

# Inspect Yourself

Your clients — and lenders — can benefit from hiring third-party inspections for their construction projects

By **Diana Clark**, vice president and chief financial officer, Construction Inspection Specialists

**T**HE USE OF UNBIASED, THIRD-party inspectors has become vital to construction lenders, as well as to developers. Audits from independent companies can provide an invaluable component to the funding process — a checks-and-balance system for construction projects.

These progress inspections are not intended to replace regulatory inspections. Rather, they provide an objective opinion through the inspector's knowledge of the construction process and experience in the field. Additionally, using qualified third-party inspectors offers lenders another opportunity to analyze projects in an effort to help keep each one on schedule and within budget.

With the construction climate's dramatic changes in the past few months, it is now extremely important to help ensure that your clients' construction projects stay on track. Brokers who understand what these inspectors do and how to help developer clients get their projects ready for inspection can better help their clients and lenders.

## Getting the project ready

Before a lender agrees to fund a construction project, it will review and analyze all plans and budget documents to verify completeness and quantification amounts. To expedite the process, your clients should perform a complete cost analysis.

Numerous companies are available to perform these cost reviews and to provide qualified costs for each market. These reviews can range from cursory to in-depth, depending on the scope of the job and the comfort level between the lender, broker and borrower.

The items needed to start a cost review might include a full set of plans, any signed contracts or bids, complete project specifications, a schedule of materials, and a complete budget for the project. Any additional items that your client can provide will add to the cost review's thoroughness.

A couple of typical results of these reviews include cases where necessary line items were not included in the budget and rate increases for products that were not factored at current levels, such as when the costs of copper or asphalt skyrocketed because of economic changes or when labor costs are established by friends donating time to help out and not by market rates.

If these things are discovered before the lender agrees to finance a deal, your client can benefit from adjusting the budget documents accordingly.

## The inspection phase

When the lender agrees to finance your client's construction project, the inspection phase begins. It goes from groundbreaking through to the certificate-of-occupancy issuance. The more information the inspection company receives at the onset, the more closely it can monitor the project.

Each lender has a different way of processing its loan-draw applications, and each borrower has specific loan-draw needs. Typically, borrowers submit their request to the lender, which processes it and forwards it to the inspection company, which in turn gives the field inspector a complete checklist to take onsite. The inspector's duty is to verify the progress-to-date against the application submitted.

Inspectors should address any problems and clear up any discrepancies with the onsite project superintendent. They also will discuss any pending issues that should be documented for the lender. With each inspection, the inspector is trained to not only monitor the completion of the items in the pay application but also to review and compare the remaining work with the remaining budget. During construction, inspectors also will photograph all areas of progress and note any areas of noncompliance. They will notify the lender immediately of any significant line-item discrepancies.

For the property-owner's and lender's benefit, all appropriate lien-waiver releases may also accompany each draw request. Although lien-waiver processing is typically done through the lender, the inspection company or inspector could provide a better monitoring system as they are more familiar with the project's progression. Stored materials must be duly noted and handled in accordance with the lender's practices. Some lenders pay off invoices immediately; others pay when materials are onsite; and others pay only when the materials are installed.

Change orders are typically handled at the site level between the owner and the contractor. Your clients should include any change-order documents pertaining to the project with the draw-request submission. This will keep the inspector apprised of any changes to the original scope of work and help make sure that the change order is in fact completed.

Inspectors should craft a complete written report that documents the observations and recommendations from each site visit. The report should include all pertinent site information, such as the lender, borrower, site address, etc.; inspection date and time; results of the inspection while onsite; and photographs documenting the findings. In the event of a dispute, these third-party inspection reports could be invaluable.

When the lender takes a property as collateral for a project to move forward, it presumes that it may have to take that property as repay-



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ment on the debt. As such, it is essential that the inspection company keep the lender apprised of actual levels of completion so the loan doesn't become upside-down.

When your client submits the final pay application and the lender requests the final inspection, the inspector must spend ample time on the site. The resulting report and photos should document completion of all budgeted items or reflect the level of completion of any items that are not completed accurately. It also should clearly document any discrepancies with photos. Once the project is confirmed to be 100-percent complete, a certificate of occupancy is issued.

### Overall benefits

An inspection company's thoroughness and competence allows it to provide an assessment of the job at hand as well as an overall perspective of the entire project. Inspection companies and their inspectors should have no personal or financial interest in the project. They must demonstrate honesty, integrity and a sense of fairness.

Third-party inspections also can be more cost-effective for clients and lenders in the long run. Using a qualified, third-party inspection company throughout the construction process offers peace of mind for the owner and the lender. **■**