Real Estate Mortgage

# Renovation loans get pandemic boost as homeowners want home offices

## The growing demand for FHA 203(k) by homebuyers and homeowners

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Vexed by work-from-home arrangements owing to the COVID-19 pandemic, homeowners are taking the long view and rethinking floor plans. The reality is, home offices are no longer a luxury.

In the initial three weeks of public health lockdowns in March, according to Gallup, the percentage of employed Americans working from home doubled to 62%. Of these workers, three in five said they'd prefer to work from home when restrictions are lifted. Homeowners are serious about dedicating room for work.

There's a mainstay in mortgage finance poised to help in working from home. The **Federal Housing Administration's** 203(k) rehabilitation mortgage insurance program is designed for borrowers to renovate when they purchase or refinance.

For over 40 years with Section 203(k) of the National Housing Act, FHA has been protecting lenders with fully-insured mortgage loans even as renovations are underway. In turn, the program opens access to much-needed renovation capital for borrowers.

As with any program, there are parameters, but this one isn't confined to repairs. It allows for actual home improvements to complement contemporary lifestyles. And these days, that means renovation choices brought on by the coronavirus and the remote economy.

"Since many people work from home – and plan to be home more now since COVID – I'm seeing both purchases and refinances with homebuyers and homeowners, who are planning projects to add more square footage to the existing structure of homes in their desired location, but not enough room to convert into space," said Patrice Watkins, vice president of Renovation Lending at **Guaranteed Rate**.

The FHA 203(k) presents two options for borrowers. The older, more well-known option is the Standard 203(k). As HUD literature describes it, the "Standard K" is FHA's primary program for rehabilitating owner-occupied residential properties.

"A new addition using the Standard K loan can go 'up' or 'out' from the current structure, and can involve removing walls or adding walls to accomplish the goal of the project," said Watkins, who is based in Atlanta, and is renovation-certified and licensed in eight states.

"These borrowers are bound to the Standard 203(k) loan," added Watkins. "Depending on the scope of work, these projects will require engineered blueprints or simple drawings with a detailed work write-up from an approved HUD 203(k) Consultant, so that appraisers know exact square footage, applicable amenities, and location of the addition, in order to value against recently-sold comparables in the area."

The second option, created by FHA in 2005, is known as the Limited 203(k). As it turns out, 15 years later during a pandemic haze and shifting economic landscape, the aptly nicknamed "Mini K" dovetails nicely with the scale of many projects that involve repurposing a room into a home office.

Under the Limited 203(k), a single mortgage through an FHA-approved lender allows homeowners to refinance and rehabilitate their existing home with up to $35,000 of proceeds going toward a pre-approved scope of renovation. Eligible expenses span the categories of minor remodeling, upgrades, and nonstructural interventions. The Mini K requires that the home remain habitable throughout the renovation. There is no minimum cost threshold.

"The Limited 203(k) is being used more in situations of converting currently unused space into livable space," Watkins said. "As long as the work doesn't include anything structural and the total renovation budget stays within $35,000," she said. "Homebuyers are able to convert, for example, garage space. Or finish basements. These projects are perfect for a household where multiple adults have job responsibilities that are now 100% remote, with school-age children also needing additional space for remote learning."

A senior HUD official added, "FHA's Limited 203(k) program remains a great option for homeowners to make home improvements for improved functions and modernization, where the rehabilitation costs are less than $35,000, or, if the home is in an Opportunity Zone, less than $50,000."

Last December, the FHA fine-tuned the Limited 203(k) to strategically twin with Qualified Opportunity Zones (QOZ), increasing the cap to $50,000 in total rehabilitation costs on owner-occupied, residential real estate located in the federally-designated zones. This expansion of the Limited 203(k) runs through Dec. 31, 2028, and is available for the first 15,000 mortgages secured by properties in QOZs per calendar year.

With the Limited 203(k), homeowners may address issues like space functionality, accessibility for disabilities, electrical system upgrades and outlet reconfigurations, energy conservation, central air, ceiling lighting, replacement doors, non-load-bearing partition walls, sound proofing, new flooring or carpet, built-in bookcases, window repairs for air circulation and natural light, and other long-term cosmetic comforts.

“A room conversion, adding or removing non-load-bearing walls, as long as it does not include anything structural, is a great project for a Limited 203(k),” said Ragen Cunningham, AVP, National Renovation/Construction Lending Division Manager at **Plaza Home Mortgage**. “Meanwhile, the Standard 203(k) is perfect for large, more involved projects, adding square footage, and structural work. Plaza is definitely seeing an uptick in borrower interest.”

“After the instantaneous pause with the pandemic,” Cunningham said, “it’s been interesting and very encouraging to watch renovation business begin to revitalize as we navigate the ‘new normal’.”

Based in Portland, Cunningham, an HW 2019 Insider, leads a team of regional renovation specialists. “People are home now more than ever and are seeing their homes in a new light. And that’s whether they’re taking advantage of the vibrant housing market to buy and remodel an existing home – or to refinance and reinvent the home they are living in now.”

More broadly, the 203(k) is recognized as an impactful resource for neighborhood appeal and community revitalization. By extension, the 203(k) advances opportunities for homeownership, thereby benefitting cities and counties nationwide.

“The 203(k) programs have been around and shown to be proven solutions for decades,” Cunningham reflected. “You can think of them as an FHA loan with three additional items: the contractor’s bid, contractor approval, and forms. This offers buyers an opportunity that other lending products don’t: low down payment, with funds to remodel and potentially to gain equity in their home. They’re definitely the right products for how we work and live today.”

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