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Theresa Springer's

Construction Loan FAQ's Reference Guide

Welcome to my Custom Construction Program. I have prepared this brochure to help answer your questions about the Custom Construction program and the service during the construction of your home. However, I still welcome your calls or emails if you have further questions even after the loan is closed.

Once your loan has closed the Lender's Construction Administration Group will be your contact point for service questions during the construction of your home.

Frequently Asked Questions

❖ How is interest calculated during the Construction Phase on the loan?

The interest payable during the Construction Phase is calculated on the loan amounts actually advanced. Interest will begin to accrue on the date of the first advance of loan proceeds. The first payment will be due on the first day of the month after closing.

❖ What are "Prepaid (Builder) Credits" and how do they affect my Draws?

Prepaid (Builder) Credits are basically the same as "cash". Where work has been completed and paid for prior to the loan closing, to the degree that the borrower has closing costs to pay, prepaid (builder) credits may be used to offset these closing costs.

For example, on a purchase construction transaction, a borrower must bring to closing \$25,000. This is known as the "Cash to Close". However; part of the construction costs included plans and permits totaling \$15,000, which the borrower has paid for prior to obtaining our construction loan. In this example, the bank may credit the borrower with the \$15,000 they have paid against the \$25,000 "Cash to Close". The borrower would then only have to provide \$10,000 (\$25,000 - \$15,000) "Cash to Close" amount. The construction funds are also reduced by this amount.

Three requirements must be fulfilled to receive Prepaid (Builder) Credits.

1. The work must be completed.
2. The work must be paid for, with receipt and canceled check as proof.
3. The item must appear as a budgeted line item on the Construction Cost Breakdown form.
4. The amount must not exceed the amount for the specific budgeted line item.

Prepaid (Builder Credits) will not be provided for "stockpiled" materials. Any materials must be installed or a part of the real estate. *Note:* In the case of a lumber package or log home package, credit is not given until the package arrives on site.

If the "Cash to Close" is less than the approved prepaid (builder) credits, only the amount needed to close the loan will be allowed as a Builder Credit at closing. The remaining amount of Prepaid (Builder) Credits will be disbursed on the first regular construction Draw. The first Draw request you submit will be decreased by the amount of (Prepaid) Builder Credits given at closing.

❖ **What is a “Draw?”**

“Construction Draws” are disbursements of funds. This is a withdrawal against the loan funds available for construction. Draw funds are to be used to immediately pay all unpaid bills for labor and materials on completed work and claims against the property.

❖ **What do I do to receive a Draw?**

Shortly after your loan has funded with the bank you will be sent a “Draw Request” form and welcome packet. It shows the amount budgeted for each portion of construction and how much is still available for disbursement. Work with your builder to estimate how much they need now, and complete the “Amount Requested” column. Both you and your builder must sign and date the request and then return the request to the lender.

❖ **What is the standard Draw process?**

An outside inspection company will visit your job site each month, usually between the first and fifth day of the month. They will fax to the lender their result of what the percentage of completion is by line item. The inspector will also take pictures of the work in progress that will be sent to the draw dept. with the original inspection report.

The inspection is compared to your Draw Request. If there are discrepancies, the Construction Admin Dept. will contact you to clear them up.

The bank will then issue a check for the approved Draw amount, and send the check to you, unless instructed otherwise. They will also include an updated copy of the Disbursement Record report and an updated Construction Draw request for your next use. Draw checks are normally issued by the 10th of each month.

❖ **How do I get money to pay for materials that I need to buy before they are installed?**

Normally, the Contractor will take care of most of the purchase cost of the materials. Contractors have relationships with suppliers where their terms allow them 30 to 60 days to pay for the materials.

However; in the case of an Owner / Builder, you will have to make your own arrangements with suppliers. You may need to have enough cash on hand or credit card purchasing power to acquire the materials. Draws are not approved for advance purchases.

❖ **How do I handle a request for a down payment on an invoice?**

Exceptions *may be* made for deposit requirements on high-end custom order materials, such as cabinets. Submit an invoice with your Draw Request, detailing the work, and down payment required. The bank may approve a Draw check (subject to normal reviews) for the down payment amount. The check may be made payable to you and the vendor, or at your request, the vendor only.

❖ **Do I have to submit receipts for each Draw Request?**

Typically no, as long as the inspection matches your request for funds, in case of discrepancy, the receipts may be asked for to clarify work done.

❖ **What if I spend more than the budget amount?**

You will be responsible for cost overruns. Your construction loan is set up to follow the Construction Cost Breakdown form that you and your Builder agreed to at the start of the construction project. This provides for enough construction funds to complete your house as agreed upon prior to your loan closing. During the construction phase, you may have some changes in building plans or type of materials. Additional costs associated with these changes or upgrades will have to be paid for by you, the customer, at the time they are

realized. No amount greater than shown on the Cost Breakdown form will be disbursed for any line item. Your contract with your builder should address this issue.

❖ **When can I access the Contingency Budget amount?**

If you have a line item in the cost break down for a contingency, the purpose of the Contingency is to set aside funds for unforeseeable cost overruns.

Under certain circumstances, a Contingency amount is required in your Construction Budget. A Contingency budget is required for all Owner/Builders. If required, the Contingency Budget amount is under the complete control of the Bank during the construction phase. Funds may be disbursed from the contingency budget on a case by case basis at the Bank's discretion, given its view of the overall project and costs, total disbursements will be limited to not exceed the overall percentage of completion of the house.

If at the end of the project, there are funds remaining, they can be used for documented upgrades or other additional hard costs. Any unused portion of the Contingency Budget will be credited to the original loan amount at Conversion.

If not required, you may have elected to have a contingency included in your construction budget. Elective contingency funds can be used for documented upgrades or other additional hard costs at the discretion of the borrower.

If the Borrower makes a principal reduction, the Borrower will have the choice to leave the Principal and Interest payment unchanged, or to recast (re-amortize) the payment over the life of the loan. If the Borrower requests a recast of the payments at conversion, a fee of \$250.00 will be charged. This is only available as long as the bank holds the loan in its servicing portfolio.

❖ **Who will the Draw Checks be made out to?**

The Draw check will be made out to both you and your Contractor. If you are requesting a down payment for an invoice, the check will be made payable to all three parties. The check will be mailed to your address, so that you can endorse it and then deliver it to the Contractor and/or supplier as payment. If you are an Owner/Builder, the Draw will be sent to you directly.

❖ **Can I get a second Draw check in the same month?**

An additional inspection and Draw can be ordered. There will be an additional Inspection charge. The dollar amount requested will be reduced by the inspections charge and it will be your responsibility to make up the difference.

❖ **Why was my Draw Request amount changed?**

The most common reason is that funds are requested for work that has not been completed. Draws can only be approved for actual work completed. No draws will be approved for items stored on site or not attached as part of the real estate.

Other reasons might include, but are not limited to, an error in addition, a request for more than the budgeted amount of a line item or, towards the end of construction, a request which would leave the remaining balance below the amount of the required holdback (5% of the hard costs or 10,000.00, whichever is greater).

❖ **Why do I receive a Billing Statement?**

You have chosen the option to be billed monthly for the unpaid accrued interest. You made this choice as part of the loan package. Interest begins to accrue on the closing date of the loan. For example if your loan funds on the 10th of the month, you will receive a billing statement on the first of the next month for interest due from the 20th through the end of the month.

❖ **What are the charges that appear on my first Billing Statements?**

These are the closing costs that occurred at escrow. Some of the disbursements reflect a combination of closing costs your settlement statement provided at escrow. Please refer to your Settlement Statement for details. These charges will only appear on the first Billing Statement.

❖ **Why does my Billing Statement say, "Due on the 1st" when I didn't even receive it until the 5th?**

Because of the nature of a construction loan, it is possible for the disbursed construction funds balance to change on any date through the end of the month. In order to calculate the interest for the full month, the statements are produced on the first business day of the following month. The statements as quickly as they can be in order to get them to you in a timely manner. Even though the contractual due date is the 1st of each month, please remember that there is a Grace Period of 15 days before Late Charges are applied.

❖ **I sold my existing home, can I make my construction loan amount smaller with the proceeds of the sale?**

Yes, this MUST be done prior to the final draw and inspection being requested. Call the bank and let them know that you are reducing the outstanding balance of the construction loan. They will instruct you on how to proceed and send the bank the large payment as a principle reduction.

❖ **What do I do different for my final Draw Request?**

Notify the bank and I when your Building Permit is signed off, the Appraiser will be contacted to perform a Final Inspection (Form 442).

The following items before required prior to approving the final Draw Request:

- Final Inspection Form 442, provided to us by the Appraiser
- Copy of the final sign-off on your Building Permit by the Building Department – or a Certificate of Occupancy
- Proof of completion of any conditions listed on your Commitment letter

❖ **What is a Construction Lien?**

A "Lien" is a claim for payment against your property. Under Washington and Oregon laws, those who work on your property or provide materials have a right to place a construction lien against your property. You have final responsibility for seeing that all bills are paid even if you have paid your contractor in full.

If you receive a notice to enforce a lien, take the notice seriously. Let your contractor know you have received the notice. Find out what arrangements are being made to pay the sender of the notice. Prior to making final payment on your project, make sure you or your contractor have a "Lien Release" form completed by each of the contractors and material suppliers.

If the bank receives notice of a lien against your property, they will place a "Hold" on your Draw file. Lenders will not disburse any Draws until the issue has been resolved.

Oregon customers

Special considerations and procedures apply to construction loans on properties located in Oregon; Borrowers/Builders will be required to close the loan with a Title Date-Down package at the expense of the borrower.

The Construction Loan:

Construction loans by their very nature are all unique. It takes a highly skilled and experienced construction loan officer to process a construction loan to closing. While communication between the customer and loan officer is important on every loan, on construction loans you will find much closer contact throughout the process. There is much more documentation required from you on a construction loan. Steps in the construction loan process have to be completed in sequence. Delays in getting documentation to me, your loan officer for a step in the process, will delay the final closing as well. I want to help make you aware of some normal processes on most construction loans, so we can work together to keep to your requested timelines for closing.

Construction Loans are approved differently than normal refinances or purchases. There are usually two major points when your loan is reviewed at the lender:

❖ **Initial Underwriting Review of the "Credit Package"**

The lender simply reviews your requested loan amount, payments, income, debt ratios, credit report, assets and other items pertaining to your financial situation and compares them to their guidelines. The lender may also review some preliminary general construction costs or scenarios. The lender does not review any construction related items for any type of final okay at this point in the process. This initial lender review is similar to a normal refinance or purchase transaction but with much more strict guidelines.

❖ **Final Underwriting & Construction Review of Construction Package**

The underwriter does a final review of the entire complete package. After underwriter review, the total application package is sent for Construction Review. Construction costs, materials description, plans, contracts, etc. are analyzed for industry norms. The appraisal is reviewed for accuracy and compliance to guidelines. Your builder goes through an approval process to be sure the lender is comfortable with your builder being able to complete the project as submitted. This Construction Review process is similar to the way mortgage loans were approved back 30-40 years ago and takes as long as it did then. You need to expect 5-7 business days for this process. It is normal to expect conditions or questions I need to send in to underwriting for review, 1-2 business days. Then the Loan Papers take 2-3 business days to complete and have to be sent to escrow. You sign the Loan Papers and escrow sends them overnight back to the lender for review. The loan closes and funds a day or two later. Closing and funding three weeks from the start of this point in the process is the normal timeframe on most construction loans.

❖ **You need to provide these items before I can order your appraisal:**

(Construction Appraisals take about 2 weeks to get back in a metro area and can take a bit longer in rural areas.)

- a. Architectural Plans (Full size)
- b. Site Plan (should be included in architectural plans)
- c. Construction Cost Breakdown
- d. Materials Description
- e. Purchase Agreement or Land Information if already owned
- f. Pre-Paid Item List

❖ **You need to provide these items before I can submit for Final Underwriting Review:**

- a. Sewer or Septic approval
- b. City Water access or Well Flow Test & Purity
- c. Pre-Paid Items Receipts & Proof Paid, if necessary
- d. Builder Fixed Price Contract or Owner/Builder Bids
- e. Permits Approved
- f. Lender Specific Construction Loan Forms
- g. Any Special Requests

- ❖ **New information obtained during the loan process may require more paperwork & delays.**
Examples of this include Builder Fixed Price Contracts that do not match Cost Breakdowns, changes to plans or materials, issues with the appraisal, City or County agency's last minute requirements, Builders that may not be approvable by the lender, underwriters asking for clarification on items in your file, and other items. I will work with you to overcome these situations as quickly and simply as we can. Many times, there are multiple ways to overcome them and we may pursue them all to see what works fastest.
- ❖ **Try to give yourself plenty of time for getting necessary documentation from others.**
Construction loans can be a time of excitement as well as high stress for customers. Many times you will be working with Builders who work with Sub-Contractors, Suppliers, Architects, City/County workers & inspectors, Sellers of land, Listing/Sales Realtors, Well Drillers, Septic Installers, Utility Companies and others. Frequently you will need to go back and forth between some of these people to get paperwork finished. Some are more helpful than others are in your requests for their assistance. While you need to keep things moving, allow for delays beyond your control.
- ❖ **Most Construction Loans have a Non-Conversion/Modification Fee.**
Most lenders write Construction or OTC loans so that they can have the final loan as well. The loan during the construction period (9 mos. is typical), has to be converted or modified to the final financing period (Remainder of 30 year loan, or 351 mos. is typical). If you do not do this most lenders charge a 1% fee of the original loan or current balance. They do not want you to refinance after construction is complete. See your loan papers for your exact dates & terms of your loan. I help you to get the final loan for your desired situation and avoid extra fees if possible.

