VA Renovation Loan Basics

- Purchase and Refinance Options
- Used to finance minor remodeling and non-structural repairs
- There is no renovation consultant requirement
- Fully Amortizing Fixed Rate
- 10 year, 15 year, 20 year, 25 year, and 30 year term options
- One or Two Unit Homes
- Primary Residence Only

What are the benefits?

100% Financing

VA mortgages offer one of the only no money down home financing options available in the marketplace. This is a huge advantage to qualifying veterans, military personnel, and their families, who can become homeowners without waiting many years or depleting their savings.

Low Mortgage Rates

The VA Renovation Loan makes it possible to finance both the purchase or refinance of a home and the cost of repairs or updates in one low rate, first mortgage loan. This can offer considerable savings when compared to a higher rate second mortgage, using other types of credit such as credit cards, or a home equity line of credit with a variable interest rate that could increase over time.

Who is eligible for a VA Renovation Loan?

As with any VA loan the borrower must be a qualifying active duty member of the US military, veteran, or surviving spouse. Other requirements of this program include:

- Repairs must be minor remodeling or cosmetic in nature and not on the list of ineligible repairs
- Construction must be completed within four months of closing
- Only one General Contractor may be used
- General Contractor must be registered with the VA
- General Contractor must carry sufficient insurance through a current general insurance liability policy
- 620 minimum FICO score

Veterans Benefits Administration
Department of Veterans Affairs
Washington, D.C. 20420

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Loans for Alteration and Repair

1. Purpose. This Circular replaces Chapter 7, Topic 4, *Loans for Alteration and Repair*, in the Department of Veterans Affairs (VA) Lender's Handbook, 26-7.

2. Background. VA has received inquiries regarding the procedures to process loans for alteration and repair. The Aging housing stock in the United States has contributed to the increased demand for alteration and repair loans. Due to the condition of this aged housing, homes are often sold as "cash or conventional financing" which does not allow Veterans to use their VA earned benefit. This guidance will allow Lender's to make VA-guaranteed loans to Veterans who wish to purchase or refinance a home that is in need of alteration and/or repair. The terms alteration, repair, renovation, and improvement are interchangeable for the purposes of this Circular.

3. Policy. VA may guarantee a loan for alteration and/or repair that allows improvements to be included in the value and completed after closing of the loan. The loan proceeds are paid out to the builder and/or contractor during the alteration/repair period. The lender must obtain written approval from the borrower before each disbursement or draw payment to the builder and/or contractor.

a. Eligible VA Loan Types. The types of alteration or repair loans eligible for VA guaranty upon completion of the improvements are VA purchase loans, and VA regular (aka Cash-Out) refinance loans. Alteration and repair loans must adhere to the VA Lender's Handbook, 26-7, Chapter 3.

(1) Loans for alteration and repair in conjunction with a purchase: this allows the Veteran to purchase a home that needs improvement, or where the buyer wants to alter the home to their preference. It is mandatory to use the lesser of the as-completed value, or the acquisition costs in the transaction.

(2) Loans for alteration and repair in conjunction with a refinance of an eligible residence already owned and occupied by the Veteran: this allows the Veteran to refinance the existing loan and use the as-completed value in the transaction.

b. Credit and Underwriting. Loans for alteration and repair are underwritten in accordance with the VA Lender's Handbook, 26-7, Chapter 4.

c. Property Eligibility and Appraisals. The property and appraisal requirements for alteration and repair can be found throughout the VA Lender's Handbook, 26-7, Chapter 10 and 16. All VA minimum property requirements (MPR), outlined in the VA Lender's Handbook, 26-7, Chapter 12, must be met prior to issuance of the Loan Guaranty Certificate (LGC) and the final inspection/certificate of occupancy.

d. Eligible Alterations and Repairs. Eligible alterations and repairs must be those ordinarily found on similar properties of comparable value in the community.

e. Acquisition Cost versus Value.

(1) Loans for alteration and repair in conjunction with a purchase must use the lessor of the acquisition cost or the as-completed value determined by the VA fee panel appraiser. To determine the acquisition costs for a purchase, add the following: Contract sales price, total cost of alterations and repairs, contingency reserve (if any up to 15 percent of the repair cost), inspection fees, title update fees, and permits.

(a) Contract sales price $100,000, alterations and repairs $75,000, contingency reserve of $7,500, inspection $250, permit $250, for a total acquisition cost of $183,000. Notice of Value (NOV) is $180,000. The lesser amount of $180,000 is to be used as the acquisition cost and the borrower must bring $3,000 to closing. This is not considered downpayment as it is greater than the value.

(b) Contract sales price is $100,000 alterations and repairs are $75,000, contingency reserve of $7,500, inspection $250, permit $250, for a total acquisition cost of $183,000. Notice of Value (NOV) is $190,000. The lesser amount of $183,000 is to be used as the acquisition cost. Therefore, the entire acquisition cost of $183,000, plus the funding fee may be financed.

(2) Loans for alteration and repair in conjunction with a refinance must use the lessor of the acquisition cost, or the as-completed value determined by the VA fee panel appraiser. To determine the acquisition costs for a refinance, add the following: Existing loan payoff, total cost of alterations and repairs, contingency reserve (if any up to 15 percent of the repair cost), inspection fees, title update fees, and permits.

(a) Payoff is $200,000, alterations and repairs are $25,000, contingency reserve of $2,000, inspection $250, permit $250, for a total acquisition cost of $227,500. NOV is $220,000. The lesser amount of $220,000 is to be used as the acquisition cost and the borrower must bring $7,500 to closing, or reduce the project costs and obtain a reconsideration of value based on the adjusted alteration and repair costs.

(b) Payoff is $200,000, alterations and repairs are $25,000, contingency reserve of $2,000, inspection $250, permit $250, for a total acquisition cost of $227,500. The NOV is $230,000. The lesser amount of $227,500 is to be used as the acquisition cost and the borrower may finance the entire project cost of $227,500. In addition, the borrower may finance closing costs, prepaids or take cash-out, up to 100 percent loan to value.

(3) Contingency Reserve. A contingency reserve is not required, however, a lender should consider a contingency reserve if the project warrants such a reserve. The maximum contingency reserve is 15 percent of the alteration and/or repair cost. In a purchase, any unused contingency reserve funds must be applied to the principal balance, unless it was paid in cash at closing by the borrower. In such a case, it can be returned to the borrower. In a refinance, any

unused contingency reserve funds may be returned to the borrower or applied to the principal balance at the borrower's discretion.

f. Builder and Contractor Registration Requirements. For any property appraised for alteration and repair, the builder, or contractor must have a valid VA builder identification number prior to a VA NOV being issued. For information on obtaining a builder identification number see the VA Lender's Handbook, 26-7, Chapter 10. The builder or contractor must be registered with VA. A list may be found at https://vip.vba.va.gov/portal/VBAH/Home. Instructions to become a registered builder with VA can be found at https://www.benefits.va.gov/HOMELOANS/appraiser_cv_builder_info.asp. Borrowers are free to choose their builder or contractor, subject to any additional requirements the lender may require. It is the lender's responsibility to ensure that the builder or contractor is licensed, bonded, and insured according to all state and local requirements.

g. The Process. The list below is a general guide for Lender's to follow when processing a VA Alteration and Repair loan. It is not meant to be inclusive of all steps.

(1) Verify Veteran eligibility in WebLGY (VA Lender's Handbook, 26-7, Chapter 2)
(2) Qualify the borrower(s) (VA Lender's Handbook, 26-7, Chapter 4)
(3) Determine the scope of the alteration and repairs (VA Lender's Handbook, 26-7, Chapter 10)
(4) Order the appraisal as appropriate (VA Lender's Handbook, 26-7, Chapter 10)
(5) Underwrite the loan (VA Lender's Handbook, 26-7, Chapter 4)
(6) Issue the NOV (VA Lender's Handbook, 26-7, Chapter 13)
(7) Close the loan
(8) Establish the draw account. The lender must deposit dedicated alteration / repair funds in a custodial escrow account. These funds may not be comingled with other lender funds.
(9) Pay the funding fee within 15 days of loan closing (VA Lender's Handbook, 26-7, Chapter 8)
(10) Work commences
(11) Funds are disbursed as progress is verified and approved by the Veteran
(12) VA MPRs are met (VA Lender's Handbook, 26-7, Chapter 12)
(13) Certificate of Occupancy (if applicable)
(14) Final inspection by the VA fee appraiser signifies the end of the project (VA Lender's Handbook, 26-7, Chapter 14)
(15) Guaranty the loan (VA Lender's Handbook, 26-7, Chapter 5)

h. Change Orders. Borrowers are permitted to pay for change orders and upgrade out of pocket. Change orders/upgrades made after the appraisal cannot be mortgaged into the new loan, unless the appraisal is updated. Change orders must be approved, in advance, by the appraiser, to ensure there is no loss in value. If an appraisal is to be updated, the lender is responsible for contacting the appraiser with the documented change order(s). The lender should contact the Regional Loan Center (RLC) of jurisdiction for assistance, if needed. The Veteran is allowed to pay an additional appraisal charge if change orders are requested. This additional appraisal charge may come out of available contingency reserve funds.

i. Alteration and repair project management. The lender is responsible for all aspects of establishing the account containing the alteration and repair funds. The lender must ensure that funds are accounted for and disbursed according to the progress completed. The lender should have the specialized experience to process, underwrite, close, and set-up the loan in progress (LIP) account or draw account.

(1) Any remaining funds in the LIP account upon completion should be disbursed according to the contract. If the remaining funds are the borrowers, re-imbursement is acceptable up to the verified amount that has been paid in advance; otherwise the funds must be applied to the loan balance.

(2) In addition, the lender has the responsibility to evaluate, monitor, and manage the project. It is the lender's responsibility to ensure that the project is completed per the plans, specifications, and /or contract documents, so that the value of the home is preserved.

(3) When a project is primarily cosmetic (i.e. carpet, paint, minor repairs) and does not require permitting and inspection from the local authority, the lender may condition the NOV for lender certification "or" may condition for appraiser reinspection/certification. Lender certifications in these cases reduce, days to finalize loans and obtain guaranty and/or may promote financial savings (i.e. reinspection fees) benefiting Veterans.

(4) If the project requires permitting and local authority inspections or requires detailed construction exhibits to be provided to the appraiser, the lender "must" condition the NOV for appraiser reinspection/certification. This ensures compliance with exhibits and information used in the preparation of the subject's valuation.

(5) Specifications for materials to be used in projects must be provided to the appraiser for consideration in the preparation of the appraisal report. If renovations require permits and local authority inspection and/or require building plans, these exhibits along with any materials specifications "must" be provided to the appraiser at the time of appraisal order to be utilized in the preparation of the appraisal report for valuation purposes. Appraisers will "hold" appraisal assignments until the appropriate exhibits are received. The appraiser should contact the point of contact (POC) if not received within one day of appraisal order and "must" put notes in the case in WebLGY.

(6) Any re-inspections by the appraiser must ensure that the completed renovations meet at least the minimum specifications originally utilized in preparing the appraisals final value. The use of any lower grade materials or deviations that may lower the original value provided in the appraisal report must be noted as to the specific deviation and its impact.

j. Fees and Charges. Lender's may charge the Veteran a construction fee of up to two percent of the amount of the loan for its services, provided that the majority portion (51 percent or more) of the loan proceeds are paid out by the lender during the actual progress of the construction, alteration, improvement, or repair. Such charges may be in addition to the one percent origination charge. If the portion of disbursed proceeds for services is less than 51 percent, a one percent or less construction fee is permissible in addition to the one percent origination charge.

(1) Fees charged on the loan guaranteed by VA must comply with the VA Lender's Handbook, 26-7, Chapter 8.

(2) The funding fee is due and payable to VA within 15 days of loan closing. It is not tied to the commencement or completion of construction.

(3) Loans must be reported to VA within 60 days of receipt of a clear VA final inspection report.

(4) In an alteration/repair purchase, for the purpose of reducing the funding fee, a down payment will only apply to the extent that the loan amount is based off of the lessor of the NOV or the acquisition cost.

(5) In an alteration/repair refinance, for the purpose of reducing the funding fee, equity will count only to the extent that the loan amount is less than the NOV.

k. Inspections. Improvements must be completed according to local building codes. The options allowable to satisfy the inspection requirement for cases ordered as r of the NOV or

(1) If the local authority performs the required inspections and issues a Certificate of Occupancy (CO) or equivalent, VA will accept the CO for the property as evidence of local authority inspections and satisfactory completion of construction. Loans for alteration and repair ordered as "Proposed" require local authority inspections according to the extent of the improvements and local requirements.

(2) If the local authority performs the required inspections, but does not issue a CO or equivalent, VA will accept copies of the inspection reports, which verify full compliance with local builder codes, or a written statement from the local authority that states that the required inspections were performed in a satisfactory manner.

(3) Final inspection: When the property is 100 percent complete, the lender will contact the original VA fee appraiser to complete the VA final repair inspection. If the original VA fee appraiser is not available, the lender will contact the RLC of jurisdiction for another VA appraiser to complete the VA final inspection. Note: The VA final inspection is to certify all VA MPRs have been met and the house was improved according to the original plans, specifications, approved change orders, and the as-completed value from the appraisal was maintained.

(4) It is the lender's responsibility to negotiate an inspection schedule with the builder or contractor, and it is the lender's responsibility to ensure it is followed.

l. Guaranty. The guaranty for alteration and repair loans will not be issued until a clear final inspection report has been completed by the VA fee appraiser.

Note: Contact the Government National Mortgage Association (GNMA) for pooling eligibility questions.

(1) If the improvements are not fully completed and loan proceeds are not fully disbursed, the guaranty will apply only to the proper pro rata part of the loan.

4. Rescission. This Circular is rescinded April 1, 2020.

By Direction of the Under Secretary for Benefits

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