Understanding the Construction Process

Introduction:

David Boye, Broker/Owner at Black Diamond Mortgage

david@blackdiamondmortgage.com

Zach Falk, Sales and Processing Manager at Black Diamond Mortgage

zach@blackdiamondmortgage.com

The 3 C's - Credit, Cash Flow (income), Collateral (appraisal)

The Why

- No Homes available
- Desire for a custom home
- Homes available are not what you want
- Cost of current homes on the market are too high
- Can build for less than purchasing
- I am a builder and can build my own home
- My family can build the home for me
- I already own land

What are the Benefits?

- You design the home
- All details are made up front

Luke 14: 28-30: 28 For which of you, desiring to build a tower, does not first sit down and count the cost, whether he has enough to complete it? 29 Otherwise, when he has laid a foundation and is not able to finish, all who see it begin to mock him, 30 saying, 'This man began to build and was not able to finish.'

What are the Features?

- All details are made up front
- Cost is actually higher than you think
- More down payment may be required
- Understanding the Costs associated with construction
- Length of Construction and how it impacts you

The Process (Using the Process Flow Charts)

- Contractor Approval
- Project Approval
- Budget Process
- Loan Approval and Closing
- Draw process

Types

- One Time Close (Favors VA, FHA, USDA)
- Renovation
- 2 Time Close
- Builder Spec (Favors VA, FHA, USDA)

Key Takeaways:

1) The more you put down / more equity you have, the more flexibility you are granted, the less administrative oversight and control required by the lender. But you can put as little as $0 down, as long as cost and design can be tightly controlled. A contingency is a required and important part of construction.

2) One time close loans are best for controlling the details for a limited down project to protect against a budget overrun. They do not cost less, and may cost more, as banks do not take unnecessary rate risk, and most 1xClose loans are refinanced in short order after construction (within 1-3 years) so the buyer/borrower rarely benefits from the rate protection or reduced number of closings.

3) Gaining bid or tight numbers on all line items of a construction project takes a lot of upfront work, but leads to the least overruns or stress during construction. All construction loans ultimately require this, but the low down payment, 1xClose loans require the most upfront due diligence, which is for the lender's protection, but can be considered the borrower's protection as well.

4) People should understand the basics of the plans and specs worksheets and receive them from Black Diamond asap, early in the process. As a company, we do not prefer 1xClose or 2xClose, but wish to help clients choose based on the features, and our income security comes from placing them in the best option and guiding them, leading to 1 or 2 closed loans over a couple years and a completed new home. Loan approval amounts are the most important details, and knowing those requires a great understanding of the entire and complete cost of the land+home+interim construction costs.

5) Construction loan costs are basically the same as a traditional loan, with the following exceptions:
- Interest during the course of construction, usually interest only, usually 6-12 months.
- Construction administration is usually paid as a fee or in an origination fee, but the lender will need to check on the project for draw approvals and home completion verification.
- Interest rates secured upfront for 12 months rarely benefit the consumer, so focusing on all other cost points is a better risk -reward decision.