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Seller Financing Under The Dodd-Frank Wall Street Reform And Consumer Protection Act

By David Hamerslough

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In July 2010, the Dodd-Frank Wall Street Reform And Consumer Protection Act ("Dodd-Frank") was signed into law. This law was designed to address, among other things, some of the lending practices alleged to have caused or contributed to the economic downturn.

One of the issues Dodd-Frank raised regarding residential real estate was the new law's application to seller financing of residential properties. The federal Consumer Financial Protection Bureau ("CFPB") has now published regulations covering this subject matter.

Starting January 10, 2014, a seller who finances the purchase of residential property containing one to four units may be considered a "loan originator" and therefore required to comply with truth-in-lending ("TLA") disclosures. (Seller financing of residential property containing five or more units, vacant land, or commercial properties are not subject to the TLA disclosures.) If you are unfamiliar with TLA disclosures, you should consult a lawyer or other qualified individual with that knowledge and expertise.

CFPB established two exemptions from these disclosure requirements. These exemptions will probably apply to most of the seller financing taking place in our geographic area.

The exemptions turn on several factors. One is the number of residential property transactions financed by the seller in a 12-month period, the capacity of the seller, whether the seller constructed the property, and the terms of the loan.

The regulations provide that natural person, estate, or trust that meets all of the following criteria is not a loan originator if

- the natural person, estate, or trust provides seller financing for the sale of only one property in any 12-month period to purchasers of such property, which is owned by the natural person, estate, or trust and serves as security for the financing;
- the natural person, estate, or trust has not constructed, or acted as a contractor for the construction of, a residence on the property in the ordinary course of business of the person;
- the natural person, estate, or trust provides seller financing that meets the following requirements:
 - a. the financing has a repayment schedule that does not result in negative amortization; and
 - b. the financing has a fixed rate or an adjustable rate that is adjustable after five or more years, subject to reasonable annual and lifetime limitations on interest rate increase. If the financing agreement has an adjustable rate, the rate is determined by the addition of a margin to an index rate and is subject to reasonable rate adjustment limitations. The index the adjustable rate is based on is a widely available index such as indices for U.S. Treasury securities or LIBOR.

Alternatively, the regulations provide that a natural person or organization, such as a corporation, limited liability company (LLC), partnership, trust, estate, etc., is not a loan originator if

- the individual or entity providing seller financing for the sale of three or fewer properties in any 12-month period to purchasers of such properties, each of which is owned by the person and serves as security for the financing;
- The individual or entity has not constructed, or acted as a contractor for the construction of, a residence on the property in the ordinary course of business of the person;
- The person provides seller financing that meets the following requirements:
 - a. the financing is fully amortizing;
 - b. the financing is one that the person determines in good faith the consumer has a reasonable ability to repay; and
 - c. the financing has a fixed rate or an adjustable rate that is adjustable after five or more years, subject to reasonable annual and lifetime limitations on interest rate increase. If the financing agreement has an adjustable rate, the rate is determined by the addition of a margin to an index rate and is subject to reasonable rate adjustment limitations. The index the adjustable rate is based on is a widely available index such as indices for U.S. Treasury securities or LIBOR.

Even if these exemptions apply, California law still requires that a seller providing financing for a residential property of one to four units must use a seller financing addendum. With seller financing, the focus is usually on the terms of the financing, the credit-worthiness of the buyer, the impact of any senior loans, and the seller's ability to carry those senior loans and other costs associated with the property in the event of a default.

What sellers often still forget to do, however, is request a copy of a Notice of Default and a Request for

Notice of Delinquency. With respect to the latter notice, the seller should check with any senior lien-holder to verify that they will honor such a request. Sellers should also consider retaining a tax service to ensure that property taxes are being paid, and they should consider obtaining title insurance as a lender and be included as an additional named insured on any homeowners' insurance or other insurance coverage.

Sellers should also remember that any notices they are entitled to receive as a result of any of these requests or other services will go to the address provided by the seller at the time the notices or obligations are set up. If a seller's address changes, then the seller should record an appropriate notice reflecting the new address and/or provide written notice of that change of address to any appropriate individual or entity.



Laurie and I had two very challenging real estate rights issues that we were advised were going to be difficult to prevail on. The RHRC team engaged with us and helped us understand our rights and prevailing position. RHRC were thoughtful advocates for us from the beginning to conclusion of our cases. We feel fortunate to know we will always be able to call on the firm in the future and that they are our legal counsel.

Albert "Rocky" and Laurie Pimental, President of Global Markets and Customers, Seagate Technology

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