

CONTROLLING HOME CONSTRUCTION COSTS



In the flush of excitement from watching your dream home become a reality, it can be all too easy to increase the price tag without really noticing. Seemingly small changes can have a big impact on costs, though, and in most cases the homeowner will need to foot the bill come closing time for any overages above the agreed-upon loan amount.

“Early in your construction loan journey, you’ll finalize building plans and get a cost estimate from a contractor, required steps for securing a construction loan. Based on this estimated value, and once approved, the lender offers a loan up to 85% of the appraised value for a contractor-build project, or up to 75% for an owner- or self-build project,” says Jody Smith.

The estimated value of the home is based on specifications given at that point. For example, the contractor may have estimated for laminate countertops, or a certain style of window, or standard paint finishes. Certainly, the contractor is planning to build according to the blueprints. Any changes to

these plans add costs – either direct costs for higher-end finishes, for example, or labor costs for changing plans or redoing work. Moving a wall, expanding a porch, upgrading to hardwood floors all increase cost overruns noticeably, but smaller changes to things like faucets and cabinet pulls can add up, too.

Sometimes, cost overruns aren’t a matter of the homeowner’s choices. In the 2020-2022 timeframe, for example, lumber costs skyrocketed, so early construction estimates may fall woefully short when it comes time to actually purchase materials. Carolina Farm Credit recommends that customers building homes keep a reserve of 5% of the original estimated build cost. We also suggest that homeowners stay in daily contact with their builder to stay on top of the budget, and visit the site daily to make sure no costly mistakes are being made, another source of unexpected cost overruns.

“Like most mortgages, construction loans are typically written at a maximum loan-to-value ratio. If you’ve borrowed up to that limit in your initial construction loan, any cost overruns will have to come out of your pocket. If you haven’t borrowed the full amount you qualified for, you may have an option to secure a separate loan to cover the difference,” said Jody.

Progressing through the months of your new home build is an exciting time and it’s easy for emotions to start driving decisions. Consider carefully, though, before straying too far from your budget, or be prepared to write a check to your contractor when the work is done.

Jody Smith
Regional Lending Manager, Carolina Farm Credit

