



Renovation Review

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Contractor Screening & Validation

Contractor screening and validation are critical functions for any lender who is originating renovation loans to fully understand. It is imperative to put appropriate policies and procedures around these functions to ensure they are completed to both investor and agency guidelines and standards. The importance of ensuring that the contractor your borrowers have selected is qualified to complete the proposed project cannot be overstated. The benefits of doing this properly extend to all parties involved in the renovation loan transaction.

In this month's Renovation Review, we outline some of the requirements of each agency as well as the basic elements any screening process should include.

Before reviewing these elements, lenders should keep in mind that they are not "approving" a builder/contractor and are not lending any money directly to the builder but are looking to find the contractor either "acceptable" or "unacceptable" to participate in a renovation lending project with your borrower.

It is also worth noting that lenders should refrain from providing any "approved" contractor lists, and/or make recommendations on any contractor. The reality is: contractors are entering into a contract with your borrower and not the lender. Avoiding using the word "approved" could ultimately help your company avoid possible borrower claims that could make you liable for the contractor's performance.

At a minimum, your goal is to ensure that the contractor has satisfactory answers to the following questions:

- Does the contractor perform the intended repairs as a full-time job?
- Does the contractor have experience in completing projects of similar size, scope, and nature?
- Is the contractor properly licensed to perform the proposed repairs and, in the market where the work will be completed?
- Is the contractor properly insured per agency and investor requirements, and state law?
- Does the contractor have sufficient supplier references to ensure materials will be supplied for the proposed project?
- Do they have customer references that can be contacted to confirm the quality of their work and past customer satisfaction?
- Do the company/entity names match on all the contractor-related documents (For example: Licenses, insurances, W-9s, etc.)?

Planet Home Lending provides a comprehensive packet of forms, which we refer to as our “Contractor Toolkit” (which you can [access here](#).) It ensures these questions are asked and answered thoroughly. Additionally, we provide Contractor Screening Services through your Renovation Lending Account Managers in conjunction with our RenoStar Home Services Team, should that service be of interest to you.

**Does the contractor
have experience in
completing projects
of similar size,
scope, and nature?**

Requirements by Agency

FHA Standard 203(k)

According to HUD Handbook 4000.1, pg. 397, 6/29/2022 the FHA Standard 203(k) contractor requirements are:

"Prior to closing, the Mortgagee must ensure that a qualified general or specialized contractor has been hired and, by contract, has agreed to complete the work described in the Work Write-Up for the amount of the Cost Estimate and within the allotted time frame. To determine whether the contractor is qualified, the Mortgagee must review the contractor's credentials, work experience and client references, and ensure that the contractor meets all jurisdictional licensing and bonding requirements."

FHA Limited 203(k)

According to HUD Handbook 4000.1, pg. 400, 6/29/2022 the FHA Limited 203(k) contractor requirements are:

"The Mortgagee must review the contractors' credentials, work experience and client references and ensure that the contractors meet all jurisdictional licensing and bonding requirements. The Mortgagee must examine the work plan and the contractors' bids and determine if they fall within the usual and customary range for similar work."

View full handbook here:

https://www.hud.gov/program_offices/housing/sfh/handbook_4000-1

Fannie Mae HomeStyle®

According to Fannie Mae Selling Guide, pgs. 755-756, 12/14/2022 contractor requirements are:

"All renovation work must be performed by a licensed contractor or subcontractor, unless contractor licensing is not applicable under state or local law for the specific trade or type of renovations being performed. The borrower must choose the 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 may not choose the contractor or refer the borrower to any one specific contractor. However, the lender may require the borrower to obtain a completed Contractor Profile Report (Form 1202) from the contractor that is selected to ensure that the lender has sufficient information available to make a determination about the contractor's qualifications."

View full document here:

<https://singlefamily.fanniemae.com/media/33041/display>

Freddie Mac CHOICERenovation®

According to the Freddie Mac Single-Family Seller/servicer Guide, the contractor requirements for Freddie Mac CHOICERenovation® are:

“Unless otherwise noted below, all contractor(s) and/or tradespersons chosen by the Borrower to complete the renovations must:

- Have entered into an executed, binding renovation contract with the Borrower to complete the renovations within a reasonable time period after the Note Date, not to exceed 180 days or 365 days, as applicable. (See Section 4607.4(a) regarding the required completion date for CHOICERenovation® Mortgages.) The contract must include an indemnification provision requiring the contractor to indemnify the Borrower for any property loss or damage caused by the contractor, its employees or its subcontractors.*
- Be licensed and insured as required by local and/or State requirements, and*
- Be financially able to perform the duties necessary to complete the renovation work in a timely manner”*

Source: <https://guide.freddie.mac.com/app/guide/section/4607.10>

VA Alterations and Repairs Loan Program

According to VA Home Loans Builder Information, the contractor requirements for VA Home Loans are:

“Builders (contractors) are not approved by VA. They need only to register with VA to obtain a VA Builder ID number. Thus, there is no lengthy processing time and in most cases, an ID number can be issued within five (5) business days.”

Source: https://www.benefits.va.gov/HOMELOANS/appraiser_cv_builder_info.asp

To obtain our VA Contractor Toolkit, [click here](#).



As you can see, each agency varies slightly on this topic, but all have taken time to address this important step in the renovation lending process. By taking the time to put your own policies and procedures around contractor screening, you will not only be performing a great service for your borrowers, but also addressing an important risk mitigation function that could spare your company from financial or reputational risk.

The other benefit of having a solid contractor screening process is the future new business you may get from your borrowers upon successful completion of your project.

At the end of the day, if contractor validation and screening are done thoroughly and correctly, everyone wins. Hopefully, the time, effort, and energy invested in contractor validation will lead to happy customers and renovation loan business for your company. If you have any questions or comments, feel free to reach out to us at PHLCorrespondent@PlanetHomeLending.com.



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