must demonstrate that once the rehabilitation is completed, the property will meet minimum property standards as defined by Fannie Mae.
4. A contingency reserve of 10%-20% is required.
- 5.

General Program Policies

- **Borrower Eligibility** – As per Fannie Mae selling guide
- **Occupancy:**
 - Owner-occupied
 - Second homes
 - Investment properties
- **Transaction Types:**
 - Purchase
 - Limited Cash out Refinance only
- **Loan Terms:**
 - Fixed rate only
- **Maximum Loan-To-Value (“LTV”):** Purchases and Limited cash out refinances

	Principal Residence	Second Home	Investment Property
1 unit	95%	90%	80% purchase 75% Limited cash out
2 units	85%	N/A	N/A
3-4 units	75%	N/A	N/A

- **Sales and Financing Contributions:** Sellers, or other interested parties such as real estate agents, builders, developers, are permitted to contribute the following percentages towards the buyer's closing costs, prepaid expenses, discount points and other financing concessions:

	Primary Residence	Second Home	Investment Property
>90%	3%	3%	2%
>75%, but ≤ 90%	6%	6%	2%
≤ 75% LTV/CLTV	9%	9%	2%

- **Property Eligibility:**

- Eligible Properties:

- ◆ 1-4 unit principal residence
- ◆ 1 unit second home
- ◆ 1 unit investment property
- ◆ Detached PUDs
- ◆ Detached Condos*
- ◆ Condominiums (Exception Basis Only: Subject to HOA/CC&R prior review and permission of proposed work)

- Ineligible Properties:

- ◆ Manufactured Homes
- ◆ Condotels
- ◆ Cooperatives

*When the security property is a detached condo unit, the project must be one for which the proposed renovation work is permissible under the bylaws of the homeowners' association by-laws or one for which the homeowners' association or co-op corporation has given written approval for the renovation work.

The renovation work for a detached condo unit must be limited to the interior of the unit, including the installation of fire walls in the attic.

- **Loan Amount:** Fannie Mae conforming loan limits
- **Underwriting:** DU – approve/eligible only
- **Minimum FICO Score:** Minimum credit score of 620 is required. Loan must be Approved/eligible through DU.

Documentation Required:

Additional documentation is required supporting the rehabilitation portion of the HomeStyle Renovation loan as follows:

- HomeStyle Renovation Maximum Mortgage Worksheet (“MMW”) (Form 1035)
- *Construction Loan Agreement (Form 3735) – signed at closing
- Contractor Profile Report (Form 1202) and supporting documentation
- Contractor Bid’s or Plans and specification of Repairs, listing all repairs as shown in the appraisal
- Construction Contract (Form 3734)
- HomeStyle Renovation Consumer Tips (Form 1204)
- *Construction Addendum Amending Note (Form 3736) – signed at closing
- *Construction Loan Rider to Security Instrument (Form 3737) – signed at closing
- If applicable, Investor Rider to Security Instrument (Form 2728) – signed at closing

Renovation-related costs:

Renovation-related costs that may be considered as part of the total renovation costs include:

- Draw Administration fee – Fee equal to greater of 1.50% of the rehab portion of the mortgage or \$500
- Draw inspection fees (\$175.00 per draw)
- Costs and fees for the title update (\$150.00 per title update)
- Architectural and engineering fees
- Independent consultant fees
- Costs for required permits

Maximum Loan Amount:

Maximum Mortgage Worksheet (Fannie Mae Form 1035) is used to calculate the maximum loan amount and LTV. See “Maximum Loan-To-Value” section for more information.

- Maximum loan amount is calculated as follows:
 - Purchase: max allowable LTV (as stated above) multiplied by the **lessor** of the purchase price plus improvement costs, or “as completed” appraised value of the property.
 - Refinance: max allowable LTV (as stated above) multiplied by the “as completed” value of the property.
 - Loan amount is based on the amounts shown on the HomeStyle Renovation Maximum Mortgage Worksheet ([Form 1035](#)). The maximum mortgage calculation differs based on the applicable transaction type. See “Maximum Loan-To-Value.”

Limited cash out refinance:

When a HomeStyle Renovation mortgage loan is originated as a limited cash-out refinance transaction, the mortgage amount may include the amount required to satisfy the existing first mortgage, the amount required to satisfy any outstanding subordinate mortgage liens that were used to acquire the property, closing costs, prepaid, points, and the total renovation costs, including allowable renovation-related costs for the home improvements up to the maximum permitted LTV and CLTV ratios.

However, the borrower may not obtain any other funds from the transaction, including those that are generally allowed for a limited cash-out refinance transaction (i.e. max 2% or \$2,000).

Excess funds if any, after renovations are completed, may be applied to the loan balance as a curtailment or may be reimbursed to the borrower for the cost of actual supplies or additional renovations for which paid receipts are provided. The value of sweat equity may not be reimbursed.

How the program works

- **Eligible Expenses:**

- Expenses eligible to be included in the cost of rehabilitation are materials, labor, contingency reserve, overhead and construction profit, plus expenses related to the rehabilitation such as permits, draw inspection fees during construction by a consultant/inspector, title update fees and architectural/engineering fees.
- The full loan amount is funded at closing. The funds reserved for the rehabilitation, including any contingency reserve, inspection fees, title update fees and mortgage payment reserve, must be set-up in an interest-bearing repair escrow account and the balance dispersed to purchase the property or refinance an existing mortgage. At the completion of work, any interest earned or unused rehabilitation funds will be applied towards a principal curtailment (see “Contingency Reserve” for more information).

- **Contingency Reserve:**

- A contingency reserve must be established to allow for cost over-runs or additional repairs that are discovered during the course of rehabilitation. The contingency reserve is minimum 10%. Higher contingency amounts (up to 20%) may be required depending on property age, scope and complexity of the rehabilitation project, and at Renovation Loan Specialist’s discretion. A minimum 15% contingency will apply when utilities are off.
- The amount of the contingency required can be funded by the borrower at close. If the borrower funds the contingency reserve with their own funds, any funds remaining after the completion of the scope of repairs identified will be returned to the borrower up to the amount brought in by the borrower at closing.
- When adjustments to the proposed rehabilitation (i.e. deleting a non-essential item from the scope of work) are made following loan closing, the amount by which the costs are reduced are added to the contingency reserve. Work items cannot be deleted from the rehabilitation if it will decrease the value of the home.
- Change order Request Form must be completed when the scope of rehabilitation will be affected.

- **Mortgage Payment Reserve:**

- When the property cannot be occupied during rehabilitation, funds not to exceed six (6) Mortgage payments, including PITI and mortgage insurance, can be included in the cost of rehabilitation and deposited into renovation escrow account.
- The number of mortgage payments cannot exceed the completion timeframe required in the rehabilitation loan agreement.
- The monthly mortgage payment must be made directly from the interest-bearing reserve account. These payments will be handled by the Servicing and Accounting departments.

- Funds that remain in the account after the final release notice is issued must be used to reduce the principal through a principal reduction, unless the funds were provided by the borrower, in which case the funds will be returned to the borrower.
- **Rehabilitation Period:** Rehabilitation construction must begin within thirty (30) days of closing must not cease for more than a thirty (30) day period and all work must be completed within none (9) months of closing.
- **Appraisal Requirements:** All appraisals must be ordered through one of Towne Mortgage's approved Appraisal Management Companies.
- **"As Completed" Value:** The appraisal report must provide an "as completed" value that estimates the market value of the property upon completion of the proposed rehabilitation and/or improvements. The APPROVED work proposal/Contract must be provided to the appraiser to use in order to determine the "as completed" value, and therefore must be provided prior to requesting the appraisal. The appraisal report should be noted: "subject to repairs, alterations etc."
- **Property Insurance Requirements:**
 - Property hazard and flood insurance policies apply on all transactions. Please refer to our Hazard Insurance Policy guidelines for specific requirements.
 - Builder's risk policy is required for construction of property additions or any large scale rehabilitation project.

File Submission for Contractor and Project Review

Contractor and project review will be completed by Towne Mortgage Company Renovation Specialist in our Draw Administration Department.

Once all contractor/project review documents are received, determination of eligibility will be provided in 48 hours.

Contractor Requirements

All renovation work must be performed by a licensed contractor or licensed builder

Towne Mortgage Company **does not** allow Self-Help Agreements (Borrower may not complete the renovation). Contractors also MAY NOT have an identity of interest with the borrower (i.e.; may not be a family member or employer)

A borrower must choose his or her own contractor to perform the needed renovation, subject to the lender's determination that the contractor is qualified and experienced, has all appropriate credentials required by the state, is financially able to perform the duties necessary to complete the renovation work in a timely manner, and agrees to indemnify the borrower for all property losses or damages caused by its employees or subcontractors.

The lender or any other party (such as real estate agent) may not choose the contractor or refer the borrower to any one specific contractor. Borrower's MAY NOT use any contractor listed on Towne Mortgage Company Contractor/Consultant Exclusionary list.

Contractor Review Documentation:

- Contractor's current unexpired license
- Fully completed Contractor Profile form (Fannie Mae Form 1202). Must provide references for at least two recently completed rehabilitation projects.
- Copy of current insurance policy – must have at least \$300,000 in liability coverage
- Fully Completed W-9 form
- Workman's Compensation Insurance: Evidence of Worker's Compensation insurance, if Contractor has employees. If no employees, a Certificate of Exemption or a letter from the contractor stating he/she has no employees is required.

Contractor review process:

- Contractor's name will be checked against the Towne Mortgage Contractor Exclusionary List. If contractor is on list, all parties will be notified that contractor will not be approved.
- Contractor/Builder Requirements: The qualifications of the renovation contractor are evaluated to determine if they have the requisite experience to perform and complete the proposed renovation work, as well as the credit worthiness to pay their obligations and deliver the home free of mechanics' liens. The Contractor information is gathered through a completed Renovation Contractor Profile Form.
- Licensing and Certifications: Current contractor license information is reviewed on the State website where property is located to make sure license is active and not expired. If a contractor is in a local area that does not require licensing, homeowner, subcontractor or supplier references must be checked. In addition, any certifications the contractor has acquired should be provided.
- State website, Better Business website and google will be checked to verify builder/contractor does not have any open complaints or negative reporting.
- Liability Insurance: Evidence of liability insurance in an aggregate amount of at least \$300,000 is required.
- Workman's Compensation Insurance: Evidence of Worker's Compensation insurance, if Contractor has employees. If no employees, a Certificate of Exemption or a letter from the contractor stating he/she has no employees is required.
- Tax Information: Receipt of a W-9 form from Contractor. This requirement cannot be waived due to Federal Law.
- Contractor must have a minimum three year experience in home renovation. Must hold full builder's license for projects consisting of additions where GLA will be increased or projects involving major structural modifications.

Project Review

Contractor bid/ Plans and Specifications

- The contractor bid/plans and specifications must be prepared by a licensed general contractor. The plans must break down costs for each specialized repair or improvement and fully describe all work to be done including the nature and type of repair and materials to be used (i.e.: granite countertops, oak hardwood flooring, Cherry cabinets). The contract MUST break out material and labor costs.
- A proposed draw schedule of when various jobs or stages of completion (including both the start and completion dates) is required.
- Architectural drawings completed by general contractor or architect will be required for all property additions involving increase in Gross Living Area (GLA) OR modification or adjustment to floor plans (e.g. moving walls regardless of structural load transfers). Architectural Exhibits must show the layout and dimensions of the proposed project. Engineer Reports may be required for

foundation & structural repairs.

- Feasibility Study can be prepared by HUD Consultants, FHA Fee Inspectors, General Contractors (independent from subject project), Architects, or Renovation Consultants. Feasibility Studies should include information about the property condition, floor plan sketches (if changes are proposed), specification of proposed work or line items, and cost estimates. It is the responsibility of the loan officer to determine in the initial borrower interview if, based on the project proposed, a Feasibility Study should be ordered.
- General Contractor is required who will oversee and assume responsibility for all sub contracted work. Exception may be made where scope of work consists of system replacements ONLY such as roofs or HVAC. In this case, contractor must hold current license for specialized work.

Towne Mortgage construction specialist will review the plans and specifications and evaluate the quantity, quality, and cost of the renovation work to be done and to determine the amount of financing that will be available. These plans and specifications also must be used by the appraiser in the development of his or her opinion of the “as completed” value of the property

Towne will obtain a Lexis/Nexis or similar report to check for relationship w/ other entities, litigation history, financial health, and any other negative reporting

Appraisal Completed

Once appraisal is completed, the underwriter will review and evaluate the appraisal and conditions to confirm FNMA HomeStyle requirements and scope of work is met, ensure the project is program compliant, and feasible.

POST CLOSING AND DRAW ADMINISTRATION

When a HomeStyle loan closes:

Draw administration specialist will confirm closing amounts, closing documents, and renovation escrow balances are correct. All renovation escrow funds will initially be deposited into the lender's rehabilitation escrow account.

DRAW ADMINISTRATION

Throughout the rehabilitation period, our Draw Administration team will be available to:

- Manage the draw process;
- Address inquiries by all parties of interest;
- Manage inspections, draws, and related support.
- Detailed customer service phone and email logs will be maintained for support and audit purposes.

Welcome Call:

After initial set-up, the borrower and contractor will both receive a welcome call that describes in detail the draw procedures including, but not limited to:

- Draw submission,
- Requisite forms,
- Inspection procedures, and
- Respective duties and responsibilities of the borrower and the contractor.
- The borrower and the contractor will be informed that any changes to the original plan must be approved prior to any work beginning to avoid the risk of having disbursements delayed or withheld.

Commencement of Construction:

- Construction on the project must commence within thirty (30) days of the Note Date. Required permits must also be received within thirty (30) days of the Note Date.
- Rehabilitation progress will be monitored per below:
 - Thirty (30) days from close: if no inspection/draw has been requested, the borrower and contractor will be contacted to determine the progress of construction. Tracking screens will notate conversations with parties.
 - Sixty (60) days from close: if no inspection/draw has been requested, a status inspection will be scheduled to determine project progress. If the inspection finds that work is not being performed on a timely and compliant basis, a written action plan for completion will be developed with the contractor and borrower. All parties will sign the agreed to written plan.

- Ninety (90) days from close, verification that the action plan has been implemented will be obtained. If deemed necessary, a status inspection will be scheduled to verify that the action plan is being properly executed.

Inspections:

- Draw inspection requests will be made via a completed Draw Inspection request form signed by contractor and borrower.
- Inspections will be completed by the appraiser or Consultant.
- Inspections will be done to confirm the work is in place and complete per each draw request. The scope of inspection will include the entire budget and will be on a line by line basis. Work completed will be noted as a percentage of each line item.
- Inspections will be submitted with a field report along with pictures of all work completed.
- Payment will not be made for materials that are not installed or work that has not been completed.

Completion of Construction: Construction on the project must be completed within Nine (9) months of the Note Date, unless an extension has been requested and granted pursuant to FNMA guidelines. If construction is not complete and an extension is not granted, the loan will be considered to be in technical default for non-performance/Suspension of Construction.

Customer Service:

Throughout the rehabilitation period, our Draw Administration team will be available to:

- Manage the draw process;
- Address inquiries by all parties of interest;
- Manage inspections, draws, and related support.
- Detailed customer service phone and email logs will be maintained for support and audit purposes.

Draw Processing and Funds Disbursement Overview:

- Draw Requirements - Detailed
- Draw requests must be applied to specific budget line items. Individual line items cannot be overdrawn. The amounts allocated to individual lines, and the total of the draw must reconcile.
- The expiration dates for the contractor's license and insurance, as well as the twelve (12) Month loan rehabilitation expiration date is tracked by Draw administration specialist
- No draw will be approved unless all such license or insurance are current. If the contractor's insurance or license has expired, proof of renewal will be obtained prior to any draws.

- With respect to the expiration date of the 12 rehabilitation period, no draw will be paid past this date without the proper written extensions being obtained.

With each draw, a draw transmittal package is required consisting of:

- Draw Inspection completed by appraiser or consultant stating the percentage of line item work completed in each category
- Condition lien waivers sign by contractor
- Copies of any required permits and final inspections required by local bldg. authority for repair items complete

Holdback: A 10% retainage will be netted from each total draw request. The holdback will be released with the final draw.

Draw Processing and Funding: Upon receipt of the draw transmittal package, it is reviewed and approved by Draw administration specialist. The signed draw approval is then used to request funds from Servicing and to be used for payment to all approved payees.

Other Disbursements

- Monthly Mortgage Payment from Reserves:
 - If a reserve for the monthly mortgage payment was established at closing, the monthly mortgage payment must be made directly from the interest bearing reserve account. Payment will be made by the 5th of each month by the servicing department of the lender.

Expiration of Rehab period: Prior to the release of any draw, the completion date of the construction period will be checked. Loans that have exceeded the construction period without being extended will have funding suspended and require that work on the project cease until extension is executed.

Final Draw Processing and Funding:

The final draw requires additional documents to be included in the Draw Request Package. These documents are as follows:

- An inspection showing work has been completed to 100%;
- Certificate of Occupancy, permit sign-off or other local equivalent, where appropriate;
- Completion Certificate (Form 1036);
- Final Release Notice;

- Contingency Release Letter;
- Any other State Statutory required documents.
- The final draw will be processed and funded following the same procedures for all other draws.

At the time of final disbursement, any construction budget funds and contingency will be applied to the outstanding principal balance of the renovation loan, except when the borrower funded the contingency. In this case, the remaining contingency funds will be returned to the borrower.

Contingency/Change Orders:

- All contingency requests will be reviewed with regard to the appropriateness of amount and timing. If the change order is deemed acceptable, the request will be approved or if deemed unacceptable the amount may be adjusted accordingly.
- As a general rule, a change order or a proof of payment/receipt is required to process draws from the contingency. The cost of a change order will be paid out of the contingency fund. In the event that the contingency fund is inadequate, the fee must be paid by the borrower.
- Contingency reserve funds may be used for cost overruns and related changes associated with the mandatory work items as detailed in the defined scope of work.
- If funds are remaining after the completion of the mandatory work items, they may be used for property improvement “upgrades” per FNMA guidelines, but generally these upgrades will be in line with the scope of work which has already been approved.
- Unused contingency funds will be applied as a principal reduction to the mortgage, or if funds were provided by the borrower, funds will be returned to the borrower.

Line Item Transfer:

- During the draw process there may be a need to transfer funds from one line item to another. Evidence savings must be verified in the surplus line item, and a change order with additional costs must be submitted and verified before surplus funds from another line item can be utilized to fund the deficient line item.
- If applicable, surplus funds may be transferred into the contingency reserve from lines that have been inspected to 100% complete and proof of payment to the subcontractor and/or supplier has been received.
- Lien Release Policy: In order to protect the collateral value of the home we must ensure that subcontractors and suppliers have been paid. Invoices and lien releases from the General Contractor(s) and certain other support in accordance with generally accepted best practices will be required with each draw.
- Some states require a State-specific lien release to be used. In those states, the required State-specific form must be used; otherwise, the standard Waiver of Lien forms will be used.
- Title Update Policy: Title updates will be made on each draw. Draws will be funded only if the

title update reflects that there are no mechanic's encumbering the property.

- If a lien is filed on the project, all construction will be suspended until the issue is resolved satisfactorily;
- All specific statutory pre-lien notices, lien notices, or communications regarding non-payment of subcontractors or suppliers must be forwarded to the Draw Administration Team

Non-Performance - Suspension of Construction

- Towne Mortgage complies with Fannie Mae Homestyle Renovation Guidelines in regards to the uninterrupted continuation of work, and compliance with all HomeStyle construction and completion guidelines.
- Project rehabilitation non-performance includes, but is not limited to: inability to complete rehabilitation work in the required timeframe, refusal to complete Fannie Mae minimum property repairs, expanding improvements without prior written approval, absence of occupancy by primary or co-borrower in required timeframe, liens filed on the property and are not cleared, changing contractors without prior written approval by Towne Mortgage or if construction ceases on the property for more than thirty (30) days.
- Loans that remain non-performing for sixty days (60) days will require further action and no further draws from the Rehabilitation Escrow Account will be allowed.

Contractor Replacement Requirements:

In the event a contractor needs to be replaced, the following is required:

- A written letter from the Borrower requesting that the existing Contractor be replaced including the reason for the replacement and a list of all known liens recorded or pending.
- A written release from the current contract signed by BOTH borrower and contractor.
- A fully completed *Contractor Profile Form* with all required documentation the new Contractor.
- A fully executed Renovation Contract from the new general Contractor to complete the project, and verification that the remaining funds are sufficient to complete the project. The contract is required to be compliant with the requirements
- If the new budget is greater than the amount left in the renovation escrow account, then the borrower must supply his/her own funds which must be deposited into escrow account in order to insure adequate funds are available to complete project. NOTE: It is possible for these additional funds to come from the existing contingency account as long as the contingency funds are still adequate to meet the requirements of its purpose.
- A final lien waiver executed by the original Contractor.
- A current title update.
- All other Contractor Acceptance requirements apply.

Extensions:

- Extensions of the original completion date may be requested up to an addition 90 days may be granted, due to unforeseen circumstances only.
- A written request for extension must be submitted, including the reason for delay and new completion date, and must be signed by both Contractor and Borrower. Extensions requests, with adequate documentation, must be submitted to Towne Mortgage Draw Administration Department for review and approval PRIOR TO EXPIRATION OF THE INITIAL 9 MONTH REHABILITATION PERIOD.
- An extension can only be granted if the loan payments are current. Extensions will be required when necessary before any disbursement can be made.

Non-Performance Default

- In the event of a non-performance default, Towne Mortgage Loans will work with the borrower and contractor to review the available risk mitigation alternatives. Towne Mortgage has the option to call the mortgage loan due and payable.
- The funds remaining in the account may be applied to reduce the mortgage principal.

Annual Year-End Reporting:

- In order to satisfy annual 1099 IRS Reporting requirements, Towne Mortgage will perform the following:
 - Obtain completed IRS Form W-9's from all payees of funds as such may be required by applicable IRS rules and regulations. Prepare, issue and mail Form 1099-MISC using Banc Home Loans' EIN to all payees of funds and submit applicable reports on an annual basis in compliance with IRS guidelines and time requirements.
 - Prepare report and provide to borrowers all interest earned by borrowers from the funds held in the rehabilitation accounts in the form of an IRS Form 1099-INT on an annual basis in compliance with IRS guidelines and time requirements.