

# Success by Design

THE DECISION TO RENOVATE IS A BIG ONE. SAVVY INVESTORS UNDERSTAND THE BEHAVIORS THAT ARE ESSENTIAL TO A WINNING CONSTRUCTION PROJECT.

by Kelly Edwards and Chris Edwards

**I**n his best seller, “The 7 Habits of Highly Effective People,” Stephen Covey provides seven concepts to guide the reader toward self-mastery and business success. The general theme of the book is that, in order to achieve success in one’s life, certain habits should be implemented. A successful life can be built by design.

In the world of investment real estate, as in life, winning doesn’t just “happen.” Choices must be made—early and often—to ensure that one’s investment will be profitable. The decision to purchase a property that requires a substantial amount of rehab work is a big one. Some get it right, some do not. The good news, for investors, is that there is a success “road map.”

Let’s take a look at seven habits that savvy investors can employ when rehabbing investment properties.

## 1 BEGIN WITH THE END IN MIND

Have you ever purchased a property and thought to yourself, “Worst case scenario, I’ll just rent it for a while”? Caution! Buyer beware—of yourself! Savvy investors have a plan and adhere to it as strictly as possible. As an investor, you should be cognizant that market conditions change from time to time, and you need to have a clearly defined rehab goal to help navigate the uncertainties of the real estate market. Ask yourself this question: “What is the purpose of the project—rehab to rent or rehab to flip?” This question should be answered before the first dollar is spent.

## 2 ESTIMATE CONSERVATIVELY

A number of methods can be used to estimate rehab costs, with some being more accurate than others. It’s not uncommon for new investors to “estimate” a project’s cost by simply going room to room creating a list of items that may require work. This method works well for newbies because it’s easy to categorize the costs on a “per room” basis.

Another investor may feel comfortable using a per-square-foot calculation as a gauge for estimated renovation cost. This method, while more of an average and often less accurate, should be used by more experienced rehabbers. Such investors

have a firm grasp of their real estate market, subject properties, comparable sales and the local economic climate.

When using a per-square-foot method, it’s wise to have a solid understanding of your contractor team and associated costs. Our team utilizes a very detailed estimating process whereby each work component is categorized by construction cost code, or line item. This method is the most time-consuming but also the most conservative, as it guarantees a more accurate and detailed rehab estimate. Remember, the estimating process doesn’t just include the proposed “material” numbers. Contractor labor estimates must be accounted for before a total project budget can be finalized.

## 3 CREATE A SCOPE OF WORK (SOW)

The scope of work (SOW), sometimes referred to as the statement of work, is essentially the “road map” for your project. It’s arguably the single most important component of your renovation plan. The SOW outlines, for your contractors, the specific tasks that are to be completed to ensure a successful project.

Developing the knowledge of a renovation project and its processes can take time and, therefore, the ability to generate a quality SOW is typically reserved for experienced real estate investors. New investors should work closely with their general contractor to gain such knowledge.

The length and level of detail of the scope of work will vary by each investor, the project and work required, and the contractor team. Our team prefers to include enough detail to clearly state the work rules, requirements and expectations, but generally strives to keep the length of the SOW to one page (and no more than two pages) per contractor trade, where possible. It’s important to note that the SOW should be included in the contractor agreement and should be signed by the contractor.

## 4 BUILD A PROJECT BUDGET

New investors sometimes confuse the estimate with the project budget. Contractor estimates, when fine tuned and finalized, are used to create the rehab budget. Be sure to account



for both material and labor estimates (also known as “bids”) when creating the project budget. Astute rehabbers add in a surprise or “fudge factor” line item, worth maybe 10 percent, to account for unforeseen or miscellaneous line items in an effort to remain conservative in the budgeting process.

## 5 HIRE SLOW AND FIRE FAST

You’ve closed on the property and developed a project scope, estimate and budget. Now it’s time to begin the contractor hiring process. Contractor relationships, much like other relationships, must be a good “fit” for long-term success. For this reason, our philosophy is “hire slow, fire fast.”

Experienced real estate investors understand that building a solid contractor team takes time and the players will likely change over the years. It’s common to be anxious to begin the project, especially with your personal investment capital on the line, and feel the need to forego the necessary due diligence when interviewing each contractor.

Take the time to thoroughly discuss the requirements and expectations of the project with the contractor. The more project detail the investor provides during the interview process, the better. If, during the life of the project, it’s evident that a contractor relationship has reached a breaking point, it’s often best to move quickly and decisively to find a replacement. Doing so will save the investor time (schedule) and money (budget).

## 6 MAINTAIN A SCHEDULE

Successful rehab projects will follow a strict and predetermined schedule or workflow. Contractors often prefer to perform their work in a certain order as some trades cannot begin until others finish their respective scope of the project. A negligent contractor can easily derail a rehab effort, causing delays to other contractors, which may subsequently impact the real estate investor’s rehab profit.

For the newbie investor, setting and maintaining the project schedule is one of the greatest challenges. Consistent communication and coordination with the contractor team is key.

## 7 IT’S A CONTRACT FOR A REASON

“If it’s not in writing, it didn’t happen.” This popular adage holds true in most business transactions, but is especially critical in the rehab and construction environment. It’s difficult to hold a contractor accountable to the specific trade’s scope of work, budget and schedule if these items aren’t referenced and mutually agreed upon within some type of formal written agreement.

Our company uses an independent contractor agreement that states, among other things, that the contractor is working independently of our company and, as such, is not an employee. The agreement outlines the relationship between the investor and contractor in detail. The agreement also defines other administrative requirements such as proof of the contractor’s commercial general liability insurance and workmen’s comp insurance (COI).

Additional critical items that should be referenced in the agreement are the project start and end dates, payment schedules, change order process, financial penalties, permits and inspections, working hours and other jobsite policies and expectations aimed toward ensuring a winning rehab project.

The choice to purchase and rehab properties can be a daunting decision, but it doesn’t have to be. Judicious investors should utilize these seven habits to ensure success in their next renovation project. •



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