

Guidelines for Buying or Building a New Home

Families often spend endless hours talking and dreaming about the new home that they want to build. Many families search for home designs and floor plans that will meet their needs by looking at house plans published in new home booklets, other families tour homes presented on the Parade of Homes by the local association of builders. Families that have the financial means to do so, often meet with an architect to describe what they want in a home and the architect develops the plan. What is frequently lacking in the early stages of the planning is an understanding of how the players in the industry (developers, builders, real estate agents, and mortgage companies) function. Lack of this knowledge can be very costly and turn what should be an enjoyable experience into stressful times.

The following information and guidelines should help you avoid some of the major problems associated with building a new home or buying one that is under construction.

What Your Planning Should Include:

Your plan should include expectations for the following:

- Financial plan
- Description of needs and desires
- Lot requirements
- Role and selection of a real estate agent
- Architect/attorney need
- Selection of the builder
- Time Schedule
- Contract requirements
- Construction observation and/or inspections
- Final walk-through/home warranty review
- Closing.

While knowing what you are able to finance for the building of your new home is a necessary starting point; in most cases it would be best to start your planning by selecting a real estate agent. That is, if you will most likely build in a development which requires the builder to pay real estate commissions. If you plan to build in an area where a real estate company is not marketing acreage or lots the builder may not include the cost of the commission in the price of the home. If this is your first experience in having a home built for you and you can find an exclusive buyer agent who has considerable experience working with new construction contracts it would be

wise to employ the agent, even if you have to pay a fee for his service. The agent should then be involved with each step of the planning.

Selecting the Real Estate Agent

A search of the Yellow Pages should reveal brokers that work only as exclusive buyer agents. If your community does not have any exclusive buyer brokers, you should attempt to find a traditional agent that will work as a buyer's agent and meet the following standards.

Agent Standards:

1. Agent works only as an exclusive buyer agent (brokerage does not list property for sale) or an agent who is willing to exclude the option to change agency status to that of disclosed dual agent, designated agent, facilitator, or transaction broker.
2. Agent has experience as a supervisor or project superintendent in residential construction or has acquired the knowledge of a residential builder.
3. Agent can provide a minimum of ten references (former clients) that purchased new home construction. It would be preferred to have an agent who had worked with a minimum of five different builders in serving past clients. Discussion with references should reveal that the agent was competent with interviewing builders, development of the contract, coordination through project completion and assisting with the walk-through inspection.
4. Agent demonstrates good communication skills, has an ability to be candid and is trustworthy.
5. Agent and broker carry a sufficient level of errors and omission insurance.

An agent with the above experience should be able to assist you with each of the other elements of your plan. Your first task should be to determine your ability to qualify for a loan at a purchase price approximately 10% higher than your expected purchase price. Frequently buyers spend considerable more for new homes than they originally planned to spend.

Financial Plan

To determine your ability to qualify you should identify your gross monthly income. Your monthly income should include salary or wages, plus investment or other income. If you are self employed you will need to average the income reported after adjustments for expenses on your last two IRS reports.

The formula to determine your maximum PITI (principle, interest, tax and insurance) payment is:

1. Monthly gross Income x 28% = PITI with debt ratio adjustment if necessary.
2. Identify your debt obligations (those that extend beyond 10 months)
3. To determine your debt ratio: Monthly gross income x 36% = allowable debt ratio including the above PITI.
4. If the debt figure is greater than the 36% figure, the difference must be subtracted from the PITI amount.

Example: Family monthly income is \$7,200, Total monthly debt obligation for auto loans, student loan and credit cards is \$650.

1. $\$7,200 \times 28\% =$ PITI of \$2,016
2. $\$7,200 \times 36\% =$ allowed debt ratio of \$2,592
3. Adding \$650 to \$2,016 = \$2,666, this is \$74 above the allowed debt ratio, therefore \$74 is subtracted from the PITI of \$2,016 and the maximum PITI becomes \$1,942.

Assuming a monthly tax of \$300, insurance of \$60 and a principle and interest payment of \$1,582 buyers qualify for a 30 year conventional loan of \$226,000 @ a 7.5 % interest rate.

The above example assumes the buyers are putting a minimum of 20% down on the purchase. If the buyer is not able to put 20% down, a PMI payment will need to be considered in the above formula.

New Home Loan

The common practice is to have the builder finance the cost of the home while it is under construction with the buyers closing when the home is finished. When the builder finances the construction cost, the cost of financing will be included in the price of the home. The builder will purchase the lot and hold the title for the property until title is transferred at closing. When financing the construction cost, most builders will require non-refundable earnest money varying between 5-10% of the total purchase price. In order to have more control over the contractor and to save money on the cost of the home, buyers may want to consider getting a construction loan. This loan will allow you to lock in your interest rate and takes out the risk of the rate rising while you would be waiting 6-8 months to close on the home. Your interest rate will most likely be 2% or more lower than what the builder would pay for his financing. This alone would be a considerable saving on the project, approximately \$1,000 on a \$100,000 loan. There are other savings as the builder will also pay loan closing cost, which will range from \$1,500 to \$2,000. Getting a construction loan to finance the construction of the home could reduce the cost of the home by 2-3% and also give you more control of the project.

The greatest disadvantage of getting what is referred to as an end loan and closing on the home when the construction is complete, is that the payment of non-refundable earnest money is put at risk. You can seldom find the protection you would like for the return of your earnest money should the builder default on the contract, as most homebuilders are unable to purchase performance bonds to insure that the home will be completed. You might have \$10,000 to \$20,000 of non-refundable earnest money paid down on a property for which the builder holds title. With a builder defaulting on the contract that money might be held up in the courts for some time, thus financing the construction loan has merit.

Description of Needs and Desires

When planning your home you should determine what the basic needs are, these are all the elements that must be include in your home to meet your family needs. Next consider the desired features, the elements you would like to have which could be eliminated if the cost are above what you are willing to pay for the home. If you are concerned with the future resale value of the home, you should evaluate each up-grade you are putting in the home. You should ask your agent to assist you with this evaluation. If the up-grade is one that does not add to resale value, you must justify it as a worthwhile cost for the time you will plan to live in the home.

Basic Needs	Desired Features
Story & 1/2	
Foyer – separate space, not part of a room	oak or tile floor, ceiling 10 ft. or higher
Stairway- include a platform steps carpeted	stairway to basement open with a rail
Dining room— minimum 10 x 12 ft., carpet	12 x 14 ft., built in hutch, with glass, wall paper
Great room -- minimum 14 x 16 ft., fireplace, book shelves	16 x 18 ft. or larger, entertainment center cabinets
Kitchen – with breakfast area, oak floor, island, door to deck, adjacent to garage	hearth room, corian counter top, pantry

Utility room – on first floor	include cabinet and sink
Half bath – on first floor, insulated walls	wall paper
Master bed room – 14 x 16 ft. walk-in closet	16 x 18 ft., double door entry
Master bath – double vanity, exhaust fan, toilet room, shower	one vanity raised 4 inches, whirlpool tub, tile floor, skylight
Other bed rooms (3) minimum 12 x 12 ft.	12 x 14 ft., walk-in closets
Other bath rooms – (1)	(2) tile floor
Basement -- full, daylight, ¾ bath stubbed	walk-out, finished rec. room
Lot – 1/3 acre, cul-de-sac	½ acre or more, trees

Some buyers that are budget conscious may be tempted to make unwise decisions. Eliminating 200-300 square feet, which may be needed in 3-4 years as your family grows, to lower your monthly payment by \$150 may be an unwise decision. If your plan is to stay in the home 10-15 years your needs should be considered that far in advance. To ensure resale value of the home keep in mind what sells: location, curb appeal, open floor plans, large master bedrooms and low maintenance features.

House Style and Cost:

Most expensive to least expensive:

1. Ranch
2. Story & ½
3. Two story
4. Split level/tri-level
5. Front-to-back split level
6. Raised-ranch or bi-level

Floor Plan Deficiencies:

- walk through rooms to get to room
- kitchen sink visible from front door
- no entry area (enter directly into room)
- poor access from garage to kitchen
- poor access from kitchen to deck
- too little "wall for furniture placement"
- small secondary bedrooms
- carpeted walk ways

Lot Requirements

Lot selection is one of the most crucial decisions you will make. Always heed the statement "location, location, location." First, is the development in a good location? Next, is the lot location going to provide what you need for privacy, sunlight where most of the windows will be, and protect your children from traffic? Find out if homes that are more expensive are planned to be built around the lot you choose. You can increase the value of your home significantly if you build a smaller home on one of the more costly lots where other homes being built are costing \$75,000 to \$100,000 more than yours. If you want the home to appear massive be sure the home will set significantly above street level. Developments that include rolling terrain, curved streets, trees, and scenic views and walking paths add value to your property.

You will want to review the covenants and restrictions for the development, to determine if there are any restrictions that will prevent you from doing what you have planned. Most developments will have restrictions designed to protect the value of your property, often these will prohibit what you might want to do on the property

If you are in an area of the country where homes are built over basements you will want to observe whether rock has been removed in the digging of other basements or whether it may be necessary to remove many large trees. Both of these conditions will add significantly to your lot preparation cost and most frequently it is a cost that can only be determined after the contract is finalized. These are cost you will pay as a change order to your contract. Determine if the area where the home will set is undisturbed soil. If it appears that the home will set on fill dirt you should be concerned about the need for soil tests and possible additional cost for piers, or special footings.

A trip to the city planning office to study maps and to ask questions about the history of the land use may prevent future problems. You won't want to build over an area where a creek bed may have been rerouted or where environmental hazards may have been buried. You will want to know what is

planned for undeveloped land that is adjacent to your development and any future street and highway developments.

Selection of the Builder

In some developments, you may not have the option to bring in your own builder as the developer may have agreements with four or fewer builders. In these developments, if you like one of the model homes you will be limited to the builder of that model home. In other developments, your builder and house plan will need to be approved by the developer.

In most cases you will want to consider only builders that have been in the business for several years, who have established a fine reputation. Start your evaluation of builders by visiting their model homes to observe the quality of their work. Ask your agent to assist you with this process. If you are pleased with the quality of their work get a list of the people that the builder has built for. Asking them the following questions will give you additional criteria to use in selecting the builder.

1. Did the builder meet the closing schedule?
2. Was there good project management?
3. Were phone calls returned within the day?
4. What types of problems were experienced?
5. Was the home clean and ready for the final walk-through?
6. Was your list of corrections completed before you closed? If not, how long was it before they were completed?
7. Were any significant problems experienced within the first year of your ownership?
8. Were there any surprises with additional costs?
9. Would you have the builder build for you again?

An additional evaluation of the builder can be achieved by visiting the city building inspection office and reviewing the inspection reports of other homes the builder has completed. A lengthy list of corrections needed before approval may illustrate that there was poor supervision of sub contractors or little concern for quality. A call to the Better Business Bureau may reveal complaints made against the builder. In addition, you may want to go to the county court to check the records for court cases that may have been brought by former buyers. Even good builders may have some of the cases. Often what will be found in these searches are cases filed by sub contractors and vendors against the builder or cases filed by the builder against these parties. If you do find cases brought by a buyer you should find out all you can about the cases. If there is only one or a limited number over many

years, It is possible the builder may not have been at fault but had buyers with unrealistic expectations.

Time Schedule

The time required to build a home will vary according to the size of the home and the availability of the construction crews. Smaller homes may take 90-120 days while larger homes will typically take 180-240 days. If your builder has a company that employs all of the craftsmen rather than sub-contracting the work, the time period may be shorter. Once you start meeting with the builder it is quite common to spend a minimum of 30 days discussing your needs and arriving at a price on the home. After the home is under contract, it may take another 30 days for the builder to secure financing for the project and get approval from the city for the plan. These 60 days are not part of the days required to build the home. To meet the closing schedule the builder will assume that you will not delay the schedule by being late with the selection of paint colors, carpet, tile, appliances, light fixtures, plumbing fixtures, ceiling fans and other accessories. If the buyer makes many changes after the construction begins there may be an extended period of time to complete the project.

Contract Requirements

While the majority of the builders will have contracts documents which are universal among the local real estate industry other builders may have contracts documents which have been written by their own attorney. In either case you can expect these documents to be builder friendly and to protect the builder rather than you the buyer. The residential new construction sale contract should include:

1. Parties to the contract,
2. Real estate address, including plat and lot number,
3. Purchase price, including earnest money, loan and down-payment,
4. Closing and possession dates,
5. Addenda/entire contract: allowance addenda, plans, and specification addenda, covenants and restrictions addenda, financing addenda, contingency for sale of buyers home, warranties, and homes association declarations,
6. Commencement or continuation of construction,
7. Construction of home,
8. New home orientation/walk -through,
9. Language describing seller and buyers rights and responsibilities concerning:

Definitions	Deed
Estimated closing costs	Title insurance
Declarations	Prorations
Special assessments	Reassessments/clarification
Survey	Termite inspection
Delays, extension of closing	Plans and change orders
Allowances; adjustments/overages	Placement of improvements
Materials	Radon notice, disclaimer/inspection
Entire agreement, modifications	Escrow of incomplete items
Casualty loss	Utilities
Earnest monies/added deposits	Representations
Assignment/amendment	Notices
Defaults and remedies	Subsurface conditions

The law assumes that if you sign a contract, you have read the contract. Therefore, read the contract and ask the real estate agent questions on any part of the contract, which you don't understand. If you are uncertain whether you will want an attorney to review the contract, include a clause making the contract contingent upon review by an attorney with an opportunity to modify the language of the contract.

Excavation

Specifications

- excavate to undisturbed earth, all dirt to be used on lot.
- extra dirt required, removal of extra dirt and any additional expense incurred in rock or tree removal paid for by purchaser.

Foundation Specifications

pads -	according to plan,
footings -	16" x 8" concrete with ½" re-bars
walls -	8" concrete with ½" re-bars
columns -	2 1/2"
girders -	according to plan
damp-proofing -	sprayed asphalt
windows -	according to plan
floor -	4" concrete, with ½" re-bars over gravel
footing drain -	½" rock over drain tile, with sump pit

Additional cost because of poor ground conditions requiring piercing or floating footings to be paid by purchaser.

**Framing
Material**

Specifications

front elevation -	according to plan
plates-	# 2 & # 3 fir, or equal, plates on concrete to be treated material
floor joist-	#2 & #3 fir or equal - 16" o.c.
studs -	#2 & #3 fir 2" x 4 " or equal - 16" o.c.
ceiling joist -	#2 & #3 fir or equal - 16" o.c.
rafters -	#2 & #3 fir or equal - 24" o.c.
roof sheeting -	½" plywood for composition, 1"x4" for shakes
sub flooring -	¾" t.&g. glued and nailed
siding -	according to plan or model
facia and batten-	cedar
roofing material-	½" #1 shake shingles

Framing material, grade, size and spacing will meet city requirements.

**Masonry
Material**

Specifications

- Material - according to plan with elevation
- Allowance \$ _____ per square ft.
- Fireplaces - wood burning - 0- clearances
- Log lighter - gas

**Guttering and
Downspouts**

Specifications

- Guttering - aluminum 4" pre painted
- Downspouts - 2 #3 aluminum steel pre painted

Drywall Specifications

- Finished areas ½" sheetrock, taped, filled & finished
- Finished ceilings ½" sheetrock w/spray texture, painted per model allowance
- Garage ceilings taped and filled, not finished, spray texture
- Garage walls taped and filled, not finished

Decorating Specifications

Exterior siding	one coat primer, one coat latex
Interior walls	two coats, latex
Woodwork	stained & sealed or enameled
Wallpaper	trim and material allowance per contract
Paneling	time and material per model

Doors and Trim Specifications

Exterior front door	material allowance \$200
Exterior rear door	according to plan or model
Interior doors	per model
Trim	white pine or MDF
Garage doors	size 16 x 7 or two 8 x 7

Windows Specifications

Size and style according to plan

Insulation	Area To Insulate	Insulation Type	Thickness	R-Value
	Exterior walls	Fiberglass batt	3 1/2	13
	Flat ceilings	Fiberglass blow	11	30
	Vaulted ceilings	Fiberglass batt	6	19

Garage cold walls	Fiberglass batt	3 1/2	13
Garage ceiling	Fiberglass batt	6	19
Rim Joist	Fiberglass batt	3 1/2	13

Air chutes

Foam

**Finished
flooring**

Specifications

Kitchen	Hardwood
Entry Hall	Hardwood
Family room	carpet
Living & dining	carpet
Master bedroom	carpet
Other bedrooms	carpet
Bedroom halls	carpet
Stairs (excluding basement)	carpet
Bathrooms	vinyl
Utility rooms & other areas	vinyl

Allowances

Carpet with pad	\$_____yd
Oak flooring, time/material	\$ _____sq. ft.

Vinyl \$ _____
yd

Ceramic Tile

vanity tops Marbelite

shower Tile 6 ft over base

tub tile enclosure

master tub \$ _____

Walks and Drives

Walks 3 ft wide 4" thick

Drives 4" thick concrete

Landscaping

Finish grade standard size lot
allowance

Blue grass sod \$1,200 includes fine
grade time

You will want to review the specifications to ensure that they cover all the signification details for the construction. It is important to have all the allowance be very specific. The following example is ambiguous:

Sod ----- entire lot----- \$3,500.

If it cost the builder more than \$3,500 to sod the entire lot, who pays?

The greatest risk you will have with the contract is with the builder's demand for a significant sum to be paid at the signing of the contract as non-refundable earnest money. It is quite normal for this request to be 5-10% of the contract price. It is recommended that you negotiate this sum to the smallest payment possible and that it be paid at various stages of construction. Before making this payment of nonrefundable money you will want a loan approval commitment from a bank or mortgage company. You will also want to be sure that you will not desire to back out of this contract. In addition, it would be best not to consider upgrade changes after the contract has been signed and the non-refundable payment made, as the contractor will be able to charge inflated cost for the changes. Some contractors charge an administrative fee for all change orders. Therefore,

have all the decisions regarding the home made before you sign the contract.

Construction Observations/Inspections/Final Walk-Through

Someone should take the responsibility of observing the construction as the project progresses through the various stages. You may want to consider hiring a structural engineer to review the progress through the framing stage. Another option is to employ an inspector, with considerable experience in new home construction, to inspect the home. These inspections are usually done on the following schedule when:

- the forms are in place for the footings to be poured

- the foundation walls have been poured, waterproofed and the drainage tile in place

- the home is roughed in (framing complete with roof sheeting) the framing should be checked to ensure that the framing meets the industry standards

- the electrical work should be observed before the insulation is placed on the exterior walls

- the insulation job and foaming, if used, should be observed before the contractor installs the sheet rock

If an inspector is used their service will generally include the final walk-through inspection.

Contractors are notorious for leaving a considerable amount of work remaining for the last few days before closing. Before you do the walk - through, you should request that the home be thoroughly cleaned with windows washed and walls wiped free of dust. The painter should have made noticeable touch-ups before your walk-through. The walk-through should begin in the bedrooms and proceed in a pattern so that no part of the home is missed. You will want to:

1. try all plumbing
2. open and shut doors and windows
3. look at walls and ceilings for damage and paint flaws
4. check all trim for damage which will need repair
5. open and observe all cabinet doors and drawers
6. check carpet for poor installation (inferior seams)
7. check hard wood floors for defects
8. check appliances for correct operation
9. check all lights and outlets
10. make sure the heating and cooling systems are operational
11. check the basement foundation and floor for cracks
12. on the exterior of the home check all walls, roof and trim for damage and proper painting or finish

13. check the finish excavation of the lot to ensure proper drainage away from the home

Closing on the Home

Prior to closing on the home you should secure a title insurance policy. The builder, at his cost often provides this policy. In most communities the Mortgage Company will require you to purchase a policy, at your cost to protect their investment. You may need an attorney to review the policy to make certain that the insurance policy does not exempt conditions that would put a cloud on your title. An example might be a survey that showed that the home was built over one of the setback lines or that the home was built over an easement. You will want to be sure that you get protection from mechanic and material liens.

If weather conditions do not permit all outside work to be completed, it is common to escrow money for the remaining work. The escrow is usually at one and a half times the cost of the work. Most builders will want you to close as soon as they can get an occupancy permit. While you might be tempted to close leaving an extensive list of items found on the final walk-through, it is better to get these task completed before you close. If you depend on the work being completed after you close, the builder is not as apt to put pressure on his sub-contractors as he has already been paid.



About the Author, Donald J. Welsh, Ed.D.

Dr. Welsh, a training consultant, National Lecturer for Nova University, and a former college administrator, has devoted his career to the development of people in diverse stages of their lives. His leadership has been instrumental in the development of many nontraditional programs that have served unique community needs. He has always been motivated by the challenge of a change agent role.

In his early development as a craftsman in residential home building and a vocational woodworking instruction, Dr. Welsh was a student of design and technology changes in the housing industry. Later in a mid-career change, he expanded that interest into the real estate industry as a real estate salesman and investor. Dr. Welsh has been a licensed real estate salesman and broker since the late 70's. In 1991, after extensive research on changes in the industry, Dr. Welsh established a buyer agency real estate brokerage.

Conditioned to follow the "Golden Rule" throughout his growth and career, Dr. Welsh soon learned that these values were not practiced by many of the professionals involved in the industry as changes were being made to provide home buyers agency representation. The failure to communicate

changes even extended to newspaper editors, television program directors, corporate relocation managers and personnel directors. At each of these levels, the fear of losing business and or personal favors extended by those in the industry seemed to prevail over the duty to inform their constituents of the changes in the real estate industry.