CONSTRUCTION LOAN GUIDE

A HELPFUL GUIDE WHEN BUILDING YOUR DREAM HOME

Are you planning on building your dream home or completing a renovation project? We understand these projects can be stressful, which is why we're here to help! Our construction loan programs are designed to provide you with the financial support you need to get the job done. Use this guide to help you decide which type of construction loan is best for you, learn steps to take to obtain a construction loan, learn construction terminology, and review a checklist of items you'll need to prepare before applying for a construction loan.

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Standard Construction Loan

This type of loan, often referred to as a standalone or two-time-close construction loan, is used to cover the cost of building a home before the homeowner obtains a separate, permanent mortgage. The loan duration is for the construction period only.

Once the home is finished, you would then have to apply for a permanent loan (a standard mortgage) to pay off the construction loan. This effectively means you are applying for two separate loans: one for the construction phase and one for long-term financing once the house is built. It is called a 'two-time-close' because you close on the loan twice: once for the construction loan, and again for the permanent mortgage.

PROGRAM DETAILS:
- Finance construction period with a fixed rate based on current rates
- Interest only monthly payments during construction period
- Refinance to permanent loan at the end of construction

BORROWER REQUIREMENTS:
- Owner-occupied residential properties only
- Release of construction funds by a title company after confirming work progress and clear property claims
- Customary fees related to construction loan paid by borrower
- Higher rate applied without an active Bank First checking

Construction-to-Permanent Loan

This type of loan, also known as a single-close or one-time-close loan, combines the construction loan and the permanent loan into one. This means you only have to apply and qualify for one loan, and you only have to pay closing costs once.

During the construction phase, the bank will disburse funds to the builder as the work progresses, and typically the borrower will make interest-only payments over this period. Once construction is complete, the loan is automatically converted into a regular mortgage. The interest rate for the permanent mortgage is typically locked in at the time of the loan agreement.

PROGRAM DETAILS:
- Finance into a fixed rate or adjustable rate mortgage
- Mortgage rates based off current rate sheet
- Loan rolls automatically into full repayment when construction is complete
- Release of construction funds by a title company after confirming work progress and clear property claims

BORROWER REQUIREMENTS:
- Owner-occupied residential properties only
- Customary fees related to construction loan paid by borrower
- Higher rate applied without an active Bank First checking

SUMMARY:

The main difference between the two is the number of times you need to apply for a loan and go through closing costs.

A standard construction loan requires two applications and two sets of closing costs, but it may give you more flexibility in terms of loan terms and interest rates.

A construction-to-permanent loan requires only one application and one set of closing costs, simplifying the process, but you'll have to accept the terms and rates in effect when you close the loan.

The best choice between the two will depend on your circumstances, including your financial situation, the current state of the mortgage market, and your construction timeline.

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Getting started

We're glad you've chosen to learn more about construction loans. Here's a handy step-by-step guide to obtaining a construction loan:

1. **EVALUATE YOUR FINANCIAL STATUS:**
   Before applying for any loan, it's crucial to understand your financial status. This includes understanding your credit score, income, debts, and overall financial health. Lenders will generally require a good credit score and a stable income to approve you for a construction loan.

2. **CHOOSE YOUR PLAN:**
   You will need a clear plan before applying for a construction loan. This should include choosing your desired property, a blueprint of the home, and a detailed plan of how you intend to carry out the construction.

3. **PREPARE A DETAILED BUDGET:**
   A thorough and detailed budget is essential. Your budget should outline all construction-related costs including labor, materials, contractor fees, permits, land costs, and a contingency for unexpected expenses. Lenders will want to see this to understand how the loan will be utilized.

4. **HIRE A QUALIFIED BUILDER:**
   Most lenders require that you work with a licensed and insured builder. If you plan to act as your own general contractor or build the home yourself, you may find it difficult to secure a construction loan.

5. **APPLY FOR THE LOAN:**
   Once you have all your necessary documents and plans in place, the next step is to apply for the construction loan. The lender will need to see detailed plans, a realistic budget, and your financial documents like bank statements, tax returns, proof of income, etc.

6. **LOAN PROCESSING:**
   Once the application is submitted, the loan processor will review your document and order an appraisal if necessary. The appraisal will determine the estimated value of your home once it's finished.

7. **UNDERWRITING:**
   The underwriter will review your application and either approve or deny your construction loan request based on your creditworthiness and the feasibility of your construction plans.

8. **LOAN CLOSING:**
   If your application is approved, you will proceed to closing. At closing, you'll sign all necessary paperwork and the construction loan will go into effect.

9. **CONSTRUCTION PHASE:**
   With the loan secured, construction can begin. The funds from the construction loan are usually dispersed in draws, or increments, as different stages of the construction project are completed.

10. **CONVERSION OR END LOAN:**
    Once construction is complete, you'll need to get an end loan to pay off the construction loan. This often is a standard mortgage. This stage will require another application and approval process if you've selected a standard construction loan.

Please remember, the requirements and processes may vary based on your individual circumstances. It's always recommended to consult with your relationship manager for personal guidance.

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Documents you'll need

Obtaining a construction loan means gathering some important papers. Let's break down what you'll need so your loan process can be smooth and straightforward. On this page, we'll outline the key documents you need in your toolkit when applying for a construction loan, setting you on a path for success from the get-go.

1. **PERSONAL FINANCIAL DOCUMENTS:**
   - Recent pay stubs
   - W-2 forms or other proof of income
   - Federal tax returns for the last two years
   - Recent bank statements
   - A list of all your assets and liabilities
   - Credit history and score

2. **DETAILED CONSTRUCTION PLAN:**
   - A blueprint of the home
   - A detailed plan for the construction project

3. **COMPREHENSIVE BUDGET:**
   - Detailed list of construction costs (including costs for labor, materials, etc.)
   - Cost of land
   - Any fees related to zoning or permits
   - Contingency funds for unforeseen costs

4. **CONTRACT WITH A QUALIFIED BUILDER:**
   - The builder's credentials, including license and insurance information
   - A signed construction contract detailing project timeline, costs, and other specifics

5. **VALUE OF LAND:**
   - Proof of ownership if you already own the land
   - The purchase agreement if you are buying the land
   - An appraisal or tax documents showing the value of the land

6. **PROOF OF INSURANCE:**
   - Proof of insurance on the construction project
   - Proof of liability insurance from your builder

7. **END LOAN INFORMATION:**
   - Details about your permanent mortgage (also known as the end loan)

Why choose Bank First?

When you choose Bank First for your home construction loan, you're tapping into more than just financial support; you're joining a community-oriented institution that understands local needs. Our quick pre-approval process gives you a head start, allowing you to embark on your construction journey with assurance and clarity. Additionally, our innovative banking platform embraces the digital age, offering you the convenience of effortless digital payments. With Bank First, it's not just about financing; it's about fostering a relationship built on trust, local expertise, and modern solutions for every construction dream.

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Terminology you'll need to know

Understanding construction loan terminology will be crucial as you navigate this process. Here are some important terms and their definitions:

1. **DRAW:**
   The partial disbursement of the total loan amount. The lender disburses the funds in "draws" as different stages of construction are completed.

2. **APPRAISAL:**
   A professional evaluation that estimates the value of your property. For construction loans, this is typically the estimated value of the completed home.

3. **CONTINGENCY RESERVE:**
   Funds set aside to cover unexpected costs during the construction process. Lenders often require a contingency reserve to handle overruns and unforeseen expenses.

4. **LIEN RELEASE:**
   A document stating that a contractor or supplier has been paid in full and waives their right to place a lien on your property.

5. **LIEN:**
   A legal claim on assets, like your home, for the payment of a debt. A contractor, subcontractor, or supplier can place a lien on your home if they are not paid.

6. **GENERAL CONTRACTOR:**
   A professional who manages a construction project. They oversee the day-to-day work, coordinate with subcontractors, and communicate with the client.

7. **INTEREST RESERVE:**
   A portion of the loan proceeds that is set aside to cover the interest payments during the construction phase.

8. **LOAN-TO-VALUE (LTV):**
   A ratio that compares the amount of your loan to the appraised value of the property. For example, if your loan is for $80,000 and the home is appraised at $100,000, the LTV is 80%.

9. **DEBT-TO-INCOME (DTI):**
   A ratio that compares your monthly debt payments to your gross monthly income. It helps lenders evaluate your ability to manage monthly payments and repay loans.

10. **CHANGE ORDER:**
    A change to the original construction contract. Change orders can affect the cost and timeline of your project.

Thank you for choosing Bank First as your trusted partner in bringing your construction dreams to life. We understand the intricacies and challenges of building something from the ground up, and that's why we've crafted this guide to simplify the process for you. If you have further questions or need assistance, don't hesitate to reach out to your relationship manager via phone, email, or by visiting one of our local branches. Your success is our commitment!

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